A Guide to Tax Treatment for Long-Term Care Insurance

From Mark Baron, CLTC

BARON LONG TERM CARE INSURANCE

Afford the care you need ▲ Have the life you want

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***The information provided here came from the American Association for Long-Term Care Insurance, whose purpose is to help you better understand the various tax implications relating to LTCi policies. This is for informational purposes only and should not be construed as tax advice. Please consult a tax advisor regarding your particular circumstances

CLTC One Page 2018 Tax Summary
Tax-Qualified Long-Term Care Insurance (LTCI)

Type of Taxpayer / Premium Deduction (Traditional Policies)

Individual taxpayer who does NOT itemize

No deduction.

Individual taxpayer who itemizes deductions

(Schedule A)

Below are the deductibility limits for 2017 and 2018. Amounts above these limits are not considered to be a medical expense.

Attained age in tax year	Deductible premium limit
40 or less	$420
More than 40 but not more than 50	$750
More than 50 but not more than 60	$1,560
More than 60 but not more than 70	$4,160
More than 70	$5,200

Source: IRS Revenue Procedure 2016 – 55 (2017 limits) and 2017-58 (2018 limits)

HSA & Archer MSA

Eligible LTCI premium is a qualified medical expense.
IRC §213(d)(1)(D)

Employee (W-2)

(NON-owner)

Premium paid by employee (e.g., “voluntary” or payroll deduction):

- May NOT be paid through cafeteria plan. *IRC §125(f)*
- May NOT be paid through FSA or similar arrangement. IRC §106(c)
- Deductible by employee who itemizes *(subject to limitations above)*

Premium paid by employer (ANY business type):

- Employer provided LTCI treated as accident and health plan. *IRC §7702B(a)(3)*
- Deductible by employer - NOT limited to Eligible premium (subject to reasonable compensation). May also include spouse and other eligible tax dependents. *IRC §162(a)*
- Total premium excluded from employee’s income (NOT limited to Eligible premium). Not subject to FICA, etc. *IRC §106(a)*
- Benefits remain tax-free. *(See column to right)*

C-Corporation Shareholder / Employee (with W-2)

- Including PCs and LLCs taxed as a Cv

- *Treated as employee. (See above)*

C-Corporation Shareholder / Employee (with W-2)

- Sole Proprietor
- Partner
- S-Corporation >2% shareholder/employee (W-2)
- Member of a LLC or PC taxed as any of above

NOTE: Limited Liability Corporation (LLC) is a legal, not tax, entity – ask how the entity files.

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Source: IRS Revenue Procedure 2016 – 55 (2017 limits) and 2017-58 (2018 limits)

Taxation of Benefits

Reimbursement benefits are not included in income.
IRC§§104(a)(3), 7702B(a)(2)

Per diem (or indemnity) benefits are not included in income except amounts that exceed the greater of:

- $360 per day (2017 indexed), or
- Total qualified LTC expenses.

IRC §§104(a)(3), 7702B(a)(2), 7702B(d)

Return of premium (nonforfeiture) benefits:

- Available only upon total surrender or death.
- May not be borrowed or pledged.
- Included in gross income to extent of any deduction or exclusion allowed with respect to premium.

IRC §7702B(b)(2)(C)

Linked-Benefit LTCI

LTC benefits paid from a Tax-Qualified (7702B) annuity or life insurance “linked benefit” plan are tax-free as noted above.
IRC§7702B(e)

Cash surrenders from a LTCI linked-benefit plan that paid LTCI benefits may have a reduced cost-basis.
IRC§72(e)(11)

Premium payments for annuity or life insurance linked-benefit LTCI plans are NOT deductible. (Separately-billed TQ LTCI riders may be deductible.)

The information contained in this summary is provided with the understanding that it is not to be interpreted as specific tax or legal advice. Neither the Corporation for Certification for Long-Term Care, LLC, nor any of its employees or CLTC® designees are authorized to give legal or tax advice. Individuals are encouraged to seek the guidance of their own qualified tax and/or legal counsel. (Rev. November 2016)

Recognizing that government can't pay the bill for long-term care, federal and a growing number of state tax codes now offer tax incentives to encourage Americans to take personal responsibility for their future long-term care needs. The Health Insurance Portability and Accountability Act of 1996 (HIPAA) included provisions for favorable tax treatment of qualified Long-Term Care insurance (LTCi) contracts.

AS YOU AGE … YOUR TAX DEDUCTIBLE LIMIT INCREASES

For Individual Purchase

Tax-qualified LTCi premiums are considered a medical expense. For an individual who itemizes tax deductions, medical expenses are deductible to the extent that they exceed current amount required to meet the individual's Adjusted Gross Income (AGI). The amount of the LTCi premium treated as a medical expense is limited to the eligible LTCi premiums, as defined by Internal Revenue Code 213(d), based on the age of the insured individual. That portion of the LTCi premium that exceeds the eligible LTCi premium is not included as a medical expense.

Individual taxpayers can treat premiums paid for tax-qualified long-term care insurance for themselves, their spouse or any tax dependents (such as parents) as a personal medical expense. The yearly maximum deductible amount for each individual depends on the insured's attained age at the close of the taxable year (See chart on previous page). These deductible maximums are indexed and increase each year for inflation.

Tax Savings Tip: Long-term care insurance premiums may be paid from a Health Savings Account (HSA) up to the limits shown above.

Taxability of Benefits Received: Generally, benefits received from a tax-qualified LTCi policy that was purchased by an individual are non-taxable and therefore excluded from Adjusted Gross Income. Benefits paid under an indemnity policy are not taxed unless they exceed the higher of the cost of qualified long-term care or $330-per-day (the 2014 limit).

Self-Employed

A self-employed individual can deduct 100% of his/her out-of-pocket long-term care insurance premiums, up to the Eligible Premium amounts listed above [IRC 162(l)]. The portion of LTCi premiums that exceeds the Eligible Premium amount is not deductible as a medical expense. The deductible amount includes eligible premiums paid for spouses and dependents [IRC 162(l)]. It is not necessary to meet an adjusted gross income threshold in order to take this deduction. However, a self-employed individual may not deduct LTCi premiums during any calendar month in which he/she or his/her spouse is eligible to participate in a subsidized LTCi plan (where the employer pays all or part of the premiums for LTCi).

Partnership ² Limited Liability Company (LLC) ² Subchapter S Corporation

Partners is a partnership, members of an LLC that is taxed as a partnership, and shareholders/employees of Subchapter S Corporations who own more than 2% of the Corporation, are taxed as self-employed individuals. The partnership, LLC or Subchapter S Corporation pays the premium.

The partner, member or shareholder/employee includes the LTCi premium in his/her Adjusted Gross Income, but may deduct up to 100% of the age-based Eligible Premium, as listed in Table 1. It is not necessary to meet an adjusted gross income threshold.

Planning Tip: In a sole proprietor or a partnership situation, the owner/partner who has a spouse who is a true employee can deduct the actual (full) premium for that spouse's policy. If that spouse's policy had a shared benefit rider that would be included in the deductible premium amount (actual total premium is deductible).

Subchapter C Corporation

When a business purchases a tax-qualified LTCi policy on behalf of any of its employees, or their spouses and dependents, the corporation is entitled to take a 100% deduction as a business expense on the total premium paid. The deduction is not limited to the aged-based Eligible Premiums.

The purchase of a tax-qualified LTCi policy is not subject to any non-discrimination rules, thus allowing an employer to be selective in the classification of employees it elects to cover.

Planning Tip: Premium payments generally will be tax deductible when the class is based on such factors as the officers of the corporation and length of service (e.g. company pays for all those who are

Senior Vice President or higher and have been with the company for 12 or more years). Tax rulings have stipulated that the class cannot, however, be based on stock ownership.

Tax Savings Tip: The use of Ten-Pay or Accelerated Premium plans provide higher tax deductions for the Corporation and enable the long-term care insurance premium to be fully paid-up by the time the owner retires (no ongoing premiums) or sells.

Selling Tip: Fiscal Year-End Planning for profitable companies with a retained earnings issue. The fiscal (tax) year for C-Corps generally don't end on December 31st (as they do for 'pass through' entities and individuals). At the beginning of the fourth quarter of their Fiscal Year, profitable companies start looking for tax deductions. Recommend long-term care insurance as an executive benefit … benefits are far more valued than new office furniture.

The premium paid by the business is excluded (not reported) from the employee's Adjusted Gross Income even if the premium exceeds the Eligible Premium amount listed in the tables above.

Employer-Pay Contributory Arrangement on Behalf of an Employee

If an employer pays all or a portion of the tax-qualified LTCi premiums on behalf of an employee, the amount paid is deductible by the employer as a business expense. The deduction is not limited by the age-based limits. The entire employer contribution would also be excluded from the employee's AGI.
If the employer only pays a portion of the premium, the employee is able to apply the balance that he/she pays towards his/her medical expenses, up to the Eligible Premium amount, and would then be entitled to a deduction for medical expenses that exceed the threshold for adjusted gross income.

Gift Tax Exclusion

In addition to the annual Gift Tax Exclusion of $13,000 per donee, a donor has the ability to pay for the medical expenses of the donee [IRC Sec. 2503(e)]. If those medical expenses are tax-qualified LTCi premiums, the exclusion is subject to the age-based limits for Eligible Premium listed in the tables above. An individual (donor) can purchase LTCi policies for family members (donees) and still maintain the annual Gift Tax Exclusion when selecting a Ten-Pay or Accelerated Payment Option.

Return of Premium

The refund is included in the beneficiary's gross income and is taxable, to the extent it was either excluded from the owner's income or deducted by the owner. It must be included as income in the year it is received.

Health Savings Account (HSA)

Tax-qualified LTCi premiums can be reimbursed through an HSA, tax-free up to the Eligible Premium amounts listed in the tables above, even if the HSA is offered through an employer-provided cafeteria plan.

Health Reimbursement Account (HRA)

Reimbursements for insurance covering medical care expenses, as defined in IRC Sec. 213(d), which includes qualified long-term care services and qualified long-term care insurance premiums are allowable under an HRA. Although employers pay for HRAs, an HRA cannot be provided by salary reduction or IRC Sec. 125 plans. As such, the LTCi premiums cannot be paid on a pre-tax basis through an HRA.

Cafeteria Plan

Tax-qualified LTCi premiums cannot be purchased with pre-tax dollars under an employer-provided cafeteria plan. However, LTCi premiums may be paid through an HSA that is offered under an employer-provided cafeteria plan.

Flexible Spending Account

Tax-qualified LTCi premiums cannot be reimbursed under an FSA.

Individual State Tax Treatment

Many states offer tax incentives to encourage the purchase of LTCi. Below is a general summary of state specific tax information for your reference. This information was current through December 2011 and is subject to change.

Taxpayers may need to meet state specific requirements to qualify for deductions or credits for LTCi. For information regarding the tax liability of a case, consultation with a tax consultant or legal advisor is recommended.

What the Coding Means

* = No Credit or Deduction. No Broad-Based State Income Tax.

** = Same As Federal Tax Law (see above for details).

ALABAMA
Individuals are allowed an itemized deduction for qualified long term care insurance contract to the extent that the amount does not exceed specified limitations. These amounts are indexed. Businesses, whether incorporated or not, may deduct LTC insurance as reasonable compensation expenses.

ALASKA*
No tax benefits presently.

ARIZONA*
No tax benefits presently

ARKANSAS**
A deduction is allowed to the limits provided in the federal Internal Revenue Code (see above for details)

CALIFORNIA
A deduction is allowed to the limits provided in the federal Internal Revenue Code (see above for details)

COLORADO
A Credit is allowed for 25 percent of the premiums paid for long term care insurance during tax year for the individual and spouse. The Colorado credit is only applicable to those with federal taxable income of less than $50,000; to two individuals filing a joint return with a federal taxable income of less than $50,000 if claiming the credit for one policy; or less than $100,000 if claiming the credit for two policies.

CONNECTICUT*
No tax benefits presently

DELAWARE*
No tax benefits presently

DISTRICT OF COLUMBIA
A deduction for long term care insurance premiums paid annually is allowed from gross income provided that the deduction does not exceed $500 per year, per individual. It does not matter whether the individual files jointly and the LTC policy must meet District of Columbia's definitions.

FLORIDA*
No tax benefits presently

GEORGIA*
No tax benefits presently

HAWAII
Same as federal tax law, except subject to AGI threshold of HI adjusted gross income, instead of federal adjusted gross income.

IDAHO
A deduction is allowed for premium paid by a taxpayer for LTCi which is for the benefit of the taxpayer, a dependent of the taxpayer or an employee of a taxpayer and the amount can be deducted from taxable income to the extent the premium is not otherwise deducted by taxpayer.

ILLINOIS*
No tax benefits presently

INDIANA
Deduction up to full cost of premium paid for qualified LTCi for taxpayer and taxpayer's spouse paid in the taxable year.

IOWA**
A deduction is allowed to the limits provided in the federal Internal Revenue Code (see above for details)

KANSAS
For tax years beginning in 2005,a subtraction from federal adjusted gross income for $500 in the tax year 2005, increasing each year by $100 until 2010. After 2010, it is a $1000 subtraction from the federal adjusted gross income for premium costs for qualified LTCi.

KENTUCKY
Deduction from adjusted gross income allowed for any amount paid during the tax year for LTC premiums.

LOUISIANA
A credit against the individual income tax is allowed for amounts paid as premiums for eligible long term care insurance. The amount of the credit equals 10 percent of the total amount of premiums paid each year by each individual claiming the tax credit and the policy must meet the specific qualification requirements.

MAINE
The Superintendent of the State must certify the policy you purchase as a qualifying long term care policy. Then you are permitted a deduction as long as the amount subtracted is reduced by the amount claimed as a deduction for federal income tax purposes. Sounds more complicated than it really is. Employers providing long term care benefits to employees may also qualify for a tax credit which follows a formula equal to the lowest of $5,000, 20 percent of the costs or $100 for each employee covered.

MARYLAND
Taxpayer is allowed a one-time credit against the state income tax in an amount equal to 100% of eligible LTCi premium paid. The credit may not exceed $500 for each insured, may not be claimed by more than

one taxpayer with respect to the same individual and may not be claimed if the insured was covered by LTCi before July 1 2000. No carryover is allowed. For employers, a credit up to an amount equal to 5% of the costs incurred by the employer during the taxable year for providing LTCi as part of the benefit package. The credit may not exceed $5000 or $100 for each employee covered by LTCi under the benefit package.

MASSACHUSETTS*
No tax benefits presently

MICHIGAN*
No tax benefits presently

MINNESOTA
A credit is allowed for LTCi premiums equal to the lesser of: (1) 25% of premiums paid to the extent not deducted in determining federal taxable income; or (2) $100 (which equals $200 for married couples who file joint tax returns.)
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MISSISSIPPI
A credit equal to 25% of premium costs paid during the taxable year for a qualified policy for self, spouse, parent, parent-in-law, or dependent. The credit cannot exceed $500.

MISSOURI
Taxpayers may deduct 100% of all non-reimbursed amounts paid for qualified LTCi premiums to the extent such amounts are not included in itemized deductions.

MONTANA
Montana offers both a deduction for entire amount of qualified LTCi premiums covering taxpayer, taxpayer's parents, grandparents & dependents. A tax credit is now allowed for premiums paid for long term care insurance coverage for a qualifying family member. The amount of the credit shall be based on the taxpayer's adjusted gross income and cannot exceed $5,000 per qualifying family member in a taxable year. Or, $10,000 for two or more family members.

NEBRASKA
Nevada now permits a tax deduction for Long Term Care Savings Plan contributions of up to $2,000 per married filing jointly return or $1,000 for any other return to the extent that it is not deducted for federal income tax purposes.

NEVADA*
No tax benefits presently

NEW HAMPSHIRE*
No tax benefits presently

NEW JERSEY
Deduction of LTC insurance premiums may be taken if they exceed 2% of adjusted gross income and cannot be reimbursed.

NEW MEXICO
Credit / Deduction. New Mexico permits taxpayers who are age 65 and older and who are not a dependent of another taxpayer to claim a credit of $2,800 for medical care expenses which includes long term care insurance premiums paid for the filing taxpayer, spouse or dependents if expenses equal $28,000 or more within the particular taxable year (and so long as the expenses are not reimbursed). A deduction allows taxpayers an additional exemption of $3,000 for medical expenses if expenses (including the cost for LTC insurance) equal $28,000 or more within the taxable year and if expenses are not reimbursed or otherwise covered.

NEW YORK
Credit for 20% of premium paid for qualifying LTCi premiums. Taxpayer is permitted to carry over to future tax years any credit amount in excess of taxpayer's tax liability for the year. Employers are eligible for a credit equal to 20% of the premiums paid during the tax year for the purchase of, or for continuing coverage under, an LTCi policy. The credit is not refundable and the credit may not reduce the tax to less than the minimum tax due.

NORTH CAROLINA
A credit is allowed for premiums paid on LTC insurance for taxpayer, taxpayer's spouse or dependent in an amount equal to 15% of the premium costs, up to $350 for each policy on which the credit is claimed as long as adjusted gross income meets the following limitations: Married Filing Separately <$50,000; Single <$60,000; Head of Household <$80,000; Married Filing Jointly or Qualifying Widower <$100,000.

NORTH DAKOTA
A credit is allowed for premiums paid on LTC insurance for taxpayer and or spouse up to $250 within any taxable year.

OHIO
Deduction of federally qualified LTCi premiums for taxpayer, taxpayer's spouse and dependents to the extent deduction is not allowed in computing federal adjusted gross income.

OKLAHOMA**
No tax benefits presently

OREGON
Credit equal to the lesser of 15% of premiums paid during the tax year or $500 for LTC insurance coverage for individual, dependent or parents. For employers, a credit of $500 is allowed for each employee covered by an employer-sponsored policy.

PENNSYLVANIA*
No tax benefits presently

PUERTO RICO*
No tax benefits presently

RHODE ISLAND**
No tax benefits presently

SOUTH CAROLINA**
No tax benefits presently

SOUTH DAKOTA*
No tax benefits presently

TENNESSEE*
No tax benefits presently

TEXAS*
No tax benefits presently

UTAH*
No tax benefits presently

VERMONT**
No tax benefits presently

VIRGINIA
Deduction Virginia statutes permit a deduction from federal adjusted gross income for the amount paid in long term care insurance premiums provided the individual has not claimed a deduction for federal tax purposes or a credit under Virginia tax code 58.1-339.11. This code permits a credit against the individual's income taxes that shall not exceed 15 percent of the amount of long term care insurance premium paid during the taxable year. And, the credit cannot be claimed to the extent that the individual has claimed a deduction for federal tax purposes. This one is worth having your CPA decide as a tax credit can be worth far more than a tax deduction.

WASHINGTON*
No tax benefits presently

WEST VIRGINIA
Deduction for LTCi premiums covering taxpayer, taxpayer's spouse, parents and dependents to the extent the amount paid for LTCi is not deducted in determining federal income tax.

WISCONSIN
Deduction allowed for taxpayer & taxpayer's spouse for 100% of the amount paid for a LTCi policy to the extent the same deduction is not taken for federal income tax purposes.

WYOMING*
No tax benefits presently

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