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Financial Concepts

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The Basics of the New Health Care Law

On March 30, 2010, the Health Care and Education Reconciliation Act of 2010 was signed into law, representing a massive overhaul of the health care system that will affect almost all taxpayers, many employers, and much of the health care industry. However, the provisions will be implemented over a number of years. Here is a summary of the major provisions by implementation date:

2010

Medicare beneficiaries will receive a $250 rebate when they reach the gap in coverage for prescription drugs, known as the "doughnut hole." The gap exists when total costs exceed $2,830 until they reach $6,440.

A national high-risk insurance pool will offer insurance to individuals who have a preexisting condition and have been uninsured for at least six months until 2014.

All insurance policies must offer dependent coverage to children who have not yet attained age 27.

Insurance companies must cover certain preventive services. They also can no longer impose lifetime coverage limits, rescind coverage for any reason other than fraud, or exclude preexisting conditions for children.

Businesses with less than 25 full-time workers who are paid less than $50,000 per year in salary get a tax credit of up to 35% of the health insurance premiums paid for employees. The credit rises to 50% in 2014.

2011

The costs for over-the-counter drugs not prescribed by a doctor can no longer be reimbursed through a health reimbursement account (HRA) or health flexible spending account (FSA) or be reimbursed on a tax-free basis through a health savings account (HSA) or Archer Medical Savings Account (MSA).

The tax on distributions from a HSA or an Archer MSA that are not used for qualified medical expenses is increased to 20% of the disbursed amount, up from 10% for HSAs and 15% for Archer MSAs.

Medicare recipients receive free preventive services and a 50% discount on brand-name drugs purchased in the Part D doughnut hole.

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Why Long-Term-Care Insurance?

I believe the two greatest risks to a retirement portfolio's ability to meet your objectives are the inability to keep pace with inflation and the costs associated with ill health. The intent of long-term-care insurance is to help you weather the latter risk. It is not a replacement for good health insurance. It covers long-term-care services, such as help with daily activities at home, respite care, adult day care, and care in a nursing home.

Long-term-care insurance policies should be carefully evaluated, and you should not rush into purchasing such a policy. Policies vary by the benefits they offer and the type of care they cover. I used to believe that you should consider purchasing long-term coverage at retirement or early into retirement, as the premiums significantly escalate after age 65. However, I now believe it is coverage you should at least consider at an earlier age. This change of opinion is due to the fact that a change in your health may preclude you from obtaining coverage, and some policies allow you to pay for the premiums in 10 years instead of your lifetime. This feature may allow you to pay for your coverage before you retire while you have the extra income to best afford the premiums.

Please call if you would like help deciding on a long-term-care insurance policy.

Health Care Law

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2013

Starting in 2013, single individuals with earned income in excess of $200,000 and married couples with earned income in excess of $250,000 will pay an additional 0.9% Medicare tax on the excess over those base amounts.

A 3.8% Medicare tax will be imposed on net investment income of single individuals with adjusted gross income over $200,000 and joint filers over $250,000. Net investment income includes interest, dividends, royalties, rents, gross income from a trade or business involving passive activities, and the net gain from the disposition of property (other than property held in a trade or business). This tax applies only to income in excess of the thresholds. Thus, if a couple earns $150,000 in wages and $150,000 in capital gains, $50,000 will be subject to the new tax.

The threshold for deducting medical expenses on a tax return increases from 7.5% to 10% of AGI. Individuals age 65 and older are exempt from this increase through 2016.

Allowable flexible spending account contributions are limited to $2,500 per year. The dollar amount will be indexed for inflation after 2013.

2014

All U.S. citizens and legal residents must have qualifying health insurance or pay a tax penalty. The tax penalty will be the greater of:

- $95 per year (maximum of three times that amount or $285 per family) or 1% of taxable income in 2014
- $325 per year (maximum of three times that amount or $975 per family) or 2% of taxable income in 2015
- $695 per year (maximum of three times that amount or $2,085 per family) or 2.5% of income in 2016

After 2016, the penalty will be increased annually by a cost-of-living adjustment. Exemptions will be granted for financial hardship, religious objections, American Indians, individuals without coverage for less than three months, aliens not lawfully in the United States, incarcerated individuals, individuals who find the lowest-cost plan option exceeds 8% of household income, individuals with incomes below the tax filing threshold ($9,350 for singles and $18,700 for couples in 2010), and individuals residing outside the U.S.

Individuals and small businesses with fewer than 100 workers will be able to purchase health insurance on state-based health insurance exchanges. When insurance is purchased on the exchange, the individual reports his/her income. Low- and middle-income individuals and families may then be eligible for a tax credit based on the income reported. The IRS will pay the premium assistance credit directly to the insurance plan, with the individual paying the difference in premium. The premium assistance credit is available for individuals and families with incomes up to 400% of the federal poverty level ($43,320 for an individual or $88,200 for a family of four, based on 2009 poverty levels) who are not eligible for Medicaid, employer-sponsored insurance, or other coverage.

Businesses with 50 or more workers will pay an annual penalty if they do not provide health insurance coverage to workers.

2018

"Cadillac" health insurance plans must pay a 40% tax on the portion of coverage worth more than $10,200 for individuals and $27,500 for families. ❍❍❍

Choosing a Guardian

For parents with minor children, the most important reason for estate planning is to ensure that provisions have been made for their children. Some items to consider include:

- **Carefully select a guardian.** While your first inclination may be to select your parents, make sure they have the energy to raise your children. A better alternative may be a sibling or friend. If you have several children, decide whether it is reasonable to expect one person to raise them all.
- **Talk to your selected guardian.** Once you've settled on a guardian, discuss your decision with that person to make sure he/she is willing to take on the responsibility. Name a contingent guardian in case your first choice is unable to serve.
- **Make adequate financial arrangements.** You wouldn't want your children to be a financial burden, or their presence may be resented. Determine how much is needed for living expenses, hobbies, medical expenses, and college. Other items need to be considered as well. Include a financial cushion so there is plenty of money until your children reach adulthood.
- **Decide who should manage your children's finances.** The person with physical custody of your children may not be the best person to handle their finances. Thus, you may want to select another individual for that role. You should also consider whether trusts will need to be set up and how money should be distributed when your children reach adulthood.
- **Express your wishes to your selected guardian.** This will help ensure your children are raised according to your beliefs. Make sure to indicate your preferences for education, religion, lifestyle, and other important issues.
- **Review your choice of guardian every year.** As your children grow, you may realize that the person you originally selected as guardian is no longer the right choice. ❍❍❍

Avoid These Life Insurance Mistakes

Life insurance can be used for a variety of personal and estate planning needs. To ensure your life insurance policy meets your needs, watch out for these common mistakes:

❍ **Not considering life insurance at all.** Life insurance forces us to take a look at our own mortality, a subject most people would prefer to ignore. In fact, one third of all adults have no life insurance at all (Source: *U.S. News & World Report*, April 6, 2009). But without life insurance, you could be leaving your family in dire financial circumstances if you die. You should thoroughly assess your situation to see how much life insurance is needed.

❍ **Relying on rules of thumb.** When deciding how much life insurance you need, avoid common rules of thumb, such as five to 10 times your annual salary. These are general guidelines and are not meant to be a definitive guide to the amount of coverage you need.

❍ **Making your decisions based solely on the premium amount.** You should base your policy selection on the amount of coverage it provides, rather than monthly or annual premiums. A wide variety of life insurance policies are available, many designed to meet specific needs. Understand the basics of each before deciding which type is most appropriate for your situation.

❍ **Not selecting appropriate beneficiaries.** Estate and tax ramifications should be considered before selecting beneficiaries. For instance, naming your estate as beneficiary could cause the proceeds to be included in your taxable estate. Or, if your spouse owns the policy on your life with your children listed as beneficiaries, the policy proceeds may be considered a gift, subject to gift taxes. Be sure to name contingent beneficiaries in case your primary beneficiary dies before you do.

❍ **Replacing an existing policy without first evaluating it.** Look at an in-force ledger statement to determine the policy's current status and growth projections. If you need more insurance, you can always apply for another policy for the additional amount needed. A policy change may require a medical examination and may incur fees and costs.

❍ **Not evaluating your situation periodically.** Your life insurance needs are likely to change over time, as your personal and family situations change. Thus, you should periodically review your needs to see if changes are warranted. ❍❍❍

Handling Financial Aspects of Death

The emotional trauma of dealing with a loved one's death can be devastating. If you also have to handle the financial aspects, it can seem overwhelming to deal with all the details. Following is a checklist to consider:

❍ Your most immediate concern will be to notify family and friends of the death and to make funeral arrangements. If you aren't sure of the deceased's burial wishes, look for a letter of instruction. You'll probably need to contact a funeral home as well as your loved one's religious organization. An obituary will need to be prepared, a burial site may need to be purchased, and death certificates must be obtained.

❍ If a surviving spouse and/or minor children are involved, evaluate their means of support and determine whether care for the dependents needs to be obtained. In terms of the deceased's home, you may need to deal with security at the residence, provide for the care of pets, send mail to another location, and arrange for the care or disposal of perishable property.

❍ Locate any safe deposit boxes and follow necessary procedures to have them opened.

❍ If the deceased was employed, contact his/her employer to start the process of collecting any outstanding pay, life insurance proceeds, or other benefits. If the deceased was retired, notify Social Security and pension plans.

❍ Locate important documents, including wills, trusts, deeds, investment records, insurance policies, business and partnership arrangements, and other evidence of assets and liabilities.

❍ Meet with an attorney to discuss the deceased's estate matters. Depending on the estate's complexity, you may need to retain an attorney, accountant, and/or financial advisor. While you may be hesitant to spend the deceased's funds on professional services, these professionals have experience dealing with the financial matters of estates and can help significantly with the process. ❍❍❍

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Don't Forget to Organize Your Estate

Don't think you're finished with the estate-planning process once a will, trusts, and other estate-planning documents are in place. From your heirs' point of view, it's just as important for you to organize paperwork and inform them of basic decisions. One way to approach this task in a systematic manner is to prepare a notebook including the following items:

❍ **Net worth statement.** An up-to-date net worth statement is a good way to ensure heirs are aware of every asset and liability. Make sure to list all pertinent information for each item on the statement, including account numbers, contact names, and phone numbers. Identify where important documents are kept, including deeds, loan agreements, insurance policies, etc. You may also want to explain your rationale for your estate's distribution. You can go into specific detail, informing heirs how each asset will be distributed, or you can give a general overview of your estate plan. If you selected one heir as executor or trustee, explain why you chose that individual.

❍ **Individuals to contact.** List names, addresses, and telephone numbers of individuals your heirs may need to contact, including employers, attorneys, accountants, insurance agents, investment managers, and financial planners.

❍ **Personal papers.** Indicate where personal records are kept, including your birth certificate, marriage certificate, divorce or separation agreements, diplomas, military records, and naturalization records.

❍ **Safe deposit box.** Indicate where the safe deposit box is located and what is contained in the box. Note where the key is kept and who has access to the box.

❍ **Disposition of personal items.** Detail how you would like personal items distributed, including jewelry, photographs, personal collections, and furniture. Often, disputes over personal possessions are more apt to cause conflict among heirs than disputes over money, so explain your rationale for the distribution of personal items. After you have decided how to distribute your most valued possessions, come up with a method for heirs to distribute the remainder. It can be as simple as taking turns to select items or flipping a coin if more than one individual is interested in the item.

❍ **Last wishes.** Indicate your preferences for funeral arrangements, including whether you want a religious or secular service, whether you want flowers or donations to a charity, whether you want to donate your organs or body to medical institutions, and where you would like to be buried. These are details your heirs may feel uncomfortable asking about, but will be grateful your wishes are known so they can be carried out. Also, list any friends or family you would like contacted after your death.

Your thoughts on these subjects can change over time, so review and update the information periodically. Keep it in a place where heirs can find it immediately after your death. ❍❍❍

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Did You Know?

In a a recent survey, almost half (46%) of those currently working plan to delay retirement. However, most retirees (64%) retired ahead of schedule, with only 3% retiring later than they originally planned. Only one-third of those who want to work after retirement have looked into a new career (Source: MetLife, 2010).

New estimates indicate that U.S. workers need to accumulate more than 15 times their final pay to maintain their preretirement standard of living after retirement. Social Security is expected to provide 4.7 times final pay, leaving workers to provide the remaining 11 times final pay through employer-sponsored retirement accounts and other personal savings. Researchers predict that only 18% of workers who contribute to a defined-contribution plan and work a full career are likely to meet this goal (Source: Hewitt Associates, 2010).

Approximately 3.7 million individuals age 65 and over are not able to meet basic daily expenses and another 10 million are considered low income, approximately one-third of the elderly population (Source: AARP, 2010).

In a recent survey, approximately 92% of Americans have not discussed long-term care with their spouses or partners. Almost 65% of the survey respondents say the biggest barrier, besides cost, to purchasing long-term-care insurance is confusion (Source: *Financial Planning*, 2010). ❍❍❍