Securian Financial

Individual Life and Long-Term Care Insurance

Insurance products issued by:
Minnesota Life Insurance Company
Securian Life Insurance Company

Tax reference guide

Long-term care policies offered as an employee benefit

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When a company provides long-term care (LTC) coverage as an employee benefit (typically as an accident and health plan, IRC Section 106(a)), certain tax advantages may be available to the company and individual employee. Although the tax benefits may vary depending on the business structure of the company providing the LTC coverage, a few key elements of this strategy stay the same:

- In order to receive preferential tax treatment, a qualified LTC policy must be used as defined in IRC section 7702B(e)(1) and IRC Section 7702B(e)(2)
- The benefit must be offered to a "valid class of employees", IRC Section 105(a) and (b)
  - The valid class may be defined using employment-based factors, such as compensation, pay grade, title, years worked, etc., but any discriminatory factor, such as race, gender, age, etc., cannot be considered
  - A valid class may include individuals who are employees/non-owners or employees/owners of the company, but it may not include owners of the company who are not W-2 employees, IRC Section 106(a)
  - A class that consists solely of employees/owners likely will not pass as valid
- The policy's LTC benefits are typically paid on an income tax free basis

This white paper looks at the tax advantages that may result from an arrangement in which the employer pays the premium directly to the insurance carrier and the employee/participant owns the LTC contract (the employer does not have any ownership in the policy).

C corporations and limited liability companies taxed as a C corporation

Deductibility of premiums paid – company

When a C corporation provides LTC coverage to a valid class of employees, the premium associated with the purchase of a qualified LTC policy is income tax deductible to the company as compensation, IRC Section 162. This deduction applies to premium payments made on a policy that covers a member of the valid class and the member's spouse or dependents, IRC Section 152 without regard to subsections (b)(1), (b)(2), and (d)(1)(B) of IRC Section 152. Attained-age limitations do not apply to the deduction.

Income tax consequences of premiums paid – employee/participant (owner of policy)

For members of the valid class, the premium for the LTC coverage may be excluded from their income. According to IRC Section 106, employer-provided coverage under an accident and health plan may be excluded from income. This exclusion rule includes amounts paid to the employee and the employee's spouse and dependents, IRC Section 152 without regard to subsections (b)(1), (b)(2), and (d)(1)(B) of IRC Section 152. Attained-age limitations do not apply. The employee is prohibited from taking an income-tax deduction on Form 1040, Schedule A for that part of the premium. If the policy has a return of premium option and the employee/participant chooses to exercise it, the participant may have taxable income because they do not have any basis in the LTC portion of the policy.

However, as noted above, shareholders who are not W-2 employees are not considered members of the valid class and thus do not qualify for this deduction. Any LTC premiums paid for a shareholder who is not an employee of the C corporation may be treated as a dividend to the shareholder.

S corporations and limited liability companies taxed as an S corporation

Deductibility of premiums paid – company

The amount of LTC premium an S corporation may deduct for each member in the valid class depends on the member's level of ownership in the company.

When an S corporation provides LTC coverage to an employee who is a more than 2 percent shareholder, the LTC premiums may be deductible to the business, IRC Section 1372. But the LTC premium must be included in the income of the more than 2 percent owner, who may claim the premium deduction as an above-the-line self-employed health insurance deduction. The amount of the deduction is the lesser of the LTC premium or the attained-age limit for the relevant year. In addition, the deduction may only be taken if the owner is a current employee of the S corporation.

Table 1

Attained-age before the close of the taxable year	2024 limit	2025 limit
40 or less	$470	$480
41-50	$880	$900
51-60	$1,760	$1,800
61-70	$4,710	$4,810
71+	$5,880	$6,020

Source: IRC Section 213(d)(1)(D)

When an S corporation provides LTC coverage to a non-owner employee or to an employee who is a less than 2 percent shareholder, the premium of the LTC product is income tax deductible by the company as compensation, IRC Section 162. The deduction is not limited to the attained-age limit for the relevant year. The deduction can be taken for premiums paid for the employee or the employee's spouse and dependents, IRC Section 152 without regard to subsections (b)(1), (b)(2), and (d)(1)(B) of IRC Section 152.

Income tax consequences of premiums paid — employee/participant (owner of policy)

The amount of LTC premium a member of the valid class may deduct from their individual taxes depends on their level of ownership in the S corporation.

An employee who is a more than 2 percent shareholder in the S corporation is taxed as a self-employed individual and must include the LTC premium in their adjusted gross income. The shareholder may deduct a portion of their LTC premium as an above-the-line self-employed health insurance deduction. The amount of the deduction is the lesser of the LTC premium or the attained-age limit for the relevant year, IRC Section 213(d)(10). Please note: this is an above-the-line deduction, which means the shareholder does not need to itemize their taxes to take the deduction.

For a member of the valid class who is a non-owner employee or an employee who is a less than 2 percent shareholder, the LTC premium provided under an accident and health plan may be excluded from their income, IRC Section 106. The amount excluded from income is not limited to the attained-age limit for the relevant year. This exclusion rule includes amounts paid to the employee and the employee's spouse and dependents, IRC Section 152 without regard to subsections (b)(1), (b)(2), and (d)(1)(B) of IRC Section 152. The employee is prohibited from taking an income tax deduction on Form 1040, Schedule A for the LTC premium.

Family attribution rules

It's important to note that if a shareholder who owns more than 2 percent of an S corporation has an immediate family member who is also an employee at the company, it's likely the family member will also be characterized as a more than 2 percent shareholder of the S corporation, IRC Section 318.

Partnerships (also Limited Liability Companies taxed as a Partnership)

Deductibility of premiums paid – company

The amount of LTC premium the company may deduct for each member in the valid class depends on whether the member is a partner or employee of the partnership.

For a member of the valid class who is a partner in the company, the LTC premium can only be deducted if it qualifies as a guaranteed payment, IRC Section 707(c). As the name suggests, guaranteed payments are not contingent on the income of the partnership. And because partners in a partnership are not employees, the cost of the LTC coverage must be added back to the partner's income.

For a member of the valid class who is an employee (not a partner), the premium of the LTC product is income tax deductible by the company as compensation, IRC Section 162. The deduction can be taken for premiums paid for the employee and the employee's spouse and dependents, IRC Section 152 without regard to subsections (b)(1), (b)(2), and (d)(1)(B) of IRC Section 152. The deduction is not limited by the attained-age limit for the relevant year.

Income tax consequences of premiums paid – employee/participant (owner of policy)

The amount of LTC premium a member of the valid class may deduct from their individual taxes depends on whether they are a partner or an employee.

Partners are treated as self-employed and can personally deduct the LTC premium as an above-the-line self-employed health insurance deduction. The amount of the deduction is the lesser of the LTC premium or the attained-age limit for the relevant year (see Table 1). This is not an itemized deduction and allows the deduction to be taken even if the individual's medical expenses do not exceed 7.5 percent of their adjusted gross income for that year.

For a member of the valid class who is an employee, the LTC premium provided under an accident and health plan may be excluded from their income, IRC Section 106. The amount excluded from income is not limited to the attained-age limit for the relevant year. This exclusion rule includes amounts paid to the taxpayer, and the taxpayer's spouse and dependents, IRC Section 152 without regard to subsections (b)(1), (b)(2), and (d)(1)(B) of IRC Section 152. Of course, the employee is prohibited from taking an income tax deduction on Form 1040, Schedule A for the LTC premium.

Sole-Proprietors/Self-Employed

Deductibility of premiums paid – company

A self-employed individual may take a deduction as an above-the-line self-employed health insurance deduction. The amount of the deduction is the lesser of the LTC premium or the attained-age limit for the relevant year (see Table 1). The income tax deduction may be taken for the taxpayer, the taxpayer's spouse and the taxpayer's dependents, IRC Section 152(f)(1).

For a member of the valid class who is an employee of a sole proprietor, the LTC premium can be deducted from the company's income taxes as compensation, IRC Section 162. The deduction can be taken for premiums paid for the employee, employee's spouse and dependents, IRC Section 152 without regard to subsections (b)(1), (b)(2), and (d)(1)(B) of IRC Section 152. The deduction is not limited by the attained-age limit and is taken on Form 1040, Schedule C.

Income tax consequences of premiums paid – employee/participant (owner of policy)

A self-employed individual may take a deduction as an above-the-line self-employed health insurance deduction. The amount of the deduction is the lesser of the LTC premium or the attained-age limit for the relevant year (see Table 1). The income tax deduction may be taken for the taxpayer, the taxpayer's spouse and the taxpayer's dependents, IRC Section 152(f)(1).

For an employee, the LTC premium provided under an accident and health plan may be excluded from their income, IRC Section 106. This exclusion rule includes amounts paid to the taxpayer, and the taxpayer's spouse and dependents, IRC Section 152 without regard to subsections (b)(1), (b)(2), and (d)(1)(B) of IRC Section 152. The employee is prohibited from taking an income-tax deduction on Form 1040, Schedule A for the LTC premium.

Please keep in mind that the primary reason to purchase a life insurance product is the death benefit.

Life insurance products contain fees, such as mortality and expense charges, and may contain restrictions, such as surrender periods.

This information is a general discussion of the relevant federal tax laws provided to promote ideas that may benefit a taxpayer. It is not intended for, nor can it be used by, any taxpayer for the purpose of avoiding federal tax penalties. Taxpayers should seek the advice of their own advisors regarding any tax and legal issues specific to their situation.

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