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Should I Use My IRA?

LONG TERM CARE PLANNING: SHOULD I USE MY IRA AS A SOURCE OF FUNDING?

by John B. Linvill, Jr., CSA ~ June 26, 2005

Most families will have a meaningful portion of their financial resources in their IRA.

People are just beginning to realize that life expectancies are ever increasing to ages that as few as ten years ago were considered to be very old (78-80 years of age).

Now, many parents of the baby boomers are often living well into their 80 and 90s. The number of centenarians (age 100 & up) is growing each year. In 1980, there were 15,000 centenarians. In 2000, centenarians totaled 72,000.

Long term care cost is currently rising at 5% annually. Using current costs ($200/day at a Philadelphia assisted living facility providing high-level care), compounding at 5%, in 30 years the cost could reach $315,000 annually (for one person, for one year). If 4 years of care are required, the cost could be $1,200,000. Also, consider the healthy spouse who lives for several more years and then needs care. (The above care costs are based upon recent personal facility interviews conducted by the author).

Assuming that my IRA will last into my later years, what is the impact of using my IRA to fund my family's long term care needs?

Distributions from my IRA are fully taxable. A $300,000 annual IRA distribution will be taxed at the prevailing income tax rate. In order to obtain the $300,000 needed annually for home care or for the assisted living facility (more dollars are required for nursing home care) the distributions are as follows: $300,000 for the care cost + an additional $160,000 (representing income taxes on the $300,000 at a 35% tax rate + taxes on the tax dollars, also referred to as a double gross up).

Please consider the financial funding implications should care be required for 1, 2, 3, 4, 5, 6……10 years or more (severe dementia). How long will the IRA last?

If one has other long term care funding resources, the IRA may be preserved and structured as an Inherited IRA – providing decades of tax deferred growth for the children and grandchildren, a very powerful legacy.

If you do not want to use your IRA for potential long term care needs, which financial resources are you setting aside? Even taxable resources will most likely be subject to capital gains tax.

The easiest and most cost effective funding strategy is to establish a ***special pool or fund*** known as a long term care insurance policy. A properly structured policy with 5% compounded inflation capability will pay massive dollars should the need materialize. Even with a carefully designed long term care policy, one cannot be sure that the daily or monthly benefit will keep up with the future cost of care.

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Inflation calculations are based upon current economic statistics and estimates for the Philadelphia area.