

§ 75-3-917; Va. Code Ann. § 64.1-62.4; Wash. Rev. Code ch. 11.108 et seq.

Under the Arm-Wrestle in Court statute, courts are authorized but not required to interpret a formula clause in a manner that is inconsistent with its plain meaning. This allows a surviving spouse left out in the cold by a formula clause to receive assets, but not necessarily at 2009 levels and not without a fight. The Florida statute provides: "In construing the will, the court shall consider the terms and purposes of the will, the facts and circumstances surrounding the creation of the will, and the testator's probable intent. In determining the testator's probable intent, the court may consider appropriate evidence relevant to the testator's intent even though the evidence contradicts an apparent plain meaning of the will." Fla. Stat. §§ 733.1051 & 736.04114. These statutes leave it to the family to battle it out as to what the decedent really wanted, given the mess of estate tax laws. It looks like 2010 is a great year to be a probate litigator in Florida.

Dare we hope Congress will be our fairy godmother? Dream on. Recent proposals from Congress have proven to be less than magical.

One storm on the horizon is Hurricane RETA—the Responsible Estate Tax Act—proposed in late June by Senators Bernard Sanders (I-VT), Tom Harkin (D-IA), and Sheldon Whitehouse (D-RI) and the identical bill proposed in the House on July 15 by Representative Linda Sanchez (D-CA). Some provisions of RETA are relatively unsurprising: a \$3.5 million exclusion, and a progressive marginal rate structure from 45% to 55%. More controversial is the "billionaire surtax" of 10% on estates over \$500 billion. The kicker, though, is that RETA would be retroactive to 2010! Will decedents take this lying down? Will their lawyers?

Another possibility is the Lincoln-Kyl proposal, recently attempted as part of the Small Business Lending Act. Under

this proposal, taxpayers would see an immediate \$3.5 million exemption and 44% rate for transfers over the exemption amount. Over the next five years, the exemption would increase to \$5 million and the top marginal rate would decrease to 35%. The most interesting feature of the Lincoln-Kyl proposal is its *optional retroactivity*, or Pick Your Poison. With the Pick Your Poison feature, estates of decedents dying in 2010 may choose between the rather ugly carry-over basis provisions or the estate tax (and take advantage of stepped-up basis at death).

Other less-than-helpful solutions have included the Family Farm Estate Tax

Relief Act, courtesy of Representative Mike Thompson (D-CA). This act includes an unlimited exemption for farms, which is a loophole large enough to fit the barn. As much as I enjoyed watching Paris Hilton milk cows on *The Simple Life*, encouraging the use of farms as tax shelters for the mega-rich doesn't seem to do much to clean up our estate tax mess.

So as the summer of 2010 draws to a close and many of us take beach vacations and daydream about retirement, I'd encourage everyone to plan for a long, drawn-out retirement ... because the taxes associated with death are too much work. ■

## Social Security Spouse and Survivor Benefits 101: Practical Primer Part II (Or Another Reason to Put a Ring on It)

By Francine J. Lipman\* and James E. Williamson\*\*

As the country and courts continue to debate the importance of marriage in a variety of contexts, when determining Social Security benefits it is clear that *marriage matters*. Marriage matters for Social Security benefits planning because of meaningful spouse and survivor benefits. Given the broad and deep devastation of a record recession on retirement and saving accounts, including the continuing demise of defined benefit plans with joint and survivor benefits protection, Social Security benefits, generally, and spouse and survivor benefits, specifically, have become and will continue to be a more significant percentage of retirees' income. As a result of the interplay between recently phased in changes under 1983 legislation and amendments under the Senior Citizens' Freedom to Work Act of 2000 (2000 Senior Act), it is critical that Social Security benefits timing analysis becomes a more important part of many retirement plans. In this article, we describe how to use these changes to devise strategies to maximize Social Security spouse and survivor benefits.

Despite enhanced Social Security benefits for married individuals (and formerly married individuals with a minimum 10 year marriage), the rate and length of marriage in the United States have been declining, especially for African American women. For an

excellent discussion of this issue, see Madonna Harrington Meyer, Douglas A. Wolf & Christine L. Himes, *Linking Benefits to Marital Status: Race and Diminishing Access to Social Security Spouse and Widows Benefits*, Center for Retirement Research at Boston College,

\*Professor of Law, Chapman University School of Law, Orange, CA.

\*\*Professor of Taxation and Accounting, San Diego State University, San Diego, CA.

2004, available at [www.bc.edu/crr](http://www.bc.edu/crr). As a result, fewer women, who on average live longer and have lower lifetime earnings than their husbands, will qualify for these benefits, and we may experience greater gender and race income inequality among seniors in the future.

Gender and race income inequality among seniors is a tragic problem. Seventy percent of all poor seniors are women. While white married senior men have a poverty rate of only 3%, single senior women suffer a poverty rate of nearly 20%. At the intersection of gender and race the problem of poverty among seniors is staggering. African American and Hispanic single senior women suffer poverty rates near 50%. Because elderly poverty is disproportionately a women's problem, it is not surprising that Social Security spousal and survivor benefits remain the leading source of income for senior women. Social Security benefits represent 90% or more of income for 21% of senior couples, but for single senior women and all African American seniors the percentages skyrocket to 47% and 50%, respectively. Accordingly, Social Security benefits planning, which has become more important for many seniors, is critical for women and people of color.

## The Basics of Social Security Spouse and Survivor Benefits

### Spousal Benefits

The spouse of an eligible worker can receive benefits based upon his own work record or based upon his spouse's work record. If taken before full retirement age (FRA), worker and spousal benefits are reduced permanently. For boomers retiring at age 62 from 2008 to 2016, the worker benefit reduction is 25% and the spousal benefit reduction is 30% increasing gradually to 30% and 35%, respectively, for individuals retiring at age 62 in 2022 or later. Before FRA, the spousal benefit is the excess of one-half of his spouse's worker benefit at

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FRA, the primary insurance amount (PIA), over his own benefit. If benefits are taken at or after FRA, the spousal benefit is 50% of the spouse's PIA. Worker benefits, but not spousal benefits, can receive delayed retirement credits (DRCs) of 8% per year (for retirees born after 1942; retirees born before 1943 enjoyed lower FRAs, but lower DRCs) together with any applicable cost of living adjustments (COLAs). For a detailed discussion of the Social Security Retirement benefits formula, see Francine J. Lipman & James E. Williamson, *Social Security Benefits Formula 101: A Practical Primer*, NEWSQUARTERLY, Summer 2010, at 14.

Spousal benefits are also available to any former spouse from a marriage that lasted at least 10 years. However, if a former spouse remarries (anyone other than the former spouse) and remains married, he cannot claim spousal benefits on any former spouse's record. Spousal benefits from a current spouse can be taken only after the primary worker files for benefits. This requirement and the fact that spousal benefits do not accrue DRCs have motivated many retirees to claim Social Security spousal and worker benefits earlier than age 70. However, the 2000 Senior Act includes a provision that significantly changes this analysis. Under the 2000 Senior Act, upon reaching FRA a worker can file for and then suspend her worker benefit, allowing her spouse to claim spousal benefits, while her worker benefit continues to accrue DRCs up to age 70. If her spouse is at least FRA and claims only his spousal benefit (and not

his worker benefit), his worker benefit will continue to accrue DRCs up to age 70.

### Survivor Benefits

Surviving spouses of deceased workers are entitled to survivor benefits. The amount of the survivor benefit (if claimed after the survivor reaches FRA) will be equal to 100% of the Social Security benefits the deceased spouse was entitled to at death. Therefore, if the deceased's benefits were reduced because of early claiming, the survivor benefits will also be reduced. Alternatively, if the deceased's benefits were increased with DRCs and COLAs, the survivor benefits will be increased. If the deceased spouse had not yet claimed her benefits, survivor benefits will be determined as if the decedent had claimed her benefits at the later of her FRA or her date of death.

Survivor benefits are reduced if the surviving spouse claims the benefit before her FRA. Survivor benefits can be claimed as early as age 60 (age 50 if the surviving spouse is disabled). If survivor benefits are claimed at age 60 they are reduced by 28.5% permanently. This reduction is decreased to zero between age 60 and FRA. A surviving spouse can claim survivor benefits, but continue to let her worker benefits accrue DRCs through age 70. However, if a working survivor claims benefits before her FRA, she will have a payback penalty if her earned income exceeds the annual threshold amount.

Survivor benefits are also available to any former spouse from a marriage that lasted at least 10 years. However, if a former spouse remarries before age 60 and remains married she cannot collect

survivor benefits on any former spouse. If she becomes single again or remarries after attaining age 60 she will be able to collect survivor benefits on a former spouse. Any spouse receiving spousal benefits will automatically have her benefits increased to higher survivor benefits upon the spouse's (or former spouse's) death.

### Spousal and Survivor Social Security Benefit Planning

Given options under the Senior Act of 2000, later FRA, higher DRCs and the record-breaking recession, retirees and their professional advisors should reevaluate Social Security retirement strategies. The Center for Retirement Research at Boston College and the Pension Research Council (see James I. Mahaney & Peter C. Carlson, *Rethinking Social Security Claiming in a 401(k) World*, The Wharton School, University of Pennsylvania (2008), available at [www.pensionresearchcouncil.org](http://www.pensionresearchcouncil.org)) have done extensive analysis regarding these and other Social Security timing decisions and determined that the most likely beneficiaries of this Social Security spousal benefit strategy are two-earner couples with equal earnings records (the higher and the more equal the lifetime earnings, the greater the dollars of increased benefit). Moreover, given the longer life expectancy of women relative to men, the average age difference between spouses, and the higher lifetime earnings of men relative to women, they have determined that the average optimal retirement claiming age is age 62 for married (lower-wage earner, longer-living) women and 69-70 for married men (with the husband claiming any spousal benefits when he reaches FRA). This strategy ensures a generous survivor benefit for the longer-living widow and takes advantage of spousal benefits from the higher-wage earner for the lower-wage earner as well as from

the lower-wage earner for the higher-wage earner.

However, as Garrison Keillor has recognized, most people are above average so please consider the following other-than-average examples.

## Examples of Social Security Strategies

### Harry and Wendy (the Two Wage Earner Couple)

Harry is three years older than Wendy (the average age difference between spouses). When Wendy reaches age 66, her FRA, Harry will be age 69 (older than his FRA of age 66). One strategy is for Harry to file for and then suspend his retirement benefits when Wendy reaches FRA. This allows Wendy to file for her spousal benefit while her worker benefit continues to accrue DRCs and COLAs. This strategy is available even if Harry and Wendy get divorced as long as they were married for at least ten years and have not remarried (unless to each other). If they are divorced, Wendy is eligible for her spousal benefit whether or not Harry has filed for his worker benefit as long as they have been divorced for at least two years and they are both at least 62.

One year later when Harry reaches age 70, he should take his maximum worker benefit of 132% of his PIA (plus COLAs). When Wendy reaches age 70, after four years of spousal benefits, she should switch to her higher maximum worker benefit of 132% of her PIA (plus COLAs).

Upon the death of either Harry or Wendy, the surviving spouse will be entitled to receive the greatest Social Security worker benefit as of the date of death (but not both Social Security benefits). This survivor benefit is available to either Harry or Wendy even if they get divorced as long as they were married for at least ten years. If the survivor remarries before age 60, she cannot collect survivor benefits with respect to any former spouse while remarried.

### David (the Divorcé)

David was married for 20 years to Sandy. Ten years after their divorce, when Sandy is age 62 and David reaches age 67, his FRA in 2027, he can elect to claim spousal benefits of 50% of Sandy's PIA without stopping the DRC and COLA accruals on his own worker benefit whether or not Sandy has claimed any benefits. If Sandy dies while David is receiving a spousal benefit based upon her work record, his spousal benefit will automatically be increased to 100% of the benefit she was receiving (or could receive) without stopping the DRC and COLA accruals on David's worker benefit. When David reaches age 70, he can switch to his maximum worker benefit of 124% of his PIA (plus COLAs). If Sandy dies after he has reached age 70 he can receive her worker benefit at the date of her death as a surviving spouse if it exceeds his worker benefit at that time.

### Maria and John (the Working Mom and Stay-at-Home Dad)

Maria and John were described in detail in *Social Security Benefits Formula 101: A Practical Primer*. Maria has paid the maximum Social Security tax for more than 35 years, and her PIA is \$2,413. John quit his job after their second child was born. He paid in the maximum Social Security tax for each year that he worked, but only for ten years; his PIA is \$1,168.

**Early, Full and Deferred Worker Retirement Benefits for Maria and John (excluding COLAs)**

Age	62	66	70
Maria	\$1,810	\$2,413	\$3,185
John	\$876	\$1,168	\$1,542

If John decides to retire at age 62 he will receive a reduced worker benefit of only \$876. When both he and Maria reach age 66, their FRA, Maria can elect and suspend (so that her worker benefit

continues to accrue DRCs and COLAs), allowing John to claim his spousal benefit of \$914. His spousal benefit includes an additional \$38 (determined by the excess of \$1,206 (50% of Maria's PIA of \$2,413) over \$1,168 (his PIA)). Alternatively, if he had waited until age 66, his FRA, to claim his benefits he would have received an unreduced spousal benefit of \$1,206 and his worker benefit could have continued to accrue DRCs up to \$1,542 (plus COLAs) at age 70. If Maria predeceases him, his benefit will increase automatically to the amount of the benefit she was receiving at her death, which could be as great as \$3,185 plus COLAs (if she deferred claiming her worker benefit to age 70).

## Conclusions

Social Security retirement benefits will likely be an increasingly meaningful source of retirement income for millions of retirees. For too many women and people of color these benefits can mean the difference between life and death. Changes under the 2000 Senior Act and 1983 legislation as well as the declining length of marriage and the complicated facts and circumstances of many individuals and their current and former family units make the timing decisions even more complex. As tax professionals we should be conversant in strategies to maximize retirement income, which will be increasingly focused on Social Security benefits for millions of clients. Additionally, understanding these nuances will help us mitigate Social Security benefit confusion and misinformation when Social Security reform reemerges.

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# 401(k) Follies: A Proposal to Reinvigorate the United States Annuity Market

By Paul M. Secunda\*

One does not need to do anything but look around to see that the United States population is aging at an alarming pace. With the aging of America, more emphasis has been placed on retirement security. The three-legged stool of retirement security—personal savings, Social Security, and private pension accounts—is increasingly dependent on the private pension leg. This is because personal savings rates in the United States are near or at an all-time low, and Social Security, even if we assume it will remain solvent, merely provides a fraction of what most people need to live comfortably in retirement.

In the private pension world, the United States has recently emerged from a troubling move away from defined benefit plans (DBPs) (i.e., traditional pensions) to various forms of defined contribution plans (DCPs). Because employers are responsible for providing a defined benefit amount to employees at retirement under DBP arrangements, there is more regulation of these plans to ensure that the promised benefits are available upon retirement and plans do not default on their pension promises. For instance, the Employee Retirement Income Security Act of 1974 provides for minimum vesting, benefit accrual, and funding standards for DBPs and sets up an insurance scheme, operated by the Pension Benefit Guaranty Corporation in case of employer defaults.

On the other hand, employers are only responsible to contribute money to their employees' individual plan accounts under the DCP model and that is where their responsibility ends. Although DBPs historically were the retirement plan of choice, there has been a significant shift to DCPs by employers in recent years; DCPs generally cost less, place fewer obligations on the employer, and are portable from one employer to the next. For instance, from 1979 to 2001, the number of DBPs went from 139,489 to

51,000, while the number of DCPs went from 331,432 to 707,000.

## Potential Problems for Retirees

This trend is troubling. Whereas the employer was responsible for providing the pension benefit to the employee upon retirement under DBPs, DCPs only require the employer to pay a defined amount into an employee's individual account. At that point, it is up to the employee to invest the pension funds in various financial instruments so that he or she will have sufficient funds available to last through retirement. DCPs thereby place the risks of longevity, investment return, inflation, and interest rates on the employee. Consequently, no guarantee exists that a participant will receive any specified amount of benefit at retirement and many baby boomers are waking up to this strange new world of being in charge of their future retirement.

The problem is exacerbated because most individuals with DCPs now find themselves enrolled in a 401(k) plan. Under a 401(k) salary deferral plan, which may include an employer matching contribution component, the employee directs the employer to divert a specified percentage of his or her salary

\*Associate Professor of Law, Marquette University Law School, Milwaukee, WI; Chair, Association of American Law Schools Section on Employee Benefits and Executive Compensation.