

# Tax Incentives & Long-Term Care Insurance

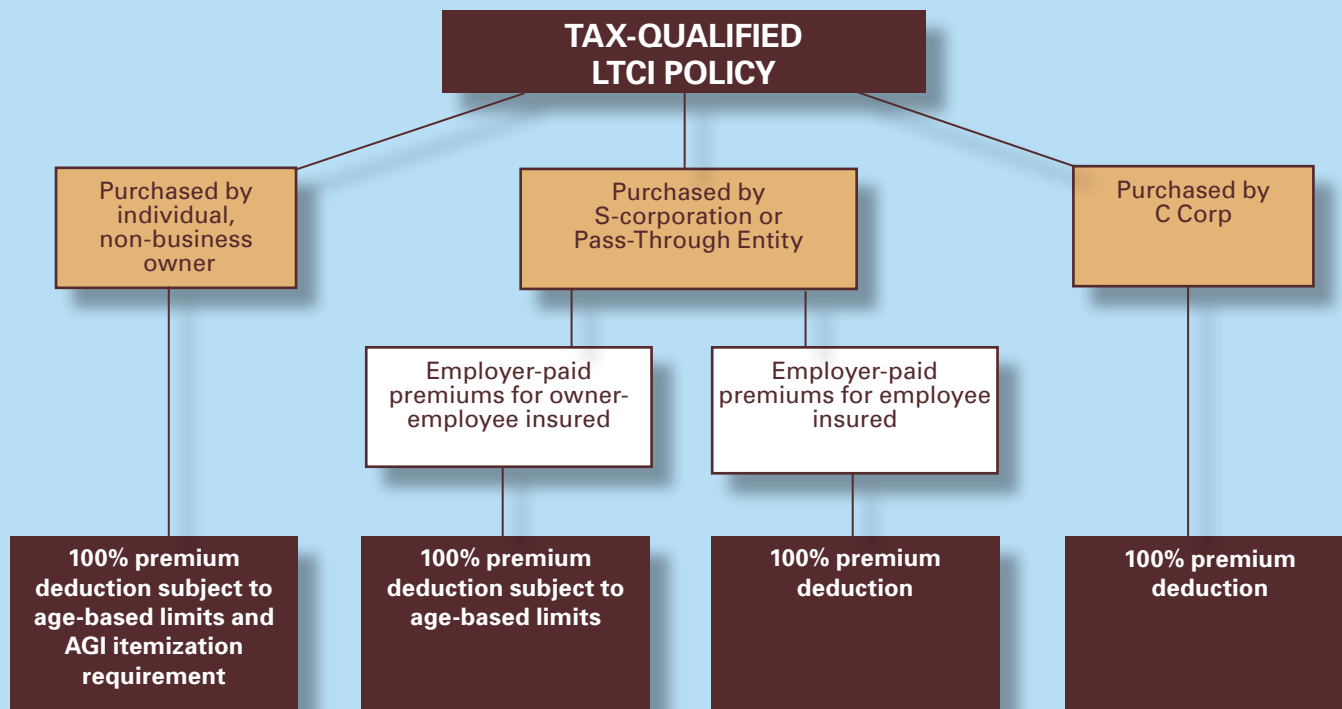
*The Company You Keep*®

*Tax laws at the federal and state levels may provide incentives for individuals and businesses to purchase qualified long-term care insurance policies, with the goal of decreasing the public's reliance upon Medicare and Medicaid as resources for funding long-term care services.*

## This brochure helps answer these questions and more...

- How do I know if my long-term care insurance (LTCi) policy qualifies for tax incentives?
- I pay the premiums for my own policy. Am I eligible for tax incentives?
- Are benefits paid at the time of a claim taxable as income?
- I own my own business. Can I deduct my own LTCi premiums? What about premiums I pay for my employees' policies?
- Our company is considering offering an LTCi plan to our employees. Can we make it available only to executives?
- Can we pay premiums using pre-tax dollars, like a Section 125 cafeteria plan?
- Am I eligible for state-level incentives in addition to the federal incentives?

## Tax Incentives At A Glance



## DEFINITION OF A TAX QUALIFIED LONG-TERM CARE INSURANCE (QLTCI) POLICY<sup>1</sup>

In order to be considered tax qualified:<sup>2</sup>

- ✓ The policy must be guaranteed renewable, meaning that the policy can only be cancelled for non-payment of premiums.
- ✓ Benefits under a QLTCi policy cannot duplicate Medicare benefits.
- ✓ Nonforfeiture benefits and benefit increase options (inflation protection) must be offered to the applicant at the time of sale, but are not required as part of the policy.
- ✓ To claim benefits, the claimant must be certified by a licensed healthcare practitioner as a “chronically ill” individual within the prior 12 months.
- ✓ The certification of chronic illness must be based on one or both of the following criteria:
  - The inability to perform, without substantial assistance, at least two of six activities of daily living (ADLs).<sup>3</sup>
  - The need for substantial supervision in order to protect the individual from threats to health and safety due to a severe cognitive impairment.
- ✓ The need for long-term care assistance must be expected to last for at least 90 days.

## HOW THE LAWS WORK

### Individuals Who Itemize Medical Expenses

There is an age-based limit on the amount of premiums for purposes of the QLTCi deduction, which may be less than the actual policy cost.<sup>4</sup>

The age-based limits for 2009 are:

(maximum deductible premium)

Insured ages 40 and under	\$320
Insured ages 41-50	\$600
Insured ages 51-60	\$1190
Insured ages 61-70	\$3180
Insured ages 71 and above	\$3980

When allowable medical expenses, including QLTCi premiums, exceed 7.5% of the taxpayer’s adjusted gross income (AGI), the excess over 7.5% may be deducted. The age-based limits above apply only to the premiums paid for the long-term care insurance policy and do not reflect the maximum total deduction that may be taken by the taxpayer.

### State-Level Tax Incentives for Individuals<sup>5</sup>

State legislatures are recognizing the impact that Medicare and Medicaid service costs have on state budgets, and several states have enacted legislation that encourages private insurance.

Currently, 28 states and the District of Columbia offer tax incentives to individuals who purchase long-term care insurance. The incentives in a state may be the same as or different from the federal incentives. These incentives do not apply to business-paid premiums.

Alabama	Idaho	Maine	Nebraska	Ohio
Arkansas	Indiana	Maryland	New Jersey	Oregon
California	Iowa	Minnesota	New Mexico	Virginia
Colorado	Kansas	Mississippi	New York	West Virginia
District of Columbia	Kentucky	Missouri	North Carolina	Wisconsin
Hawaii	Louisiana	Montana	North Dakota	

*Specific incentives vary by state. Please contact a state Department of Health & Human Services for further information.*

1 New York Life’s LTC*Select* Premier policy is intended to be a tax-qualified long-term care insurance policy.

2 26 IRC Section 7702B(b)

3 The ADLs are bathing, dressing, eating, toileting, transferring, and continence.

4 26 IRC Section 213(d)(10)

5 ACLI, “Tax Incentives for Long-Term Care Insurance”, July 2008.

## Tax Treatment For Businesses

If an employer contributes to the premium cost of QLTCi for eligible employees and dependents pursuant to a plan, the contributions will generally be excludable from the employee's income<sup>6</sup> and generally deductible to the business.<sup>7</sup> The exact rules vary according to the legal status of the business entity.

### Employee-Owners of Pass-Through Entities and Sole Proprietorships

If a partnership, S corporation, or limited liability company (LLC) treated as a partnership purchases a QLTCi policy for an employee who is also an owner<sup>8</sup> of the business, the premium is generally considered compensation income deductible to the entity and taxable to the owner-employee. The owner-employee may deduct 100% of the premium subject to the same age-based limits as those applied to individual deductions for QLTCi premiums. Owner-employees are not, however, subject to the 7.5% AGI itemization requirement.

If the policy is purchased by the owner-employee with his or her own funds in his or her own name, then the owner-employee's deduction is generally subject to the 7.5% AGI itemization requirement.

**EXCEPTION:** If a sole proprietor purchases the policy in his or her own name with his or her own funds, the proprietor may deduct 100% of the premium subject to the age-based limits.

### ERISA

Employers should be aware that a QLTCi Plan may be subject to the fiduciary, disclosure, reporting and other requirements of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). Employers should consult their legal advisors regarding the possible ERISA implications of adopting a QLTCi Plan and whether there is an applicable exemption from ERISA coverage for the QLTCi Plan.

### C Corporations

A C corporation is considered a stand-alone entity for legal and tax purposes, therefore the officers and owners of a C corporation may be treated as employees. For this reason, **business-paid premiums** for officers and owners are **100% deductible to the business**, just as they are for any other employees. The premium is not considered compensation income.<sup>9</sup>

The QLTCi coverage need not conform to Internal Revenue Code non-discrimination requirements as long as the company can prove the creation of a "plan of insurance" designed to benefit some or all employees<sup>10</sup> other than just owners and officers.

The QLTCi plan may be offered to retired employees, eligible dependents of employees and retirees, including dependent parents, and surviving eligible dependents after an employee's death.<sup>11</sup>

**Employee-paid premiums** for QLTCi coverage, such as those collected through a voluntary payroll deduction plan, are considered taxable income and may not be included in a Section 125<sup>12</sup> plan or a flexible spending account.<sup>13</sup> This means that the employer may not use salary reduction dollars to pay its premium contribution.<sup>14</sup>

6 26 IRC Section 106(a)

7 26 IRC Section 162(a)

8 An owner (or "owner-employee") is generally a partner, an LLC member, or an individual who owns 2% or more of the S corporation.

9 26 IRC Section 106(a)

10 26 IRC Sections 105 and 106

11 26 IRC Section 105(b), 152(a)

12 26 IRC Section 125(f)

13 26 IRC Section 106(c)

14 26 IRC Section 106(a)



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*The purpose of this brochure is solicitation of insurance. An insurance producer may contact you. Long-term care insurance is issued on policy form series ILTC-5000 and INH-5000 with a state identifier and edition date. Example: ILTC-5000(ID) (0305) and INH(ID) (0305) for Idaho, ILTC-5000(PA) (0305) and INH-5000(PA) (0305) for Pennsylvania, ILTC-5000(TN) (0305) and INH-5000(TN) (0305) for Tennessee, and ILTC-5000(TX) (0305) and INH-5000(TX) (0305) for Texas. The policies contain some benefit eligibility restrictions, other limitations and exclusions, as well as terms under which the policies can be continued in force or discontinued, that are common in the industry. For costs and complete details of the coverage call or write your insurance producer or company.*

*This information is intended to be accurate, but neither New York Life nor its agents are in the business of giving tax or legal advice. You should consult with your own tax or legal professionals for advice on these topics relevant to your own situation.*

## EXECUTIVE CARVE-OUT ARRANGEMENTS

In an executive carve-out arrangement, the company purchases a QLTCi for a key employee, his/her dependents, and/or company retirees.

Long-term care insurance policy benefits are generally not subject to the Internal Revenue Code's nondiscrimination rules. Employers have the option to pay all or some of employees' policy premiums and can offer multiple programs in a single worksite, for example, an executive carve-out arrangement combined with a voluntary program. The policy premiums are deductible to the business as health insurance and are not taxable to the insured as income. (Tax results may vary depending on the legal structure of the business.)

The policy benefits, when received, are not taxable as income to the insured. Long-term care insurance may be one of the only financial vehicles that offers tax incentives on both ends – tax-deductible premiums and tax-free benefits!

Individually-underwritten QLTCi policies, such as are offered by New York Life, are fully portable with no change in benefits or premiums should the executive leave the company or should the company discontinue the plan of insurance.

