HOOK
LAW CENTER
SPECIAL REPORT

Financial Planning

This Special Report is brought to you by

HOOK LAW CENTER
Legal Power for Seniors

Tel: 757-399-7506
Fax: 757-397-1267

Locations:

Virginia Beach
295 Bendix Road, Suite 170
Virginia Beach, VA 23452

Suffolk
5806 Harbour View Blvd.
Suite 203
Suffolk, VA 23435

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America is aging. From 2005 to 2020, the population of those age 65 or older, and the population of those age 85 or older will increase by almost one-half (48% and 43% respectively), and the youngest seniors, age 65 to 74, will increase by 70%. The growth of the over age 65 population is due to the baby boomers aging, but the growth of the 85+ seniors is largely due to increased longevity. The Center for Retirement Research at Boston College estimates that 60% of older workers are at risk of being unable to maintain their standard of living in retirement. As people live longer in retirement good financial planning both before retirement and post retirement becomes more important than ever to accomplish their objectives. Frequently, these objectives include:

- Obtaining and paying for appropriate medical and long-term care
- Avoiding running out of money during your lifetime while maintaining an appropriate standard of living
- Preserving your autonomy
- Remaining in your home or obtaining other appropriate living arrangements
- Leaving a legacy to your spouse, children or other beneficiary

Long-term Care Planning

As you age, the probability that you will need long-term care increases. After age 65, an American has more than a 70% chance of needing some form of long-term care.

What is long-term care? It includes a variety of services and supports to meet health or personal care needs over an extended period of time. Long-term care is intended to maintain health status while acute care aims to improve or correct a medical condition.

How much care will be needed? On average a person 65+ will need some long-term care for three years. Twenty percent (20%) of persons 65+ will need long-term care for over five years. Women need care longer (on average 3.7 years) than men (on average 2.2 years).

Who are the providers of long-term care?

Family caregivers provide the most care. Obtaining care from family caregivers, however, is not cost or stress free. Frequently, the caregiver loses wages, pension benefits, or Social Security benefits. In some cases, the family must supplement the senior's income. Children can be required by court order to provide support to their parents who are in necessitous circumstances. Additionally, the caregiver will frequently incur stress trying to assist their family member while fulfilling their other family, personal and business obligations. In some cases, it will cause disagreements among children when one child perceives he or she is doing more than others, one child perceives that another has more "power" or when only one child is receiving compensation for providing services. Children who assist their parents are frequently referred to as the Sandwich Generation, since they are providing care for their parents, supporting themselves, and assisting their children. Appropriate planning is very important when using family caregivers.

Homecare services provide home health aides or licensed nurses to assist a senior remain in his or her home. These services cost on average $19 per hour (2010) for home health aides from a licensed agency. Some clients prefer to employ home health aides directly at a lower hourly cost. This perceived savings, however, may evaporate as they comply with relevant employment and tax laws. If you directly employ a home health aides, the terms of the agreement should be committed to writing and signed. When you directly employ a home health aide, Hook Law Center can help you prepare the employment agreement and comply with the relevant laws.

Adult day care centers provide part-time care in a group setting. Most centers operate 10 - 12 hours per day and provide meals, social/recreational outings, and general supervision. Adult day care centers operate under a social model and/or a health care model. The average cost is about $60 per day (2010).

Assisted living facilities (ALF) provide assistance with the activities in a community setting. The cost of ALFs vary, but on average cost $3,185 per month (2010).

Continuing Care Retirement Communities (CCRC) provide several levels of care, independent living, assisted living and nursing care, in one location. Frequently, the resident must enter the CCRC able to live in the independent living unit. As the resident requires more care, he or she moves to the appropriate unit. Typically a CCRC charge a one-time entrance fee (frequently several hundred thousand dollars which may or may not be refundable) and a monthly fee.

Nursing homes offer a wide range of services, including 24-hour per day nursing care. Nursing homes on average cost $6,180 per month for a private room (2010).

For persons privately paying for care, it is wise to have Hook Law Center review and explain the agreements relating to the care before signing them. For example, do they contain personal guaranties that must be signed by family members or arbitration agreements? Many persons, however, are unable to pay these costs out of their income and therefore must spend their savings, frequently to the point of exhausting their savings. Other private payment options include long-term care insurance, reverse mortgages and use of life insurance.

Long-term care insurance (LTCI) is an insurance product that pays for long-term care. It is a complex form of insurance. The following matters concerning these policies should be carefully reviewed: premiums, elimination periods, triggering events, facilities (i.e. in home, assisted living facility or nursing home) covered, inflation coverage, and the financial strength of the issuing company. Recently, a new type of LTCI policy was created, called a partnership LTCI policy. If the owner otherwise qualifies for long-term care benefits, he or she can retain assets equal to the amount of benefits paid out by his or her partnership LTCI policy. We recommend that clients over the age of 60 years consider LTCI policies. Hook Law Center can help you determine if you need a LTCI policy and select the right policy. If you do purchase LTCI, you should buy enough coverage to meet your anticipated needs, and you should consider home care coverage so that you will not feel compelled to move into a nursing home.

A *reverse mortgage* is a loan against your home that you do not have to pay back for as long as you live there. It can be paid to you all at once, as a regular monthly advance, or at times and in amounts that you choose. The loan amounts can be used to pay for long-term care expenses. You pay the money back plus interest when you die, sell your home, or permanently move out of your home. The borrower must be at least 62 years of age and must occupy the residence as his or her principal residence. The reverse mortgage, however, will have a high upfront cost that makes it inappropriate, unless you intend to remain in your home for an extended period of time.

Life insurance is a source of cash to pay for your long-term care. There are several options to obtain cash from your life insurance:

- First if you own whole life insurance, you can borrow against the policy. The loan proceeds are tax- free, but the loan amount and interest will be deducted from the death benefits at your death.
- The second option for whole life insurance is to surrender the policy for its cash value. After surrendering the policy, you will not have to pay additional premiums and the receipt of the cash value of the policy is income tax-free to the extent of the premiums you have paid. However, keep in mind the death benefits under the policy will be lost.
- For the third option, you can sell your policy to a third party. If you have a terminal condition, this is called a viatical settlement and the sales proceeds are tax-free. If you do not have a terminal condition, this is called a life settlement and the proceeds of sale in excess of the premiums you have paid are taxable. In both cases, the purchaser will pay future premiums and receive the death benefits.
- The last option is accelerated death benefits. Accelerated death benefits are a policy provision (contained in some term and whole life policies) that permits a policy holder who requires long-term care to withdraw a portion of the death benefits during his or her lifetime. The withdrawals are tax- free, but the amount of the withdrawals is deducted from the death benefits.

What are the other options for the payment of your long-term care?

Medicare and Medicare Supplemental insurance policies pay for a limited amount of skilled nursing facility care, if you have been in a hospital for 3 days during the preceding 30 days. Medicare pays for the first 20 days of skilled nursing home care in full and in part for up to an additional 80 days. Most Medicare supplemental policies will pay the copayment for the additional 80 days. Medicare and Medicare Supplemental insurance policies do not pay for custodial or intermediate care.

The Department of Veterans Affairs provides several benefits for long-term care for veterans. The Improved Disability Pension is available for veterans who do not have a service-connected disability. The benefit is also available for widows and widowers of such eligible veterans. The application for this benefit will be denied, if the applicant's income exceeds published income limits that are annually adjusted. However, the costs of home health care, assisted living facilities or nursing homes will reduce countable income. Additionally, the applicant may not have resources deemed sufficient to pay for their own care. The VA uses an age analysis, but it is commonly believed that an applicant may retain about $80,000 in resources. There are no penalties for transferring assets to qualify for these benefits. There are two special allowances that may increase the improved disability pension. The first allowance is the Housebound allowance. The applicant must either have a disability rating of 100% disability and must be confined to his or her home or have a disability rating of 100% and an additional disability with a rating of at least 60% but with no requirement to be housebound. The second special allowance is Aid & Attendance for a veteran or eligible widow(er) who is living in a nursing home, or who needs assistance with activities of daily living at home or in an assisted living facility. In addition to these non-service-connected benefits, the VA will pay for nursing home care for veterans with severe (about 70%) service-connected disabilities.

Medicaid is an additional payment option that many senior citizens rely upon. Medicaid is a state- administered welfare program that pays for long-term in-home care and nursing home care. In addition to these services, the Medicaid program provides the PACE program, which provides community-based services to the elderly in an adult day care center. These services include primary medical and specialty care, nursing, social services, personal care, in-home supportive services, rehabilitative therapies, meals and nutritional care, and transportation.

There are strict income and resource limitations on the qualification for Medicaid benefits. There are penalties for some gifts made within five years of applying for Medicaid assistance. With proper planning, however, it is possible to avoid impoverishment, protect your home and qualify for Medicaid long-term care assistance. Because of the high cost, many families rely on Medicaid to pay for long-term care. Hook Law Center can assist you or a family member in obtaining Medicaid eligibility while preserving assets and can assist with the preparation of the necessary applications. We publish a guide to Medicaid eligibility in Virginia. You may obtain a copy on our webpage, www.hooklawcenter.com.

When you have aging parents, how do you begin the process of assisting them with their estate, asset protection and financial planning? Begin by having a series of frank conversations ("family meetings") with your parents. If you have siblings, we recommend, with your parents' permission, including them in the family meetings to avoid misunderstandings and to minimize the likelihood of family controversy. If siblings cannot personally attend, you should suggest that they participate by speaker phone. A single family meeting will frequently be counterproductive, since trying to do too much too fast may be overwhelming. Therefore, we recommend a series of meetings with each meeting to address a different set of questions. Where there are differences of opinion among family members, frequently having a professional, such as Hook Law Center, assist with the planning and conduct the meetings will be helpful.

These conversations with your parents should include a discussion of the following:

- What are their financial resources and sources of income?
- Where are their financial resources and records (including financial statements, deeds, tax returns … etc) located?

- Who are their advisors (attorney, tax return preparer, investment advisor, insurance agent … etc)?
- Which member of the advisory team has handled which tasks in the past?
- Do they have any debts?
- Do they have sufficient income and/or resources to pay for their long-term care?
- How do they wish to dispose of their property?
- Is their home still an appropriate place for them to live?
- When their home is no longer appropriate, where do they want to live?
- How will they obtain necessary care?
- What are their end-of-life health care preferences?
- Have they made their funeral and burial decisions?
- Who do they wish to assist them with the management of their affairs? Is that person willing and able to provide the necessary assistance?
- Do they have appropriate legal documents (i.e. power of attorney, advance medical directive, will … etc) and where are they located?

Hook Law Center has a Certified Elder Law Attorney (CELA) and a CERTIFIED FINANCIAL PLANNER™ professional (CFP®) in Andrew H. Hook who can help you develop an appropriate plan that incorporates the appropriate options for the payment of long-term care and the preservation of assets. In addition, we can help you apply for appropriate benefits or represent you if you must appeal a denial of needed benefits.

INCOME TAX PLANNING

The income tax cuts of the recent past were supposed to lift economic growth (which they did) faster than federal spending (which they did not). It was not even close. The resulting increase in federal debt and under-funded federal entitlements such as Social Security and Medicare make it probable that income tax rates will increase.

Therefore, income tax planning will become even more important in the future. However, income tax planning and tax return preparation is complex. It is especially complex for persons (and their families) that are nearing retirement, are retired, or are receiving long-term care. In addition to complexity, the rules frequently change.

Examples of this complexity include:

- Alternative Minimum Tax – For retirees whose principal source of income are dividends or capital gains, the Alternative Minimum tax may impose a higher rate of tax than the regular income tax rates.
- Additional Standard Deduction - A taxpayer who is 65 before the close of his tax year is entitled to an additional standard deduction for the elderly. Persons with visual challenges may also receive another standard deduction.
- Minimum Required Distributions – Beginning on April 1 of the year after you turn 70 ½, you must begin distributions from traditional IRA accounts. An exception to this rule for Qualified Retirement Plans applies if you are not an owner, have not retired, and are still working.

- Withdrawing Retirement Funds Early – Large retirement account balances remaining in your name at your death may be subject to both estate and income taxes. You should weigh the tax effects of withdrawing retirement funds early.
- Deduction for Long-term Care – Taxpayers that meet the definition of “chronically ill” may deduct, as a medical expense, the cost of obtaining necessary long-term care services.
- Entrance Fees to CCRC – Residents of a Continuing Care Retirement Community (CCRC) may deduct as a medical expense a portion of the one-time entry fee and ongoing payments for independent living units and assisted living units that guarantee occupants eventual access to skilled-nursing units. However, following the Tax Relief and Health Care Act of 2006, many CCRC’s are structuring their continuing care contracts as loans with graduated refund features. This approach allows the CCRC to postpone the reporting of income but thwarts the residents’ efforts to deduct a portion of the fee as a medical expense.
- Long-term Care Insurance – Benefits, subject to per day limits, under qualified LTCI polices are not subject to income tax. Premiums paid for LTCI are deductible up to specified dollar limits and subject to the overall floor for medical expenses, i.e. 10% of AGI.
- Taxation of Social Security Benefits – Depending on your “Modified Adjusted Gross Income,” a portion of Social Security benefits may be taxable for income tax purposes.
- Credit for the Elderly and the Disabled – Taxpayers with limited income who are over age 65 or who are disabled may be eligible for a tax credit.
- Accelerated Death Benefits or Viatical Settlement - Any lifetime payments received under a life insurance contract on the life of a person who is either terminally or chronically ill are excluded from gross income. A similar exclusion applies to the sale or assignment of a life insurance contract to a person who regularly buys or takes assignments of such contracts and meets other qualifying standards.
- Dependency Exemption – Frequently, a child will help care for his or her parent. The child may be able to claim the parent as his or her dependent, thus qualifying for an exemption. To qualify, (a) the child must provide more than 50% of the parent's support costs, (b) the parent must not have gross income in excess of the exemption amount, (c) the parent must not file a joint return for the year, and (d) the parent must be a U.S. citizen or a resident of the U.S., Canada, or Mexico. If the support test ((a), above) can only be met by a group (several children, for example, combining to support a parent), a “multiple support” form can be filed to grant one of the group the exemption, subject to certain conditions.
- Medical Expenses for Care of a Parent - If your parent qualifies as your dependent, you can include any medical expenses you incur for him or her along with your own when determining your medical deduction. If he or she doesn't qualify as your dependent only because of the gross income or joint return test, you can still include these medical costs with your own. The costs of qualified long-term care services required and eligible long-term care insurance premiums are included in the definition of deductible medical expenses.

These are only a few examples of the complex income tax rules confronting the elderly, disabled and their families. Hook Law Center can assist the elderly, disabled and their families with income tax planning and return preparation.

INVESTMENT PLANNING

Hook Law Center is frequently asked to assist our clients with financial planning for their retirement or the payment of their long-term care. Unfortunately, we often find that our clients have made significant mistakes in their investment planning. These mistakes jeopardize our clients' ability to provide for their support during retirement, pay for necessary long-term care and to leave inheritances to their children. In some cases, the client may run out of money needed for the client's support because of the investment mistakes.

To avoid investment errors, Hook Law Center recommends that our clients:

- Put your investment and financial plan in writing. This writing is frequently called a financial plan or investment policy statement. Although a professional advisor can assist you with this responsibility, you should not delegate the actual decision making to the professional. In making investment decisions you should not deviate from your stated goals and objectives due to emotions; however, you should annually review and revise your plan as necessary due to changes in your circumstances.
- Obtain investment advice from "fee-based" advisors rather than from "commission-based" advisors. Commissions create conflicts of interest because a commission-based advisor is compensated for making money from you rather than for you. Hook Law Center recommends that financial and investment advice from a CFP® professional on a fee basis, as opposed to a commission basis.
- Do not rely on your emotions. It will lead you to sell at market lows and invest at market highs.
- Save. Save. Save. Most Americans will not have a defined benefit pension. They must rely on their savings to fund retirement, pay uninsured medical expenses and pay for long-term care. However, it is likely that investment returns will be more modest than we have experienced in the last 25 years. To insure a reasonable high likelihood that you will not run out of money during your retirement, you should plan on withdrawing only about 3% of your savings each year. For example, $500,000 of savings will generate an annual withdrawal of only $10,000 per year. Therefore, you must save a significant portion of your disposable net income to fund your retirement expenses.
- Do not speculate. When you play the market or day-trade, you are gambling on your ability to beat the pros. You will lose.
- Do not invest primarily for "tax reasons." Tax shelters are frequently poor investments.
- Do not consider your home as an investment. Think of it as a place where you and your family live.
- Reduce investment risk and increase returns by allocating investments among different asset classes such as large cap stocks, small cap stocks, REITs, foreign stocks, and bonds. During the next 20 years, it is likely that the US share of the global economy will be cut in half. Therefore, a significant portion of your investments should be in international investments.
- Monitor investment performance on a quarterly basis and re-balance your investment allocation every one to two years.
- Review these allocations in light of tax law changes.
- Increase investment returns by controlling investment expenses and taxes. To accomplish these objectives, we frequently recommend that our clients consider using index or passively managed mutual funds.

- Understand inflation risk. Historically, inflation runs approximately 3% per year. In some periods it is lower. Too many individuals invest all of their savings in fixed-income securities (Certificates of Deposit, Savings Bonds, Municipal Bonds, Money Market accounts, … etc). After the payment of taxes on the interest income and factoring in inflation, there is little or no investment return on these vehicles. Therefore, you should consider allocating a portion of your savings to equities which historically have done better in keeping up with inflation.
- Avoid excessive withdrawal rates from your savings. As a rule of thumb, to avoid running out of savings during your lifetime, assuming a balanced portfolio of stocks and bonds, you should limit annual withdrawals to about 3% of your savings valued annually. A better solution is to meet with a CFP® and develop an appropriate withdrawal percentage as part of a financial plan based on your investment risk tolerance, investment asset allocation, and cash flow needs. This financial plan should be reviewed on an annual basis or sooner if your circumstances change.
- Reduce the number of investments that you must monitor by consolidating your accounts and using indexed mutual funds. Many of us have a dozen or more different accounts and investments. It is difficult to stay abreast of all of these accounts and investments.
- Purchase an umbrella liability insurance policy to protect yourself against liability from lawsuits. Purchasing umbrella liability coverage equal to the amount of your net worth is a simple way to reduce your risk of exposure to liability.

To assist our clients with financial and investment planning, we have formed Hook Law Center Financial Services, a Registered Investment Advisor and financial planning firm which is separate from Hook Law Center, which provides legal services.

PERIODIC REVIEW

Estate plans, asset protection and financial plans do not last forever. Most people should initially implement their plans at an early age and then review their plans at least annually (i.e. plan early and often). We never charge existing clients for a brief review of their situation.

In addition, you should review your plan every time there has been a significant change in circumstances for you or your family. For example, you should review your estate and financial plan:

- upon your marriage,
- upon the birth of a child,
- when your children become adults,
- upon your divorce,
- upon your retirement,
- upon the death of a spouse, family member or beneficiary,
- if your spouse, family member or beneficiary suffers a disability,
- if you, your spouse or other family member requires long-term care,
- when there has been a significant change in your income or assets,

- when there has been a significant change in the income or assets of a family member,
- when you move to another state, or
- when your children or other family member marry.

Many clients fail to revise their estate, asset protection and financial plans upon their divorce or prior to a second marriage. This can lead to unintended, if not disastrous, results. Timely estate planning can avoid many problems. For example, a premarital agreement before a second marriage can provide for your new spouse and protect your children's inheritance. You should contact us whenever any of these events occur.

You should also review your estate, asset protection, and financial plans every time you are aware of a significant change in the laws. We address such changes in our weekly newsletter, the *Hook Law Center News*. Please call Hook Law Center at 757-399-7506 or visit our website at www.hooklawcenter.com, if you would like to subscribe to the newsletter.

CONCLUSION

The failure to implement an effective comprehensive estate, asset protection, and financial plan can wreak havoc on the client's and the client's family's finances and cause unnecessary stress and expenditures of time and money. Hook Law Center specializes in assisting its clients in estate, asset protection, and financial planning for the benefit of the client and his or her family.

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