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The Future Is Now: Legal Planning for Elders

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Legal Planning for Elders

by Jennifer L. Eastman

Legal planning for elders focuses on protecting retirement income and finding ways to pay for long-term health care. Jennifer Eastman discusses estate and tax planning and planning for retirement income, Social Security issues, and asset preservation. She notes that protecting elder adults requires planning and advocating for (or against) policy changes that could adversely affect elders.

Legal planning for elders has changed dramatically in recent years. As estate-tax exemptions rise, along with the cost of and need for long-term care, legal services for elderly individuals have shifted focus from estate and tax planning to planning for adequate retirement income and savings and anticipating costs of long-term care needs in this era of increased longevity. Such planning is amorphous at best, as the rules and regulations surrounding these priorities for elders are in constant flux. While Benjamin Franklin said that nothing is certain except death and taxes, the better mantra of legal planners today emulates John Allen Paulos's statement that "uncertainty is the only certainty there is, and knowing how to live with insecurity is the only security" (2003: Introduction). Rarely can planners ensure that an elder will have enough income, assets, and protection to provide for a comfortable retirement and a quality end of life. Often planners face families in crisis seeking legal assistance for an elder relative, faced with an unanticipated income, tax, or health care event that threatens to upend the precarious balance of financial security and quality of life.

This article describes how the continuing development of retirement income protection and long-term health care present challenges to legal planners in advising the elderly and their families. Income protection includes not only estate and estate-tax planning, but also planning for retirement income, Social Security issues, and asset preservation. Health care issues generally revolve around paying for long-term care, but also include health care decision making. Protecting elder adults requires not only application of the current rule of law, but planning and advocating for (or against) those changes in policy that could dramatically affect the lives of elders today, and our lives tomorrow.

SOCIAL SECURITY RETIREMENT[1]

The traditional metaphor of retirement funding as a three-legged stool, built on Social Security, pension income, and private investments, finds itself on three shaky legs in the current fiscal environment. Americans do not have enough savings, are outliving the savings they have amassed, and face a continued threat of reduced Social Security benefits.

The Social Security system was designed to provide a minimum level of income for retired workers. Created by President Roosevelt in a post-Depression era, Social Security aimed to provide income for workers who had suffered through the Great Depression and had been unable to accumulate enough savings to fund retirement. Social Security was not intended to be the sole source of income for retirees; however, that is the case for many elders today. Twenty-nine percent of American households with members age 55 or older have no retirement savings or traditional pension benefits (U.S. GAO 2015). The GAO analysis of nine different studies conducted over the course of nine years concluded that up to two-thirds of workers may fall short of retirement saving targets.

Current workers tend to overestimate their future retirement income and savings. They intend to work longer and save more in the final chapters of their careers, but those plans do not always come to fruition. People retire earlier than expected, most often because of unanticipated health issues, changes in the workforce, or health issues of a spouse or family member (VanDerhei 2012). These unexpected developments and shortfalls lead to crises in legal planning for seniors attempting to maintain their independence and a satisfactory quality of life in retirement. For those retirees who are fortunate enough to maintain the additional legs on their financial stools, Social Security funds roughly 39 percent of a retiree's income. Social Security is estimated to keep over 35 percent of Americans above the poverty level (Shelton 2014). Social Security has become a necessity to maintain a minimum standard of living for many elders.

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Because of the security and protection afforded by Social Security, the retirement income system has been untouchable in the political forum. Attempts at reform within the system are viewed as an attack on the elderly, challenging the one thus-far stable expectation of retirement. But the system cannot last in its current form. The Social Security Administration indicates the surplus trust fund, currently covering the shortage between funds paid out and funds paid in, will be eliminated in 2034. With more baby boomers slated for retirement in the next 20 years, there are not enough workers paying into the Social Security system to balance the draw from benefits paid.

Legislative attempts to reduce the Social Security benefit could have dire effects on the retirement income and quality of life of the retired workers who depend on this income. Social Security is underfunded, and Congress is regularly reviewing ways to reduce benefits, particularly looking to curb aggressive claiming strategies that can maximize benefits through manipulating the timing of collection for some upper-income recipients. Considerations for reform include chaining the annual cost-of-living adjustment to the consumer price index, which could have disastrous effects on those elders who rely on their social security to pay for prescriptions and health care. Other proposals include raising Medicare premiums, which would reduce the net benefit paid to Social Security recipients. These potential reforms to protect the Social Security system would have substantial effects on middle- and lower-income retirees who must seek to maximize their Social Security benefits, often with no other source of income and looming health care expenses.

These threats to Social Security income cause legal planners to look for other ways to supplement and protect the income of their elder clients. As IRAs and qualified retirement plans become primary retirement savings vehicles for the soon-to-be and newly retired, those funds can be used to supplement any potential losses from Social Security. However, increasing the taxable-income distributions from these plans can raise tax rates for retirees, increasing the amount of Social Security subject to tax, and offsetting any income benefit from the increased withdrawal. While qualified retirement plans are an efficient tax and savings vehicle, such plans can lead to negative tax consequences when they must be liquidated to pay for long-term care.

Relying on the remaining legs of pension and private resources to support a weakening Social Security leg will not stabilize the stool of retirement security. Effects on any aspect of retirement income planning have necessary repercussions on the remaining pieces of the retirement puzzle, including tax and health care payment consequences.

LONG-TERM CARE PLANNING

As the baby boomer generation increases the draw from the Social Security system, so too do aging boomers increase the demand on an already stressed Medicaid system. Medicare does not cover the expenses of long-term care, including assisted living or skilled nursing care. The average cost of private nursing home care in the state of Maine is estimated at over $100,000 per year. There are three primary sources of payment for such care: personal funds, long-term care insurance, and Medicaid. With the high cost of care and the large number of underfunded retirees, personal funds are easily exhausted, leaving elders in need of care that they have no way to fund.

The federal Deficit Reduction Act of 2005 considerably reduced the availability of asset-preservation techniques employed by legal planners in qualifying elder clients for Medicaid benefits to pay for long-term care. An unmarried individual can retain only $2,000 in countable assets in order to qualify for Medicaid benefits. Retirement assets held in qualified retirement plans are considered countable assets. Withdrawing tax deferred retirement funds in lump sums, to privately pay for long-term care, or to spend down for Medicaid eligibility, will incur a substantial income-tax liability. Elders in need of expensive long-term care find themselves with an increased tax liability caused by the use of these funds to pay for their care, essentially wasting funds on income tax which would otherwise be available for their care.

Elder law planners support modification of Medicaid regulations to exempt pretax retirement accounts including 401(k) accounts, 403(b) accounts, IRAs, and other retirement savings from consideration as countable assets for public benefit eligibility purposes. Modification could include a slow spend down of the funds through required minimum distributions, without disqualifying individuals for benefits, or creation of tax deductions to offset the increase in liability where the funds are spent on long-term care. Often elders will be eligible for a medical expense deduction from the high cost of their care, but such a deduction typically does not serve to offset the increase in tax on a dollar-for-dollar basis. Qualified retirement plans grew in popularity because of the tax-deferred benefit. Loss of that tax-deferred benefit to pay the high cost of long-term care reduces the funds available to pay privately for the care and hastens eligibility for government benefits, but does not address the long-term care crisis by forcing individuals to spend those funds on income tax rather than for private care.

Long-term care insurance can be the port in a storm for elders and their families in health care and financial crises. Long-term care insurance can provide coverage during the five-year look back for Medicaid eligibility, offsetting the cost of care during the interim period between transfer of assets for preservation from spend down and application for Medicaid. (Per federal regulation, upon application for Medicaid long-term care benefits, the previous five years of all financial records must be disclosed for review. Any significant transfer of assets, over $100 in Maine, may subject the applicant to a penalty period of time during which the applicant will be ineligible for benefits. The penalty begins when the applicant is otherwise eligible for benefits, i.e., medically and financially in need of Medicaid for long-term care.) The increasing restrictions on Medicaid eligibility, including an increase in the look-back period for transfers of assets, increased penalty periods for such transfers, and increased estate recovery from the estates of decedents who received Medicaid benefits have all contributed to the attractiveness of long-term care insurance. Historically, long-term care insurance carried expensive premiums, little inflation protection, and often inadequate coverage. Current policies are vastly improved, as the insurance industry better understands its product and the needs of its clientele. Long-term care policies may still be a significant investment, but new policies make the insurance a wise decision.

The Maine Partnership Program for Long-term Care provides the policy holders with an asset disregard benefit previously unavailable. The federal Deficit Reduction Act of 2005, which made it more difficult to qualify for Medicaid, also expanded the Partnership Program. "A Partnership Program is a collaboration or 'partnership' among a state government, the private insurance companies selling long-term care insurance in that state, and state residents who buy long-term care Partnership policies."[2] Qualified policies provide additional benefits when the policy benefits are exhausted and application is made for Medicaid. Under the Partnership Program, assets in addition to the $2,000 limit may be kept and the individual may still be qualified for Medicaid benefits. The amount of the disregard is calculated by the amount of benefits actually received under the long-term care policy. Policies with inflation protection can provide savings over the amount of the insurance originally purchased. In addition, these disregarded assets are not subject to estate recovery.

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The Partnership Program policy serves as strong motivation for individuals to invest in their own long-term care and sends a message that Maine and other participating states are willing to provide incentives for those willing to do so.

It is clear that the United States has failed to create any effective policy on long-term care and instead has been closing loopholes and opportunities for any preservation of assets. Although Medicaid pays for long-term care, coverage is primarily in skilled nursing facilities, with few benefits (and much stricter eligibility limitations) available for in-home care. Because most people would prefer remain in their homes and receive in-home care, we must support policies that provide cost savings, protect autonomy, and allow for preservation of assets for family and in-home care.

We are facing a looming crisis. As the need for long-term care grows with the aging of the baby boomer population, who are faced with reductions in Social Security benefits and already-inadequate retirement savings, the Medicaid system will only become more burdened, pushing costs back on to the people who do not have the assets to bear them. Continued development of policies and programs to support the needs of the elder generation and provide some relief from further reductions in retirement income will help ensure the quality of life and care of our elders and forge the path for continued change to craft a new plan for retirement and health care security for future generations.

ENDNOTES

1. Much information in this section is from the Social Security Basic Facts website. https://www.ssa.gov/news/press/basicfact.html.
2. Partnership for Long-Term Care website: http://www.partnershipforlongtermcare.com/maine-partnership/index.html.

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