



## **For Those Who Want to Prosper & Thrive in Retirement**

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Provided to you by:

**Victoria Woods & Damon King**

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405-348-0909



# **For Those Who Want to Prosper & Thrive in Retirement**

Written by Financial Educators

Provided to you by

**Victoria Woods & Damon King**  
**405-348-0909**

# The Four Important Financial Issues for Retirees

In this short booklet, we cover the most important issues:

- How to generate sufficient retirement income
- How to maintain affordable health coverage
- How to maintain your independence at advanced ages
- How to best leave assets to heirs

We can only touch on the major aspects of each issue and you're invited to phone us with your questions or concerns. Of great importance is to remember that you will likely live longer than you may realize. Here are the life expectancies for specific attained ages:

If you have reached age....	The AVERAGE person can expect to live this number of additional years...
65	21
70	17
75	13
80	10
85	8
90	5
100	3

Please keep your long life expectancy in mind when considering the issues in this booklet.

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<sup>1</sup>IRS Publication 590, Appendix C, Table 1 January 5, 2014

# Having Sufficient Income

Many retirees want to generate sufficient income so that they never need to consume their principal. In fact, most invest in a manner that will increase the probability of using their principal. You may be doing this also. Many retirees think that they must keep their principal safe and available, so they invest in low yielding short-term investment such as money market funds and CDs.

These investments pay a very low return, but they are highly liquid. They include the following:

- Savings accounts
- Checking accounts
- Treasury bills
- Money market accounts

Most retirees are lulled into the false safety of these investments. Let me show you why. First, let's take a look at bank accounts. Bank investments typically pay 2% or less. After you subtract taxes and inflation, you have a negative return.

**Interest CD:** 1.15%<sup>2</sup>

**Income Taxes:** .34%<sup>3</sup>

**Consumer Inflation:** 1.30%<sup>4</sup>

**Net real return to you:** -.49%

You must remember that while your money sits in a savings or money market account for the year, the prices at the supermarket are rising 1-2%. This inflation must always be subtracted from any investment return so that you see how much you are really ahead. In the case of the savings account, you're not ahead – you're behind! Economists call this the “real return,” because it represents what you are really receiving.

So why do retirees have such a preference for investments with a negative return? First, most retirees do not even realize that they have a negative return. Secondly, retirees like the flexibility of having the money liquid in case of an “emergency.” What type of an emergency do you anticipate? Ill health? A nursing home stay? These concerns are legitimate. The cost of these catastrophes is so great that retirees could quickly wipe out their \$200,000 in savings in order to cover costs (e.g. cost of average stay in a nursing home is 29 months x \$7200 per month = \$208,800).<sup>5, 6</sup>

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<sup>2</sup> CIT Bank 12/28/14, \$25,000 deposit, 1 year CD, [www.bankrate.com](http://www.bankrate.com). CDs are subject to availability and this does not constitute an offer to buy or sell.

<sup>3</sup> 25% federal tax bracket for 2015 applies to single taxpayers with taxable income from \$37,450 to \$90,750, and married taxpayers filing jointly with taxable income from \$74,900 to \$151,200, and additional 5% state income tax is hypothetically assumed.

<sup>4</sup> <http://bls.gov/news.release/cpi.nr0.htm> November 2014, increase in CPI previous 12 months.

<sup>5</sup> Genworth Long Term Care Costs - Cost of Care Survey 2014 Survey calculations based on private room rates of 14,800 long term care providers in 440 regions nationwide.

[https://www.genworth.com/dam/Americas/US/PDFs/Consumer/corporate/130568\\_032514\\_CostofCare\\_FINAL\\_nonsecure.pdf](https://www.genworth.com/dam/Americas/US/PDFs/Consumer/corporate/130568_032514_CostofCare_FINAL_nonsecure.pdf)

<sup>6</sup> Per American Association of Long Term Care the average length of a nursing home stay is 2.4 years

<http://www.prlog.org/11931514-length-of-nursing-home-stay-varies-according-to-long-term-care-insurance-expert.html>.

Here's another idea to help safeguard your assets. Take the money out of your bank accounts, invest it for a potentially higher return (e.g. 3% from a federally and state tax exempt bond) and then use this extra income to get insurance for health care and long-term care insurance that could protect you in case of an emergency.

**Municipal Bond:** 3.0%<sup>7</sup>

**Income Taxes:** 0.00

**Consumer Inflation:** 1.3%

**Net real return to you:** 1.7%

\$200,000 invested x 2.19% (difference between CD and municipal nominal after-tax interest rates) = \$4,380 annually to pay for quality long-term care and health insurance (the premiums for these insurances may be tax deductible).

*Investments in any security involve fluctuation and may result in a loss of your investment; while CDs are FDIC-insured, municipal bonds are not. Additionally, the purchase and sales of municipal bonds may incur commissions, and municipal bonds may not be as liquid as CDs. If sold prior to maturity, municipal bonds may return more or less than your original investment. Such bonds may not be appropriate for every investor, and you should only make investments appropriate for your circumstances.*

When most people stop to think this through, they'll realize the following – they have money that they consider to be core capital. In fact, for many of us, our core capital is money that we intend to never spend. It is money that we keep working; money that we depend on to generate either interest or dividends.

Our core capital should be designed to outlive us. In fact, it's important for you to start thinking about your money in terms of it outliving you, not the other way around. You don't want to outlive your money. That makes for a very difficult existence. Your money should actually be invested for a period longer than your life expectancy. That's the only way it will outlive you, and that's the way it should be planned. Unless, of course, you think that you can time it perfectly to die when all of your money runs out. But I don't think your timing is that good.

So, your objective should be to have your core capital earn the highest possible rates with appropriate safety. By planning to have your money outlive you, you can make sure that your money will be working and providing for you until the day you go to a better place. The last thing you want to worry about is money when you retire. The one way to improve your chances for a bright financial future is to start putting your money to work for you now.

When looking at bonds, consider investing in longer-term bonds to potentially increase your interest income. The objective for your core capital is to have it conservatively earn as high a rate as possible without taking undue risks.

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<sup>7</sup>Average rate on AA rated 20 year municipal bonds, FMSbonds.com 12/28/14. Note that the interest on municipal bonds is free from federal income tax and likely also free from state income tax if the owner resides in the state of issuance. It is possible that such interest could be subject to AMT or taxable as ordinary income from private activity bonds.

# Annuitization

If “annuitization” is a new term for you, you will be hearing it more and more. The idea is to use your principal to supplement your spending money – but do so in a way that the principal lasts as long as you do. Many people will have no choice but to use their principal to sustain themselves, and this is not a bad thing as long as it is done correctly. Since you can never be sure how long you’ll last, the insurance industry provides some assistance with life annuities. You receive payments for as long as you live.

Here’s how it works. In exchange for a single payment, the insurance company will immediately start making monthly payments to you. Part of these payments is considered income and part comes from your principal investment. These payments can last for a term of years or even for your lifetime if you so choose. Note that life annuity payments could incur premium taxes in some states. Maintenance expenses and contract fees charged by the insurance company could also reduce your payments – but when you get a quotation, it will be net of these expenses.

The amount of money you receive each month is dependent on several factors, including your estimated life expectancy, the amount of money you have invested, and the current interest rate being paid by the annuity company (which is locked in at the time of purchase). The payout will typically be higher the older you are because the insurance company does not expect to have to make payments as long as they would to a younger person. Assuming that you have chosen the lifetime payment option, your annuity company will continue to make payments to you even if you live past your normal life expectancy.<sup>8</sup>

If you die sooner, the insurance company keeps the balance of the annuity if you selected lifetime payments. You may also be able to elect to receive a lower payment in exchange for having the payments continued to your heirs until the entire amount of your original premium has been paid out. For whom may a fixed immediate annuity be suitable?

- A retiree needing increased monthly cash-flow
- A person with no heirs or who is not concerned about leaving an estate
- Someone who has set aside other funds to leave to heirs if they desire to leave an inheritance
- A retiree desiring the fixed payment and wanting to avoid maturities, rolling over investments, and the maintenance and administration required of investing on one’s own

## What can you expect to receive on an immediate annuity?

<b>\$100,000 Premium, Male</b>	
<b>Age</b>	<b>Monthly</b>
65	\$572
70	\$663
75	\$788

Life annuity payments, Comparative Annuity Reports, December 2014  
<https://www.immediateannuities.com/comparative-annuity-reports/>

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<sup>8</sup> Subject to the claims-paying ability of the insurance company, please note immediate annuities are designed to enhance cash flow and save taxes but are not the only investment vehicles by which these goals may be achieved. Immediate annuities cannot be surrendered for value. Always consider all possible investment options before you invest.

# Health Insurance

The health insurance scenario for retirees is scary. You read and hear a lot about Medicare running out of money and benefits being cut. Seniors have been asked to pay for more for their Medicare benefits. The good news is that through a better understanding of your options, you can secure some peace of mind knowing that you have selected appropriate health coverage.

No retiree should rely on Medicare alone. You must have supplemental coverage – as Medicare typically pays 80% of your health care costs. That 20% that you must pay can be a very large sum if you have a serious illness.

The AARP conducted a study titled: *An Assessment of Medicare Beneficiaries' Understanding of the Differences between the Traditional Medicare Program and HMOs*. The findings<sup>9</sup> indicated that only a fraction of the total beneficiary population (11%) had "adequate" knowledge to make an informed choice between HMOs and regular Medicare. Therefore, it is important that you understand how you can receive proper medical coverage.

Medicare offers different ways to get health care benefits. Once you understand what you get, you can then get the appropriate coverage for what Medicare does not provide. The Medicare coverage options depend on which plan you select. And based on where you live, you may have more than one plan to choose from (note that available plans can vary from zip code to zip code)!

There are two basic Medicare health plans (see next page for table with breakdown):

- Medicare + Choice plans include Medicare Managed Care Plans and Medicare Private Fee-for-Service plans. These plans provide care under contract to Medicare. They may offer benefits such as coordination of care or reducing out-of-pocket expenses. Some include additional features, such as prescription drugs. The availability of plans vary among geographic areas. Many people loosely refer to all of these plans as "HMOs."
- The Original Medicare Plan (sometimes called fee-for-service) – everyone with Medicare can join the Original Medicare Plan that is available nationwide. Many people in the Original Medicare Plan also have a Medigap (Medicare Supplemental Insurance) policy or supplemental coverage, provided by their former employer to help pay health care costs that this plan does not cover. This supplement is a separate policy which we will discuss shortly.

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<sup>9</sup> <http://www.aarp.org/research/ppi/health-care/medicare/articles/aresearch-import-595-9805.html>.

## Medicare Comparison Table

	Medicare Advantage		
	Original Medicare Plan	Managed Care Plan	Private Fee-for-Service Plan
<b>Costs</b> Total Out-of-Pocket Costs	<b>High</b>	<b>Low to Medium</b>	<b>Medium to High</b>
<b>Extra Benefits</b> In addition to Medicare covered benefits.	<b>None</b>	<b>Most</b> May offer prescription drugs, eye exams, hearing aids, or routine physical exams.	<b>Some</b> Possibly foreign travel or extra days in the hospital.
<b>Doctor Choice</b>	<b>Widest</b> Choose any doctor or specialist who accepts Medicare.	<b>Some</b> Usually must see a doctor or specialist who belongs in your plan.	<b>Wide</b> Choose any doctor or specialist who accepts the plan's payment.
<b>Convenience</b>	<b>Varies</b> Available nationwide.	<b>Varies</b> Available in some areas. May require less paperwork and have phone hotline for medical advice.	<b>Varies</b> Available in some areas. May require less paperwork and have phone hotline for medical advice.



## Why Would Retirees Want Medigap Insurance As Opposed to An HMO Arrangement?

With a Managed Care Plan, you don't need to buy Medicare Supplemental (Medigap) insurance. This could result in several thousand dollars of savings each year. In fact, some Managed Care Plans may have no monthly premium at all.

There are potential repercussions, though, that could make you wish that you would have spent the additional money for the insurance and stuck with traditional Medicare.

The companies sponsoring a managed care plan might limit the number of doctors, hospitals, and other health care providers within the network. Also, they can abandon the Medicare benefits program if the insurance network finds it unprofitable. This could leave you with significantly higher out-of-pocket expenses, especially if your health has declined.

The government can create another problem if you are not happy with managed care. For instance, suppose you cancelled a Medigap policy to join a Managed Care Plan. Medicare could possibly penalize you if you decide that you don't like managed care and try to buy a new Medigap plan. Instead of having a choice of 10 plans, you might only be able to select from four. Consequently, your new policy might not be as good as the one you previously canceled.

Even though Medigap policies will not cover all the gaps in the Original Medicare Plan, they may help retirees:

- Lower their out-of-pocket costs, and
- Get more health insurance coverage

Some examples of Gaps in Medicare covered services.	Amount Clients will Pay in 2015	A Medigap Policy May Help Pay These Costs
<b>Hospital Stays</b>	> \$1,260 for the first 60 days > \$315 per day for days 61 - 90 > \$630 per day for days 91 - 150	Yes
<b>Skilled Nursing Facility Stays</b>	> Up to \$157.5 per day for days 21 - 100	Yes
<b>Blood</b>	> Cost of the first 3 pints	Yes
<b>Medicare Part B yearly deductible</b>	> \$147 per year	Yes
<b>Medicare Part B covered services</b>	> 20% of Medicare-approved amount for most covered services > 50% of the Medicare-approved amount for outpatient mental health treatment* > Co-payment for outpatient hospital services	Yes
<small>*All Medigap policies must pay 50% coinsurance for outpatient mental health treatment services. Source: Centers for Medicare and Medicaid Services <a href="http://www.medicare.gov">http://www.medicare.gov</a></small>		

Source: Centers for Medicare and Medicaid Services <http://www.cms.hhs.gov>

**Note:** Some Medigap policies also cover other extra benefits that aren't covered by Medicare. Examples include:

- Routine yearly check-ups.
- At-home recovery.
- Medicare Part B excess charges (the difference between the doctor's charge and Medicare's approved amount). The excess charge only applies if the doctor doesn't accept the assignment.
- Prescription drugs.

## Maintain Your Independence

Statistics indicate that over half of all people over age 50 will require long-term care. In fact, the most current research statistics are below:<sup>10</sup>

- a 50-year-old has a 53% to 59% chance of ever entering a nursing home before he dies and that conditional on any stay, the average duration is just over a year.
- females face a 64.9% probability of having at least one stay, compared to 49.8% for males
- An earlier study indicated that 1 in 5 that enter a nursing home will need 5+ years of care <sup>11</sup>

With such a great risk, doesn't everyone need insurance? After all, the cost of long-term care can run \$7,200 or more monthly in some locations. So if you have an extra \$200,000 to \$300,000 to pay for long-term care, you can self insure and just pay out-of-pocket in case of mental or physical incapacity.

But if you want to remain in your home, get quality in home care and do not have plenty of excess funds, then you want insurance.

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<sup>10</sup> National Bureau of Economic Research June 2013 <http://www.nber.org/chapters/c12970.pdf>

<sup>11</sup> Penn State University Policy Research Institute 3/2/06

## How to Leave Assets to the Heirs

This whole arena of asset protection would be incomplete if I didn't include a small section devoted to estate planning. Many people not only want to protect their assets for themselves, but also for their heirs. If you do not plan ahead, it's easy to watch estate taxes and poor planning rip away the value of your estate.

First, let me mention a big mistake I see most retirees make regarding estate planning. Many times, I see a single retired individual who makes an investment. Then he or she puts the name of his or her son or daughter on it as a joint tenant because he or she knows that when he or she passes away, his or her son or daughter will then inherit that asset automatically. This is true.

However, such superfluous estate planning can lead to a very severe problem. If that son, for example, happens to be a physician and gets sued for malpractice and the son's assets get attached, legally, the son appears to own half of your investment because your son's name is on it.

As a result, your son's creditors could attach that money, which is yours. So, you may not want to expose your assets in that way, and I strongly advise that you don't. Instead, you probably want to own the investment in just your name, passing it by will, or have a living trust created so that the name of your trust is on the assets at all times. In this way, you don't have exposure to the creditors of your sons or daughters, and everything is well protected. Additionally, with living trusts you also avoid probate for very quick and immediate transfer to your heirs.

There are some basics that you need to understand about estate planning. Currently, every individual is allowed to pass \$5.43 million of assets to his or her beneficiaries without gift or estate tax (as of 1/1/15, indexed for inflation in future years).<sup>12</sup> Be aware that tax laws, exclusions and estate exemptions are subject to change. Now, there's another great mistake that a lot of married retirees make. Say the husband has a will and he leaves everything to his wife. The wife has a will and she leaves everything to her husband. Here's the problem that maybe you've never been told before. Each of us has \$5.43 million exclusion on passing along assets to our heirs, or we can leave our exclusion to our spouse. The most important word in that sentence was "or," because if you leave your assets to your spouse, you've lost your exclusion.

Generally, when an attorney draws up a living trust or will for you, what happens is that he or she segregates the exclusion amount of assets directly to your heirs, not to your spouse, so that you, in fact, get the full benefit of your exclusion. This way, if you're married, you get the exclusion of \$5.43 million, your spouse gets \$5.43 million, and a married couple can pass a \$10.86 million estate to their heirs with no estate taxes. That's exactly what you want to do. For people whose estates are larger, you definitely want to consider the idea of using some type of insurance to pay your estate taxes.

Let me give you an example, and note that this is a hypothetical example that does not reflect any particular products. Let's say you and your spouse have the fortunate situation of a \$12 million estate. Now, that may not be the current value of your estate, but you've got to remember, if you're 65 years old now, it's very likely that one or both of you might live to age 85 or even longer<sup>13</sup>. So, the question is, not what is your estate worth today, but what will it be worth in 20 years?

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<sup>12</sup> IRS <http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Estate-Tax> October 20, 2014

<sup>13</sup> IRS publication 590 <http://www.irs.gov/publications/p590/ar02.html> shows a 26 year life expectancy for a couple both age 65

But let's say you have the terrible misfortune of an early death. In that case, the first \$10.86 million is not going to be subject to estate tax, but the other \$1.14 million will, and unfortunately, the estate taxes are very high. On \$1.14 million, you'd pay \$456,000, for estate taxes.

**Total estate:** \$12 million

**Potential exemption from tax:** \$10.86 million

**Taxable estate:** \$1.14 million

**Estate tax due:** \$456,000<sup>14</sup>

Who pays that? Actually your heirs do. It comes right out of their inheritance. So, how do you protect it? It may be very useful to invest in an insurance policy for you and your spouse in the amount of \$456,000. What specifically would you do?

The first step is for you to get a quote on what it would cost you to buy an insurance policy for \$456,000. Let's just assume that would cost you \$6,080 a year.<sup>15</sup> You would have to deposit that in premiums each year.

Now, before you shudder, "That's ridiculous," remember you're going to be saving \$456,000. So let's just see if you can, in fact, pay your estate taxes for a heck of a lot less than \$456,000.

Let's say you can go out and get an insurance policy for yourself. The annual premium is \$6,080 a year. What you do is take \$6,080 a year and you gift it to your children, or you can use an irrevocable life insurance trust. (Preparation of trusts can incur significant expenses). The gift helps you reduce the size of your estate and in itself reduces your estate taxes.

Your children then pay the premium on the insurance policy so that your children actually own the insurance policy. It is critical that your children or someone other than you and your spouse own the insurance policy. (In fact, if you have life insurance policies right now that you own, please see your attorney, financial advisor or insurance agent, or contact us right away about why these policies must be owned outside of your estate.)

When you have passed away and the IRS comes knocking for \$456,000 in estate taxes, the children merely take the \$456,000 they've received from the life insurance company, turn around and pay the IRS and the entire \$12 million estate passes to them unencumbered by estate taxes and any other liens or taxes. What were the premiums to the insurance company? Approximately \$127,680 (\$6,080 annually for 21 years, the life expectancy of a 65-year-old). However, the premiums in your situation could be higher or lower depending upon your age, your health, the company that places the policy, future interest rates, and your actual longevity.

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<sup>14</sup> IRS Instructions for form 709, 2014 [www.irs.gov/pub/irs-pdf/i706.pdf](http://www.irs.gov/pub/irs-pdf/i706.pdf)

<sup>15</sup> Genworth Life and Annuity Insurance Colony Term 10 12/23/14, Male, age 70, Florida resident rated preferred plus. The purchase of life insurance involves costs, fees, expenses and potential surrender charges and depends on the health of the applicant. Not all applicants are insurable. If a policy is structured as a modified endowment contract, withdrawals will be subject to tax as ordinary income and withdrawals prior to age 59 ½ are subject to a 10% penalty

So, that's the way to pass a sizeable estate to your heirs and avoid as much estate tax as possible. You can do this by doing what the wealthy do – using life insurance to pay the taxes.

Instead of paying almost \$456,000 out of pocket, you have paid \$127,680 for insurance premiums. A savings that is hard to beat! Remember, the figures will vary in each situation, and this is a realistic but hypothetical example of how to use insurance to pay estate taxes. (Note that the time value of money has not been considered in this analysis).

Even if you have a modest estate and estate taxes are not a concern, there are several other planning concerns involving wills and trusts, medical wills, living wills, and directives for health care and powers of attorney. Please contact us for a complete review of your financial situation so you can make the best possible decisions concerning your retirement planning and wealth preservation strategies.

## About Victoria Woods & Damon King



Victoria Woods is Chief Investment Advisor and President of ChappelWood Financial Services. As a premier advisor to affluent clients for over 25 years, she is recognized as a leader in the Investment Advisory industry. You may have seen her featured in Newsweek magazine's "Financial Planning Guide". She is the author of the book *It's All About the \$Money, Honey!* and has appeared on the Today show, Fox News, Fox Business, and CBS, NBC, and ABC affiliates across the nation. She can be heard on NewsRadio 1000 KTOK as host of "It's All About the \$Money, Honey!" Saturdays at 4:00 p.m. and Sundays at 6:00 a.m. Clients have benefited from Victoria's experience in working with High Net Worth households and Mid-Tier Millionaires.

Damon King, CFRE is an Advisor with ChappelWood Financial Services. Regarded as a leader in the charitable planning community as a fundraising professional by his peers and donors, he continues his work as a financial advisor developing strategies for affluent households to achieve their financial goals and preserve their values and legacy for future generations. You may have heard him as a co-host on "It's All About the \$Money, Honey" on NewsRadio 1000 KTOK. Individuals and families have used Damon's advice to establish tax-efficient gifting strategies, guarantee lifetime income, and preserve family wealth.

# About Financial District of Oklahoma - ChappelWood Financial Services

ChappelWood Financial Services is a premier Independent Registered Investment Advisory firm that was founded more than 25 years ago by our Chief Investment Advisor, Victoria Woods. Our success has been built on long term client relationships, our reputation, and consistency.

- **Customized Financial Solutions** - Mid-Tier and potential Mid-Tier millionaires; those seeking comprehensive income solutions, estate planning services, asset management, and tax preparation from one provider.
- **Retirement Planning** - Accumulation (IRA, Roth IRA, 401k), Protection, Distribution, Business Succession Planning, Estate Planning, Life Insurance Analysis, Document Vaulting
- **Financial Services** - Investment Management Analysis, Comprehensive Financial Plans, Continual Monitoring, College Funding
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- **Goal and Strategy Meetings** - Discovery, Clarity, Implementation and Monitoring; Cash Flow and Net Worth Analysis, Re-balancing, Access to a Financial Advisor Team

**Phone today with questions or to see if we can help you.  
There is no charge for an initial meeting.**

**Victoria Woods & Damon King**  
405-348-0909

**Financial District of Oklahoma - ChappelWood Financial Services**  
office@ChappelWood.com  
1725 East 15th Street  
Edmond, OK 73013

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