



## 2008 Long Term Care Insurance Tax-Qualified Plans

**Benefits received under a TQ plan are tax free and premiums are tax-deductible: the amount is dependent on how the policyholder files.**

**Individuals: (W-2)** Premiums paid by an individual for qualified long term care insurance are treated as a medical expense for purposes of itemizing medical expenses. The amount that can be used in calculating the expense deduction is limited to the lesser of actual premium paid or “eligible long term care premium”, defined as follows:

<b>ATTAINED AGE BEFORE CLOSE OF 2008 TAXABLE YEAR</b>	<b>ALLOWABLE DEDUCTION (for the tax year 2008)</b>
40 OR YOUNGER	\$310
41 THROUGH 50	\$580
51 THROUGH 60	\$1,150
61 THROUGH 70	\$3,080
71 & GREATER	\$3,850

The amount of the premium paid for the coverage of the individual, spouse and dependents may be deducted to the extent that total medical expenses, including the eligible long term care premium, exceeds 7.5% of adjusted gross income (AGI). Benefits paid on a qualified long term insurance policy to an individual are not taxable income as long as benefit payments above \$270 per day do not exceed the actual cost of care (indemnity policies), as reimbursement policy benefits do not exceed the cost of care.

**Sole Proprietor: (Schedule C Income)** Sole proprietors can deduct the full premium paid for the LTC coverage they provide their employees. With respect to their own coverage, the sole proprietor can deduct 100% of eligible long term care premiums, “eligible long term care premium” is defined above. There is no 7.5% of AGI threshold requirement. A sole proprietor can deduct the full premium paid for LTC coverage by hiring his/her spouse as an employee and providing family coverage for the employee/spouse. The employer/spouse is then covered by the plan as a member of the employee’s family. If the employee/spouse is a bona fide employee, the cost of the coverage is fully deductible by the employer/spouse and excludable from the employee/spouse’s gross income.

**C-Corporations:** Companies can deduct 100% of the premium they pay out for long term care insurance and can discriminate who gets coverage. They can provide this benefit to a select group, if desired. This allows employees to exclude the premium from their taxable income and receive long term care claim benefits tax-free. The employee's spouse and dependent parents can be extended coverage as well. The company may deduct the entire premium as a necessary business expense under Section 162 of the Internal Revenue Code. This deduction also applies to the cost of coverage paid for the spouse and dependents of the employee. Employer provided long term care insurance qualifies as an accident and health plan within meaning of the IRC Sections 105(b) and 106.

**Partnership:** When a partnership pays for LTC coverage on its partners, it can deduct premiums that qualify as “guaranteed” payments under IRC Section 707(c). LTC premiums constitute guaranteed payments if they are paid for services rendered by the insured’s in their capacity as partners, without regard to partnership income. Since partners are not employees, they can not use IRC Section 106(a) to exclude from their gross income the LTC premiums paid by the partnership. Although partners must include the full amount of such premiums in their gross income, they can deduct a portion of the premiums paid. The same rules that limit the deduction a sole proprietor can take for his or her long term care premiums also limit the premiums that a partner can deduct. Members in a limited liability company (LLC) taxed as a partnership are subject to these same limitations. If a spouse is a bona fide employee of a partnership or LLC, the same rules regarding deductibility and exclusion from gross income that are described in the section on sole proprietor apply. See above.

**S-Corporations:** For fringe benefit purposes, a 2-percent shareholder of an S corporation is treated like a partner in a partnership. Therefore, an S corporation can deduct the LTC premium it pays in consideration for services rendered by the insured shareholder, and the shareholder must include the full premium in his or her gross income. As with sole proprietors and partners, a 2-percent shareholder in an S corporation can deduct only a limited portion of the LTC premiums. A 2-percent shareholder is defined in IRC Section 1372 as “...any person who owns (or is considering as owning within the meaning of IRC Section 318) on any day during the taxable year of the S corporation more than 2-percent of the outstanding stock of such corporation or stock possessing more than 2-percent of the total combined voting power of all stock of such corporation.” IRC Section 318 provides rules for the constructive ownership of stock (the attribution rules). Under these rules, an individual is deemed (i.e. considered) to own stock owned directly or indirectly by his parents, spouse, children and grandchildren.

**Employer Deduction –LTC Premiums:** When an employer pays the premium for qualified long term care coverage for its employees, the employer should be able to deduct those premiums as an ordinary and necessary business expense to the same extent that it can deduct premiums paid for other accident and health insurance covering its employees (IRC Section 162). However, an employer can not provide long term care coverage as part of a cafeteria plan (IRC Section 125 (f)).

**Employee Income – LTC Premiums:** Under IRC Section 106(a), an employee does not have to include in gross income the cost of any employer-provided coverage under an accident or health plan. Consequently, with one exception, premiums paid by an employer for an employee’s qualified long term care insurance are not includible in the employee’s gross income. If employer-paid premiums for qualified long term care coverage are NOT included in the employee’s gross income, then the employee cannot take an income tax deduction for those premiums. However, if an employer provides long term care coverage through a flexible spending arrangement, the employee must include the cost of that coverage in gross income (IRC Section 106 (c)). Accordingly, the employee’s medical expense deduction is then limited to the lesser of actual premium paid or the eligible long term care premium, and the normal threshold of 7.5% of AGI applies.

**Employee Income- LTC Benefits:** The general rule is that any benefit received by an employee through accident or health insurance for personal injuries or sickness is included in the employee’s gross income if the employer paid for the coverage and the employer-paid premiums were not included in the employee’s income when paid (Code Section 105(a)). This general rule does not apply to amounts paid to reimburse the employee, directly or indirectly, for medical care expenses incurred by the employee, the employee’s spouse or the employee’s dependent (IRC Section 105(b)). Amounts received under a qualified long term care insurance contract are treated as reimbursements for expenses actually incurred for medical care (IRC Section 7702B(a)(2)). As a result, if an employer pays the premium for an employee’s qualified long term care coverage, the employee will NOT be taxed on the long term care benefits paid under the insurance- those benefits are treated as a non-taxable reimbursement for medical care. The result is the same whether the insurance reimburses actual long term care expenses or pays a per diem amount toward long term care. However, if the insurance pays a per diem benefit that exceeds the per diem limit provided under IRC Section 7702B(d) (\$270 in 2008), the excess is taxable income to the employee unless the employee’s actual long term care expenses equal or exceed the per diem benefit paid.

140 Broadway, 26<sup>th</sup> Floor New York NY 10005

Toll Free 212-344-4040 Fax 212-344-4020

[www.customcaresolution.com](http://www.customcaresolution.com)