# THE COMPLETE CARDINAL GUIDE TO PLANNING FOR AND LIVING IN RETIREMENT WORKBOOK

NAVIGATING SOCIAL SECURITY,
MEDICARE AND SUPPLEMENTAL INSURANCE,
LONG-TERM CARE, IRA, LIFE INSURANCE,
POST-RETIREMENT INVESTMENT AND INCOME TAXES

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The Complete Cardinal Guide to Planning for and Living in Retirement Workbook



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# CONTENTS


1. Module 1—Social Security 1
2. Module 2—Medicare 15
3. Module 3—Long-Term Care 29
4. Module 4—IRA (Individual Retirement Accounts) 59
5. Module 5—Investments 67
6. Module 6—Life Insurance and Estate Planning 87
7. Module 7—Income Taxes 119
8. Module 8—Choosing Your Advisor 127

Index 139

# MODULE 1 | SOCIAL SECURITY

**KEY QUESTIONS**

- **When can I start to receive Social Security retirement benefits?**
- **How does my spouse receiving a Social Security benefit affect me?**
- **What happens when my spouse dies if we were both receiving Social Security?**
- **How does Social Security help me pay for long-term care?**
- **Who should I consult for advice in making decisions about my Social Security benefits?**

*Corresponds to Chapter 2, "Strategizing Your Social Security Benefits," in* ***The Complete Cardinal Guide.***

## 1.1 A Bit of History

Social Security began as a response to the challenging economic head winds the United States faced following the Great War, the Great Depression, and the failure of company pensions. President Franklin D. Roosevelt routinely received requests for assistance. One letter, from Mrs. M. A. Zoller on behalf of her 82-year-old mother who had no means of support, included a news clipping advocating a national pension paying $1.00 per day for people over 60 years old. This proposed national program would be similar to the various old age pension laws already established by 25 state legislatures. The Old Age, Survivors, and Disability Insurance program was put into effect with the passage of the Social Security Act in 1935. What we call Social Security today is a combination of several different programs that together pay retirement and disability payments to millions of Americans, including children's benefits and survivors' benefits. Altogether, Social Security is one of the largest expenditures by the federal government.

Social Security, in its current state, allows retirees to choose to receive their Social Security benefits as early as age 62. **People who opt to start Social Security at 62 receive a reduced benefit. Your full benefit is payable only if you retire at Full Retirement Age. *Full Retirement Age* (FRA) is based on your birth year.** Today most retirees have a Full Retirement Age of 66 (birth year 1943 to 1954). For retirees born after 1954 the FRA will gradually increase to age 67.

You can also choose to delay your Social Security benefits. You can earn deferred retirement credits by delaying your benefits past your Full Retirement Age. Benefits increase for every month you delay past FRA up to age 70. The increase is about 8% for every 12 months of delay. The average retirement benefit paid to a Social Security beneficiary is $1,302.86 per month (2016).

The first steps to decide if you are ready to start your journey onto Social Security involve confirming eligibility and finding the primary insurance amount for you and your family. But before we do that, let's spend a few minutes understanding the math behind Social Security and the different factors that will affect your retirement benefits.

### Reading Check

At what age can a person start receiving their Social Security benefits? When does a person become eligible for Full Retirement benefits? How long can a person delay drawing their Social Security?

## 1.2 Earning Social Security Credits

Prior to 1978, the path to becoming fully insured by Social Security was very different than the way it is done today. Employers would report quarterly earnings for their employees: Earning $50 in a three-month period would earn a worker a credit. Forty credits is the maximum that means one is fully insured by Social Security, so it used to take 10 years of work to reach that level. Since 1978, however, employers report earnings only once a year, and credits are based on a person's earnings. As of our date of publication, $1,260 of covered earnings in a year will earn a worker one Social Security credit. $5,040 of covered earnings will earn a worker four Social Security Credits, the maximum for any one year. (The earnings figure can change from year to year.)

Keep in mind, only income that is subject to the Social Security tax counts toward your Social Security earnings. Sources of income like dividends on investments and interest on savings do not count toward Social Security. Due to the change in rules, you could earn enough in one quarter to earn one year's worth of credits. If you have a high-paying job you could earn your 40 credits over 10 years with only 30 months of actual work instead of 120.

## Reading Check

After coming home late from his lodge meeting, Bernie notices his wife, Ethel, sifting through a stack of papers, deep in thought, tapping a pencil on a notepad. When Bernie asks Ethel what she is doing, she says she wants to make sure they both have enough credits to start receiving full Social Security retirement benefits. Unsure of the answer, Bernie gives you a call to see if you know anything about Social Security credits, since you have recently started collecting your Social Security. What would you tell Bernie and Ethel?

## 1.3 Determining Full Retirement Age

Many of the people retiring today are eligible to receive their full retirement benefits at age 66. But it's different for people born after 1954. Use the chart below to confirm your Full Retirement Age, based on your year of birth.

*Fig. 1.1*

| Year of Birth* | Full Retirement Age |
|---|---|
| 1937 or earlier | 65 |
| 1938 | 65 and 2 months |
| 1939 | 65 and 4 months |
| 1940 | 65 and 6 months |
| 1941 | 65 and 8 months |
| 1942 | 65 and 10 months |
| 1943–1954 | 66 |
| 1955 | 66 and 2 months |
| 1956 | 66 and 4 months |
| 1957 | 66 and 6 months |
| 1958 | 66 and 8 months |
| 1959 | 66 and 10 months |
| 1960 and later | 67 |

**If you were born on January 1, you should base your FRA on the previous year.*

Full Retirement Age is part of the formula used to determine your retirement benefit. However, your FRA is not necessarily the optimal time for you to elect your benefit. Choosing when to start your benefit is a personal decision. The economic impact of Social Security on the average retiree's household is remarkable: The average individual lifetime benefit from Social Security is more than $300,000. It is especially important for couples to understand the impact of Social Security planning to ensure that if one spouse dies, the surviving spouse has enough income.

## Reading Check

Use the chart above to determine the Full Retirement age of Betty and Sue in the following example:

Betty and Sue are two sisters who are planning to retire soon. After discussions with their retirement planner and Certified Financial Planner™ professional, they both realize that figuring out their Full Retirement Age is the first step in determining their possible Social Security benefits. Betty was born on November 1, 1954. Sue was born four years later on June 15, 1958. At what age does Betty reach her Full Retirement Age? When does Sue reach her FRA?

## 1.4 Estimating Retirement Benefits

The Social Security program bases your monthly retirement benefit on your lifetime earnings history. To determine this information, the Social Security Administration (SSA) performs a series of calculations. These calculations include adjusting or indexing your actual earnings to account for changes in average wages since the year they were earned. The SSA uses data from at least 35 years (picking your highest-earning years and using $0 for any years missing earnings data). All of this data is used to determine your monthly retirement benefit, or Primary Insurance Amount (PIA).

You don't need to do the research to understand how the SSA arrived at your personal Primary Insurance Amount. There is a much easier way to find your PIA: You can request a Social Security Earnings Report online, or in print.

**HOW TO OBTAIN A SOCIAL SECURITY EARNINGS REPORT***

1. **Go to ssa.gov.**
2. **Sign in or create an account for "*my* Social Security."**
3. **Get a Personal Social Security Statement, which includes an earnings record, estimates for retirement, and estimates for disability and survivors' benefits.**

**OR**

1. **Go to ssa.gov.**
2. **Fill out Form SSA-7004 (Request for Social Security Earnings Information).**
3. **Mail the completed form, supporting documents, and applicable fee.**

**See Appendix A in **The Complete Cardinal Guide** for an example of a detailed Earnings Report.*

High earners may find that only a portion of their income has been taxed for Social Security purposes over the years. This inherently limits the amount that Social Security will pay out. If you have earned above the Social Security taxation limit for 35 years you will receive the Maximum Benefit. This limit grows from year to year with inflation or by legislation. For 2016, the maximum amount of taxable earnings is $118,500. **The *Maximum Benefit* is the highest amount of money that Social Security will pay a person, and that number is based on the amount of taxes they paid in to Social Security**.

## Reading Check

What is the easiest way to learn how much your Social Security check will be?

While attending a baseball game with your friend Alfred, he mentions that he is helping his nephew, Bruce, to estimate his retirement benefits. Alfred tells you they both have been struggling to figure out what Bruce's Primary Insurance Amount would be. What would you tell Alfred? How should Alfred and Bruce find out this information?

## 1.5 Benefit Reductions

Choosing to start receiving Social Security early will reduce your monthly benefit. If your Full Retirement Age is 66 but you elect to begin before you reach that age, you will receive only 75% of your benefit instead of the full amount.

*Fig. 1.2 Benefit Reduction*

| Age | Benefit | Reduction |
|---|---|---|
| 62 | 75.00% | 25.00% |
| 63 | 80.00% | 20.00% |
| 64 | 86.70% | 13.30% |
| 65 | 93.30% | 6.70% |
| 66 | 100.00% | 0.00% |

If you receive spousal benefits earlier than your Full Retirement Age, you will also receive a reduced amount for the rest of your life. Spousal benefits exist to compensate the lower-earning spouse who, for example, might have stayed home raising children for a number of years, thus creating a low lifetime earnings amount. The lower-earning spouse can claim benefits based upon the earnings of the higher earner.

*Fig. 1.3 Spousal Benefit Reduction*

| Age | Benefit | Reduction |
|---|---|---|
| 62 | 35.00% | 15.00% |
| 63 | 37.50% | 12.50% |
| 64 | 41.70% | 8.30% |
| 65 | 45.80% | 4.20% |
| 66 | 50.00% | 0.00% |

## 1.6 Survivor Income Planning (Early Death)

For couples, the reality that one of you may predecease the other is stark. On top of having to adjust to the distinct day-to-day changes in your life, the Social Security Administration has a different set of rules for survivors. A survivor's benefit is a payment provided to widows, widowers, and surviving divorced spouses. This monthly benefit is based on the deceased spouse's or ex-spouse's earnings history. Unlike basic Social Security retirement benefits, survivor benefits can start as early as age 60 (or as early as age 50 if the surviving spouse is disabled). Similar to starting basic Social Security benefits early, if you start survivor benefits prior to your Full Retirement Age you will be paid a reduced benefit. Waiting until your Full Retirement Age to begin receiving your survivor benefit will prevent your monthly payment from being permanently reduced.

## 1.7 Marriage Status and Survivor Benefits

There are some specifics you need to know if you no longer have a spouse that you were married to for at least 10 years and divorced, or if you are a surviving spouse.

Remarrying could prevent you from collecting benefits on a past spouse, depending on when you remarry.

- If you remarry before you reach age 60 (50 if disabled), you cannot receive benefits as a surviving spouse while you are married.

- If you remarry after you reach age 60 (50 if disabled), you can continue to qualify for benefits on the deceased spouse's Social Security record.

If you are a widow or widower, of any age, and care for the deceased's child who is under 16, you should be eligible to collect a survivor benefit. Different rules apply for Social Security benefits if there are minor or disabled children involved.

Divorce and survivorship present complicated scenarios. Always make sure to get personalized advice from a qualified advisor or Certified Financial Planner™ professional. Many of our clients have tried to research these situations on their own, or have copied the same decision as an older coworker. This shortcut style of planning often results in a loss of thousands of dollars and leaves them ill prepared for retirement.

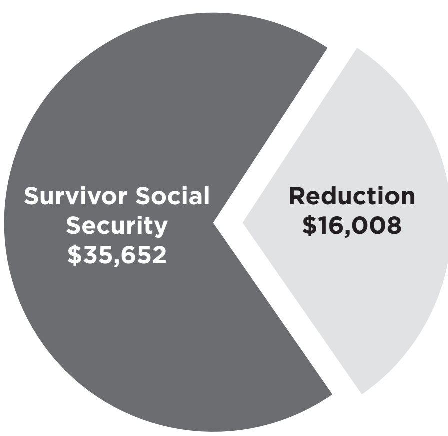
## 1.8 Survivor Income Planning (Late Death)

You pay in to Social Security your entire working life. It is often discussed in the same context as life insurance. This leads some people to believe that when they die, the Social Security Administration will provide their loved ones with a lump-sum payout like life insurance. This is not true. There is no balance and the only death benefit Social Security offers is a one-time payment of $255. Even this small payment is subject to additional restrictions that limit who can qualify and receive it.

If you and your spouse are already receiving Social Security retirement benefits, whichever payment is larger will be paid as the survivor's benefit to the widow or widower. The lower benefit will no longer be issued. This could decrease the income of the surviving spouse by as much as 50%, while their expenses would typically decline by only 30%. Planning ahead to provide sufficient survivor income from investments, annuities, or life insurance can help prevent a financial hardship on your loved one.

In the example below, a couple's combined Social Security income is $51,660. One spouse's income is $2,971 per month, while the other's is $1,334. As illustrated in the pie graph, when one spouse dies; the lower check, $1,334 (equal to $16,008/year), will go away. It does not matter which spouse dies; the remaining spouse will get to keep the higher check. The death of the spouse creates the need to replace the $16,008 that is taken away. We've multiplied this amount by 10 and 15 to show how much income would be lost to the surviving spouse over that many years. This income would not have to be made up if a life insurance policy had been bought to automatically replace the lost income.

*Fig. 1.4 Starting Household Social Security: $51,660*




| Plan for an after-tax amount of: | Plan for an after-tax amount of: |
|---|---|
| $160,080 | $240,120 |
| **To replace lost income for:** | **To replace lost income for:** |
| 10 years | 15 years |

## Reading Check

Roger's wife, Sarah, recently passed away. Roger has been trying to determine whether or not Sarah had a remaining balance of Social Security benefits. He believes that he should be able to receive a large lump-sum payment. Is Roger correct in his thinking? How could Roger and Sarah have better prepared for this situation?

During your weekly dinner with your friends Myrtle and Murray, they mention that they have been preparing in case one of them passes before the other. Murray believes the survivor would get both his Social Security retirement check as well as Myrtle's. Myrtle believes that if Murray were to pass before she does, she would only keep her own Social Security check, which is smaller than Murray's. Which one of them is right?

## 1.9 Putting It All Together

The goal of Social Security planning is to maximize the benefit for you and your family. Using your Primary Insurance Amount and demographic data, professionals can use a maximization formula to make recommendations. The maximization process involves a fair amount of calculus (think back to optimization word problems!). Instead of bogging you down in a series of complicated calculations, let's focus on how the inputs affect the formula.

Keep in mind that any mathematical projection will only be a best guess, because it has to use assumptions like life expectancy. It is difficult to determine how long someone is going to live—no one can predict the future. Social Security maximization relies upon estimates, including your life expectancy and your Primary Insurance Amount, with the goal of finding the best path to maximizing your and your family's lifetime benefits.

Using the Life Expectancy Table below to estimate your own life expectancy will give you a good starting point. As with golf, "handicapping" the estimate by working in your own personal history can provide a better understanding of your potential life-span. If you or your family has a shorter than average life expectancy, consider reducing your estimate. Likewise, if your family has a history of longevity, then increase your estimate.

*Fig. 1.5*

| | First to Die | Second to Die |
|---|---|---|
| Couple, age 55 | 18.6 to 23.7 years | 31 to 35.6 years |
| Couple, age 60 | 15.1 to 19.6 years | 26.6 to 30.9 years |
| Couple, age 65 | 12.1 to 15.8 years | 22.4 to 26.2 years |
| Couple, age 70 | 9.4 to 12.3 years | 18.4 to 21.8 years |
| Couple, age 75 | 7.1 to 9.2 years | 14.7 to 17.6 years |
| Couple, age 80 | 5.2 to 6.7 years | 11.3 to 13.8 years |

Estimating your life expectancy is the key to maximizing Social Security benefits. Those who are likely to live well into their 80s will benefit from delaying their retirement benefits, but may forego income when they are younger and more active. You will need to balance the mathematical recommendation with your own needs. The mathematical process of maximization cannot account for all the nuances of your family's needs and desires.

## Reading Check

If a person's family has a history of health problems, how should they project their life expectancy? How might that projection change if someone has a history of longevity in their family? Why is maximization a difficult process?

## 1.10 Maximizing Benefits for a Couple Age 65

In our era of continuous technological advancement, people find themselves with many more tools at their disposal. Sophisticated software once restricted to professionals is now available online for direct consumer use. These new websites help individuals acquire personalized information regarding benefit maximization. By adjusting the input variables, such as life expectancy and retirement date, you can review different potential outcomes.

In the following example, Michael and Jenny are interested in maximizing their benefits from Social Security. This is what we know about Michael and Jenny:

| | | | | |
|---|---|---|---|---|
| Male | Age 65 | Good Health | Benefit @ FRA: $2,400 | Life Expectancy: 87 |
| Female | Age 65 | Good Health | Benefit @ FRA: $1,200 | Life Expectancy: 91 |

## Filing at Full Retirement Age

Both Michael and Jenny are planning to retire at age 66. They can both file at age 66, get their full benefits, and would receive $43,200 in annual Social Security payments. Electing their benefit at Full Retirement Age, they would receive close to $1.411 million dollars from Social Security over the rest of their expected lifetimes. (This calculation assumes that there is a 2.39% cost-of-living adjustment each year.)

This is a considerable amount of income; to replicate these benefits, a conservative couple would need to invest $1,053,990 at 2% interest. A more aggressive couple expecting a 5% return would still need over $750,000 to reproduce the Social Security benefit shown in this example.

## Optimal Filing Strategy

If Michael and Jenny can continue to work at age 66 or delay their Social Security benefits by other means, such as taxable withdrawals and using other kinds of income, they can vastly improve their Social Security income and their overall lifetime benefits.

By deferring their Social Security benefits one year, Michael and Jenny would receive an 8% increase in their monthly benefit ($2,592 and $1,296, respectively). The higher payments could increase their overall lifetime benefit from Social Security. Delaying might not be optimal, however, if there are reasons to think your life expectancy might be shortened. In that case, delaying can reduce your overall lifetime benefit.

## Reading Check

Your friend Gladys has been coming to you for advice about Social Security, since you have retired recently. Gladys asks you what would happen if she and her husband were to start receiving Social Security early. Uncomfortable with giving her that advice on your own, who would you recommend Gladys speak to? If you were to tell Gladys what would happen if she starts her Social Security benefits early, what would you tell her? How could Gladys maximize her benefits?

## Special Filing Strategy: Restricted Application

In addition to the decision on *when* to file, Michael and Jenny need to consider *how* they file for Social Security benefits. If you were born before January 1, 1954, you could have additional filing options like Michael and Jenny. At their Full Retirement Ages, Jenny could elect her own benefit, while Michael could file but restrict his application to only his spousal benefit (50% of Jenny's PIA, or $600.)

Filing a restricted application temporarily lowers Michael and Jenny's annual benefit: $21,600 instead of $43,200. Because Michael is not electing his own benefit, his own benefit will increase annually at 8% per year, up to $3,168 per month at age 70. The total annual income at age 70 would be at least $54,416—more than 20% higher than if Michael and Jenny elected their own benefits at age 66.

The Bipartisan Budget Proposal Act of 2015 limited the use of restricted applications, and all but eliminated the "file and suspend" strategy. You may not qualify for these strategies.

## 1.11 Paying for Long-Term Care Expenses with Social Security

One of the most important reasons to maximize your Social Security benefit is to provide the maximum amount of monthly income should you require long-term health care. Most people who receive long-term care receive Social Security benefits. These benefits can provide a consistent stream of income that can be put toward care. However, given the current cost and inflation figures for long-term care, your check will not cover all of your costs.

When Social Security retirement benefits are not enough to pay for long-term care, the gap will have to be filled with other sources of income. Some people choose to purchase insurance policies designed to pay privately for care. Private pay options include indemnity policies, short-term and long-term care insurance policies, or accelerated payments from life insurance or annuity policies.

If you find yourself in a position with no other resources to pay for care, programs like Medicaid are able to provide additional funding. Medicaid is administered by each state, and many states require you to assign your Social Security retirement benefit to the state or a third-party health-care company to qualify. This is in addition to stringent financial requirements to "spend down" your assets. (The Veterans Aid and Attendance program does not have the spend-down requirement as of this writing. For more on that program, see chapter 4 in ***The Complete Cardinal Guide***.)

Medicaid planning is extremely complex, with state-specific rules. Consider seeing an attorney who specializes in asset protection and Medicaid qualification. Consulting an attorney and a Certified Financial Planner™ professional together will help provide an additional level of security to an asset protection plan with a contingency for long-term care funding.

## Reading Check

Why is it important to maximize Social Security retirement benefits? What are some of the private pay options that are available to people preparing for long-term care? How do Medicaid and Social Security interact with each other in regards to long-term care?

Cornelius and Arthur are having a conversation while fishing early one morning. Cornelius tells Arthur that his kids have been worrying him about long-term care. Arthur tells Cornelius not to worry about it, since Social Security would pay for it. Is Arthur right? Explain.

# Preparation for Social Security Planning

**OBTAIN A SOCIAL SECURITY EARNINGS REPORT FOR YOUR SPOUSE (IF APPLICABLE) AND YOURSELF.**

**On page 2, full retirement age is**

Self: ..................................................................

Spouse: ..............................................................

Projected retirement date: ......./......../20..................

Spouse: ......./......./20..................

Do you or your spouse plan to work ........ part time or ....... full time in retirement?