



Taxation and Long-Term Care

Long-Term Care Insurance (LTCI) can play a key role in protecting your assets and ensuring quality care as you age. Understanding the tax treatment of LTCI premiums and benefits is essential for effective financial planning. Federal law continues to provide valuable tax incentives for qualified policies, while benefits remain largely tax-free under current IRS regulations.

Tax Deductibility of LTCI Premiums

Since 1997, the Internal Revenue Code has allowed individuals to deduct a portion or all of the premiums paid for **qualified long-term care insurance (LTCI)** as medical expenses. These deductions apply only to qualified policies that meet federal requirements under the **Health Insurance Portability and Accountability Act (HIPAA)**.

To qualify, an LTCI policy must: - Cover only qualified long-term care services. - Be guaranteed renewable. - Not offer a cash surrender value or allow loans against the policy. - Provide that any refunds or dividends can be used only to reduce future premiums or increase future benefits. - Not duplicate Medicare benefits (except when Medicare is secondary or the policy pays a per diem benefit regardless of expenses).

Additionally, all qualified policies must meet HIPAA's consumer protection standards and definitions of chronic illness.

Definition of a "Chronically Ill Individual"

A person is considered **chronically ill** if a licensed healthcare professional certifies that the individual: 1. Is unable to perform **at least two of six activities of daily living (ADLs)**—bathing, dressing, toileting, transferring, eating, or continence—for at least 90 days without substantial assistance; or 2. Requires substantial supervision due to **severe cognitive impairment** such as Alzheimer's disease or dementia.

These definitions determine when LTCI benefits may be triggered and qualify for favorable tax treatment.

2025 Tax Deduction Limits for Qualified LTCI Premiums

Premiums for tax-qualified LTCI policies can be treated as medical expenses subject to the **7.5% of Adjusted Gross Income (AGI)** threshold for itemized deductions. The IRS sets annual age-based deduction limits, which increase slightly each year to reflect inflation.



2025 IRS Deductible Limits for Qualified LTCI Premiums:

<u>Age (End of Tax Year)</u>	<u>Maximum Deductible Premium</u>
40 or younger	\$470
41–50	\$880
51–60	\$1,760
61–70	\$4,720
71 and older	\$5,940

Taxpayers may include these amounts with other unreimbursed medical expenses when itemizing deductions. Self-employed individuals may be able to deduct **100% of eligible LTCI premiums** as a business expense, within these limits.

Tax Treatment of LTCI Benefits

Benefits received from a **qualified LTCI policy** are generally **not taxable**. They are treated as **reimbursements for personal injury or sickness**, provided that they do not exceed the IRS's daily limit.

For 2025, the IRS per diem limit for tax-free LTCI benefits is **\$420 per day** (or actual qualified expenses, whichever is greater). If benefits exceed this amount, only the excess is taxable as income.

Example:

If your policy pays \$450 per day in cash benefits but your actual care costs are \$430 per day, the \$20 difference would be considered taxable income.

Benefits from **non-qualified LTCI** policies may be taxable, depending on the policy structure and how benefits are paid. Always consult a tax professional for personalized guidance.

Grandfathered (Pre - 1997) Policies

LTCI contracts issued before **January 1, 1997**, are automatically considered qualified policies if they met state insurance standards at the time of issue. However, if a pre-1997 policy undergoes a **material change**, it may lose its grandfathered status and become subject to modern HIPAA qualification rules.

Employer and Business Deductions

For businesses, the tax treatment of LTCI premiums depends on the type of entity: - **C corporations**: May deduct 100% of premiums paid for employees as a business expense. - **Self-employed individuals, partners, and S corporation shareholders**: May deduct premiums within annual IRS limits as self-employed health insurance. - **Employer-paid premiums**: Are generally excluded from the employee's taxable income.

These deductions make LTCI particularly attractive as part of executive benefit plans or retirement preparation strategies.

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Key Advantages of Tax-Qualified LTCI

- **Premium deductions:** Potential federal and state benefits.
- **Tax-free benefits:** Most policy payouts are excluded from taxable income.
- **Asset protection:** Helps preserve retirement savings from long-term care costs.
- **Compliance:** Policies must meet HIPAA consumer protection standards.

Example: Combining Tax Deductions and Benefits

Mark, age 62, pays \$4,500 annually for a qualified LTCI policy. His AGI is \$80,000, and his total medical expenses (including LTCI premiums) are \$10,000. Because his medical expenses exceed 7.5% of AGI (\$6,000), he may deduct \$4,000 of the excess. If he later receives \$350 per day in LTC benefits for qualified care, those payments will be **completely tax-free**.

Key Takeaways

- **Qualified LTCI premiums** are deductible within IRS age-based limits.
- **Benefits** from qualified policies are tax-free up to the per diem limit.
- **Self-employed individuals and businesses** enjoy enhanced deduction opportunities.
- Policies issued before 1997 may remain qualified unless significantly altered.

IMPORTANT DISCLOSURES

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To the extent that this material concerns tax matters, it is not intended or written to be used, and cannot be used, by a taxpayer for the purposes of avoiding penalties that may be imposed by law. Each taxpayer should seek independent advice from a tax professional based on his or her individual circumstances.

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