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It's Time to Start Thinking About the Estate Tax

In tax years 2007 and 2008, estates valued at more than \$2 million may be taxed as much as 45 percent, while in tax year 2009, the threshold will increase to \$3.5 million. The year after that, the tax will be repealed for a year.

However, in 2011, unless Congress acts, the party's over. The estate tax will be reset at up to 55 percent on estates at a significantly lower threshold – \$1 million.

While bills continue to swirl around Congress and many expect a Band-Aid of some sort before 2011, no one seems to believe that the so-called "death tax" is likely to be eliminated altogether. That makes it tough for individuals to set a clear course for their own estate planning. If you suspect your estate or the estate of relatives you might inherit from may fall prey to the estate tax, it makes sense right now to enlist the help of experts. Assets may be expected to grow over time, and your estate may turn out to be larger than you may think. You should be talking to estate and tax specialists as well as financial advisors such as Certified Financial Planner™ professionals. *Please call us at (925) 299-1500 if you would like a referral to an Estate Planning Attorney.*

Here are some things to keep in mind as you plan those conversations:

Think about a life insurance trust: Whether you need it for estate liquidity or for other purposes, an irrevocable life insurance trust can be created to keep the proceeds of the insurance out of your taxable estate. An added benefit is that such trusts may permit spousal access to the cash value of the policy. Yet note the word "irrevocable" – it means a decision that cannot be changed.

If your assets are expected to increase: A grantor-retained annuity trust, or GRAT, is an irrevocable trust that is popular among families with assets that are expected to increase, because such appreciation can be passed on to heirs with minimal tax consequences.

Prepare a gifting strategy: Under current law, unlimited amounts can be left to a spouse or to charity free of federal estate tax. Other heirs can receive a total of \$2 million, tax-free, when deaths occur in 2007 or 2008. If your assets are over the estate tax limit, it might make sense to devise a gifting strategy that spends down your total taxable estate while still allowing you a comfortable lifestyle. You might, for instance, consider making direct payments for someone else's medical bills or education tuition. No gift tax applies for these items, so payments can be unlimited.

The Boomers Hit 62

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By Justin Fox

They're turning 62 this month, the first of the baby boomers are. Adorable, aren't they, as they hum along to the Beach Boys on their iPods and dream of Davy Crockett coonskin caps? In February the 100,000 or so of these January 1946 babies who opted for early retirement will get their first Social Security checks (averaging between \$900 and \$1,000 a month), marking the beginning of a demographic wave that will boost the program's rolls from 50 million to 80 million over the next two decades. Not so adorable, eh?

You've heard about the pending retirement of the boomers before, of course. You've also heard that Social Security faces some big funding problems. The two have less to do with each other than you might think. Social Security's insolvency remains a hypothetical threat decades into the future. But because of the particular way its funding was rearranged by Congress in 1983, the rest of the Federal Government, as well as taxpayers, will begin feeling the cost of the boomers' retirement in just three or four years.

Let me explain. In 2041 the trust fund that pays Social Security benefits is projected to run out of money. After that, a yawning gap between benefits and income stretches as far as an actuary's eye can see. This long-term gap is what President George W. Bush was trying to address with his failed plans to partly privatize Social Security. It's been the focus of almost all recent debate about the program.

Most of the baby boomers, though, will be dead by 2041. I was born in 1964, considered the final year of the boom, and according to the Social Security Administration, I should expect to keel over by the end of 2042. So it's not we boomers but long-run trends in immigration, fertility and life expectancy that are projected to leave the program chronically short of funds after that.

The trends can only be guesstimated, and that inherent uncertainty is cited by blithe spirits as reason not to do anything about Social Security. Worrywarts, meanwhile, argue that the distance of the looming bankruptcy is all the more reason to make changes calmly now. Both arguments have merit, but it's the former that is almost certain to prevail. Previous Social Security fixes came only when the checks were about to bounce, and that dire moment is decades off.

Such a funding crisis was just months away in 1983 when a bipartisan gang led by Senators Bob Dole and Daniel Patrick Moynihan cracked heads and persuaded Congress to move up some already planned payroll-tax hikes and shove back the full retirement age to 67 for future generations. Since then, Social Security has run a surplus. From an actuarial standpoint, this mostly solved the problem of funding the boomers' retirement. It also meant that the boomers will, as a group, put more into Social Security than they get out. (That's true of all age cohorts born since 1937; it's the Social Security recipients born before then who have, as a group, made out like bandits.)

The catch is that the surplus was invested in U.S. government bonds, to be cashed in later to keep the by-then-elderly boomers afloat. These bonds are simply claims on future U.S. taxpayers, and they're coming due. The Social Security surplus peaked in 2000, at 0.91% of GDP. It has held steady for the past couple of years but is expected to start shrinking fast in 2011. By 2017, Social Security should begin to run a deficit, one that's projected to grow sharply through the mid-2030s.

The crisis projected for 2041 is that the bond stash will run out. The semi-crisis set for 2011 is that Social Security will quickly go from the big boost to federal finances that it has been for the past 25 years to a big drag (a drag greatly exacerbated by the cost of paying for Medicare for the boomers, which is another story).

Something will have to give. Big changes in Social Security itself seem out of the question, so federal taxes other than payroll taxes will have to go up, government spending outside of Social Security will have to be cut, or budget deficits will grow. Or, most likely, a combination of all three. And it will begin to hit during the first term of whoever gets elected President in November. Not that you'll hear much talk about that on the campaign trail.

Long-Term Care Insurance on the Rise

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The Berkshire Eagle (Pittsfield, Massachusetts)
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By **Ellen G. Lahr**, *Berkshire Eagle* Staff

Ron and Judy Turbin are among the baby boomers who have witnessed the decline of an elderly relative, whose final years were spent in a nursing home bed.

Judy Turbin's father faded with strokes and dementia, and her mother eventually could no longer care for him alone.

Their finances were modest, so Medicaid covered the cost of her father's nursing home care. He died in 2005, after six years in a Lenox facility.

"Judy's parents were not loaded up with resources, and so his was a clear-cut Medicaid case," said Ron Turbin, a semi-retired lawyer and Williamstown selectman, whose wife recently opened a pastry business. "But we got concerned about our own situation."

Long-term care costs, he said, could be "a financial earthquake, and we might have to sell our house."

The Turbins, who are in their 60s and in fine health, bought a long-term care insurance policy two years ago, for which they spend around \$4,000 per year.

"It's worth it, but it's a sacrifice," said Ron Turbin. "Perhaps we have a little less for luxuries, but I really think it's worth it. It's peace of mind."

The policy will pay for nursing home care, but also pays for what Medicaid will not: home care and assisted living.

The Turbins want to ease the potential burden of care on each other and their children, protect their home and assets, and leave something for their three grown children.

Costs on the Rise

With the elderly population living longer, their needs for daily help or all-around care are on the rise.

In Massachusetts, average nursing home costs were \$270 per day in 2007, according to the National Clearing House for Long Term Care. Assisted living costs an average of about \$4,300 monthly, and in-home care runs about \$20 per hour.

Unless, and until, the patient is poor enough to meet federal poverty guidelines, nursing home bills must be paid with private funds. That means a potential depletion of savings, retirement funds, home equity, real estate or other assets.

"You can retire with a half-million in the bank, and it can cost \$100,000 per year to be in a nursing home," said Gary Kobran, financial services manager of Wheeler & Taylor Insurance in Great Barrington. "But long-term care insurance is a very tough sell. The people who need it most are the middle class, not poor, not rich."

Those who do buy are getting younger, however, according to Jackie Metsma, a financial planner and long-term care insurance specialist for True North Financial Services, based in Williamstown.

"People used to look at this option when they prepared to retire, but now more people are in their early 50s," she said. "People are now going through things with their parents, and they don't want their own kids to go through it."

The American Association of Retired Persons estimated in 2005 that 7 million long-term care policies were in place, with the typical consumer at age 61.

Nearly half of those policy holders had incomes above \$75,000 per year and more than \$100,000 in liquid assets.

In 2005, the average annual insurance premium, across all age groups, was \$2,000, according to the federal government's data.

Industry changes allow discounts for couples, and some companies sell "hybrid" policies that combine long-term care insurance with life or disability insurance, said Metsma.

Sharp Hikes

The earliest policies written have taken sharp price hikes in recent years.

George and Caroline Farley, of Pittsfield—he is 81, and she is 77—bought policies 14 years ago through their son, Shaun Farley, a broker now with Greylock Insurance.

The Farleys' initial annual premiums were \$1,700 for him, and \$1,100 for her, said George Farley, a retired schoolteacher.

But their most recent bill was a shocker: \$3,700 for him, and \$2,700 for her.

Though the policy cost has spiked, he said, "we will stick with it. We don't want to lose it."

They also want to live at home as long as possible, he said.

Kobran, of Wheeler & Taylor, said the Farleys are victims of the insurance industry's early errors in financial projections.

The insurance industry, which is closely regulated, relies on income from interest earnings to pay claims, and interest rates have been low in the 20 years since long-term care insurance has been around.

Second, insurance companies assumed a higher number of policies would lapse through nonpayment. That, too, proved incorrect, he said.

Most people with long-term care insurance keep it.

Patrick Sheehan, of Sheehan Health Group, which owns Craneville Place nursing home and Sugar Hill Assisted Living, said many people who have purchased long-term care insurance have not yet reached the age of needing the benefit.

Those people who do have it, he said, tend to use it for assisted living, but the numbers remain relatively small.

He advised that anyone seeking long-term care insurance become an educated consumer, since benefits vary widely, he said.

"Be smart consumers; use caution," he said. "You really need to shop around, make sure you're getting the best value for your money."

At a Glance . . .

Average costs in Massachusetts for long-term care:

Semi-private nursing home room: \$270/day

Assisted living facility: \$4,300/month*

Home health aide: \$20/hour*

* Not covered by Medicaid

Tips for shopping for long-term care insurance:

- Don't buy long-term care insurance out of fear or emotion.
- Consult a certified financial planner to determine whether your money should be used on long-term care insurance.
- Consult an insurance broker who has access to a wide variety of potential underwriters.
- Consider benefit options: Do you want full, comprehensive coverage, and can you afford it? Do you want a lifetime benefit, or a five-year cap?
- Can you tailor a less comprehensive plan that provides partial coverage, which you can supplement with income from assets or other funds?
- Do you want a "hybrid" policy, which combines life insurance or disability insurance with long-term care coverage?
- Do you have a pre-existing condition? People already in need of long-term care services won't qualify.

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