



Long Term Care University

Long Term Care University – Question of the Month

By Aaron Skloff, AIF, CFA, MBA

04/15/12

Q: Can we pay for our long term care insurance policies on a tax free basis?

The Problem – Paying for Long Term Care Insurance with After Tax Dollars

The Internal Revenue Code is loaded with tax benefits to encourage you to save for retirement through vehicles like 401(k) plans and Individual Retirement Accounts (IRAs). Unfortunately, paying for long term care insurance on a tax free basis is much less understood.

The Solution – Paying for Long Term Care Insurance on a Tax Free Basis

While companies have many ways to pay for long term care insurance on a tax free basis, individuals have fewer choices. Let's look at the tax implications of paying on an after tax versus tax free basis, then two solutions to pay on a tax free basis.

Paying for Long Term Care Insurance with After Tax Dollars		Paying for Long Term Care Insurance on a Tax Free Basis	
Income	\$1,200	Income	\$1,200
Less 35% Federal Income Tax	(\$420)		
Available to Pay Long Term Care Insurance	\$780	Available to Pay Long Term Care Insurance	\$1,200

Health Savings Account (HSA) Allows You to Pay Your Long Term Care Insurance on a Tax Free Basis

An HSA is a tax-advantaged savings account tied to a high deductible health insurance plan that is increasingly becoming more common with employers. Contributions to your HSA are made on a pre-tax basis, while withdrawals for qualified medical expenses are made tax free. Just as importantly, any growth (interest, dividends, capital gains, etc.) inside an HSA is tax free if withdrawals are used for qualified medical expenses. Tax-qualified long term care insurance premiums are a qualified medical expense. [See IRS Notice 2004-50] The maximum amount of premium you can pay on a tax free basis is indicated in the table below.

Age Before the Close of the Taxable Year	Premium Deduction Limit 2011	Premium Deduction Limit 2012
40 or less	\$340	\$350
41 through 50	\$640	\$660
51 through 60	\$1,270	\$1,310
61 through 70	\$3,390	\$3,500
71 and older	\$4,240	\$4,370

Certain Withdrawals from Retirement Plans Allow You to Pay Your Long Term Care Insurance on a Tax Free Basis

With the introduction of the Healthcare Enhancement for Local Public Safety Officers (HELPS) Act, qualified retired public safety employees can make tax free distributions of up to \$3,000 per year from qualified retirement plans to help pay for long term care insurance. A qualified public safety employee is an employee of a State or political subdivision of a State if the employee provides police protection, firefighting services, or emergency medical services for any area within the jurisdiction of such State or political subdivision.

An eligible retirement plan includes a governmental qualified retirement or annuity plan, 403(b) annuity, or 457(b) plan. The tax free exclusion applies with respect to eligible retired public safety officers who make an election to have qualified health insurance premiums (including long term care insurance) deducted from amounts distributed from an eligible retirement plan and paid directly to the insurer.

Action Step – Pay for Your Long Term Care Insurance Policies on a Tax Free Basis

Instead of the government taking advantage of you, take advantage of the government. **Follow the guidelines above and force the government to effectively pay up to 35% of your long term care insurance policy.** If federal income tax rates increase on January 1, 2013 (as expected), the benefits of paying for your long term care insurance policy on a tax free basis will become even more valuable.

Aaron Skloff, Accredited Investment Fiduciary (AIF), Chartered Financial Analyst (CFA), Master of Business Administration (MBA), is the Chief Executive Officer of Skloff Financial Group, a NJ based Registered Investment Advisory firm. The firm specializes in financial planning and investment management services for high net worth individuals and benefits for small to middle sized companies. He can be contacted at www.skloff.com or 908-464-3060.