



## Five Tax Advantaged Insurance Based Strategies for Long-Term Care

Dave DeBoer JD, CLU, ChFC, CASL  
Mutual of Omaha

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# Agenda

1. Tax Deductible LTCi
2. 1035 Exchanges
3. Retired Public Safety Officers
4. HSAs
5. Life Insurance into a Long-Term Care Trust



# 1. Tax Deductible LTCi

# Taxation of LTCi Premiums

It depends on who you are...

- Individual
- Business Owner
- Employee

# Tax Treatment for Individuals

Individuals may deduct premiums as follows (IRC Sec 213(d)):

- Qualified LTC premiums, combined with other un-reimbursed medical expenses, are deductible to the extent they exceed 7.5% of the taxpayer's adjusted gross income (AGI).
- Must itemize deductions (Schedule A).
- May include an amount up to the eligible premium.

# Eligible Premiums

**2010**

Age 40 or less	\$ 330
Age 41-50	\$ 620
Age 51-60	\$1,230
Age 61-70	\$3,290
Age 71 and over	\$4,110

Data is for 2010 and is subject to annual inflation adjustments

# Eligible Premiums

**2011**

Age 40 or less	\$ 340
Age 41-50	\$ 640
Age 51-60	\$1,270
Age 61-70	\$3,390
Age 71 and over	\$4,240

Data is for 2011 and is subject to annual inflation adjustments



# Business Entities

Self Employed

C Corporations

# Tax Treatment for Self Employed

Premiums for self-employed individuals:

- Treated as self employed health insurance premium (IRC Sec. 162(l)).
- Deductible up to the eligible premium amount (IRC Sec. 162(l)).
- Actual premium is deductible for employees (IRC Sec. 162(a)).

# C Corporations

Actual premium is deductible for:

- Employees (IRC Sec. 162(a))
- Shareholders who are employees  
(IRC Sec. 162 (a))
- Shareholder's spouse and dependents  
(IRC Secs. 162(l) and 213(d))

# Tax Treatment for Employees

The best tax treatment of the three:

- Business may deduct the actual premiums paid for the employee (IRC 162(a)).
- The employee is not required to include these amounts in income (IRC 106(a), 105(b)).
- Not subject to the 7.5% of AGI rule.
- Not subject to age-based limits.

## Taxation of LTCi Benefits

Qualified LTC insurance benefits are tax free to the extent they do not exceed the greater of:

- Qualified long-term care expenses
- Per diem amount (\$290 in 2010, \$300 in 2011) (IRC Sec. 7702B(d), 105(b))

## The Benefit “Trifecta”

- Deductible Premium
- Premium is not includible as income
- Benefits are not includible as income

# Discrimination

May you discriminate in an insured accident or health plan?

- Yes (Treas. Reg. §1.105-5)
- If the only recipients are employee/shareholders, establish that the fringe benefit is an employee benefit, not a shareholder benefit.



## 2. 1035 Exchange



# Pension Protection Act 2006

Section 844 clarifies rules pertaining to Long-Term Care Insurance:

- Enhances the rules allowing life insurance and annuities to be combined with Long-Term Care benefits.
- Provides favorable tax consequences for combination/“hybrid” policies.
- Amends Code Section 1035 to include Long-Term Care policies.

## Section 1035

Traditionally:

- Allows life insurance to be exchanged for life insurance, endowment or annuity contracts.
- Allows endowment contracts to be exchanged for endowments with same or shorter endowment dates or annuities.
- Allows annuities to be exchanged for other annuities.

## After 12/31/09

- Life insurance and may be exchanged for life insurance or annuities with long-term care benefits.
- Annuities may be exchanged for annuities with long-term care benefits.
- Both may be exchanged for stand alone long-term care policies.

## What If...

- Client has owned life insurance or an annuity for quite some time.
- Original purpose for purchase is no longer as important.
- Surrendering the current policy could create a taxable event.

## Not a Typical Result

This allows the client to take a policy with a potential taxable event and turn it into a tax free long-term care benefit.



### 3. Retired Public Safety Officers

## Misconception:

Distributions from IRAs can be used to purchase Long-Term Care Insurance.

## Fact:

Distributions from Retired Public Safety Employee Retirement Plans (up to \$3,000) may be used to purchase long-term care insurance, for the retiree, spouse or dependents.

Distribution must be paid directly to the insurance carrier.

(Code Sec. 402(l), as added by Sec. 845(a) of the PPA '06)



# Public Safety Officers

An individual serving a public agency as:

- A law enforcement officer
- A firefighter
- A Chaplin
- A member of a rescue squad or ambulance crew



## 4. Health Savings Accounts

## Payment Alternatives

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- Flexible Spending Arrangement- No
  - IRC Sec. 106(c)(1)



## Payment Alternatives

Are the following appropriate payment alternatives to the employer paying the premium?

- Health Savings Account – Yes
- HSA within Section 125 plan - Yes

(Notice 2004-50, question 40)

## What Is An HSA?

- A tax exempt trust or custodial account
- Pays certain eligible medical expenses
- Contributions are deductible/excludible from income
- Benefits are excluded from income when received

## Contribution Limits (2010-11)

- \$3,050 (Individual)
- \$6,150 (Family)
- Age 55 or older: add \$1,000

## Eligibility (2010-2011)

Participant must be covered by a high deductible health plan:

- \$1,200 deductible (individual) with \$5,950 max out of pocket.
- \$2,400 deductible (family) with \$11,900 max out of pocket.

## Distributions

- Not included in income if used for eligible expenses.
- If not, included in income plus 20% penalty (2011).
- Penalty waived if age 65 or older or disabled.

# Distributions

Eligible medical expenses:

- Used for medical care of individual, spouse or dependent.
- Doctor prescribed drugs (2011).
- Insurance premiums are NOT a qualified medical expense.
- **EXCEPTION:** Qualified Long-Term Care Insurance.

# Distributions

Long-Term care insurance premium is limited to the eligible premium amount. (IRS Notice 2004-50, 2004-33 IRB 196, A-40)



## 5. Long-Term Care Trust

(It's Not What You Think)



# Long-Term Care Trust

- Provides for the care of someone who may need long-term care now or in the future.
- It can be testamentary or living.
- It can be revocable or irrevocable.

# Long-Term Care Trust

## Example:

- John, @ 62, good health.
- Mary, @61, uninsurable (MS).
- \$300,000 Life Insurance on John, payable to a Trust for Mary's benefit.
- Annual Premium: \$5,800 for 30 years\*.

\* Death benefit guaranteed to age 120

# Long-Term Care Trust

This provides a “Pool of Money” for use by Mary.

It can:

- Be restrictive in its use.
- Have Special Needs language.
- Be structured like a long-term care policy.
- Have none of the above.

## Long-Term Care Trust

- This provides a TAX FREE “Pool of Money” for use by Mary.
- This leverages the use of premium dollars to provide for care.
- At Mary’s death, remaining Trust assets can pass to other family members or a favorite charity.

# Long-Term Care Trusts

Don't forget Long-Term Care Insurance  
on John!

## Remember

There are a lot of ways to structure the payment of long term care expenses in tax advantaged ways,

But

Regardless of that, LTCi is a valuable product for what it does for the family!  
(and tax advantages don't hurt!)



Questions?



We're Done!  
(Thank You!!)