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better prepare for the potential costs of long-term care—here are three to consider.

Daniel F. Rahill • Jul. 12, 2023

With Americans living longer, long-term care insurance has become increasingly popular as a hedge against a financial catastrophe late in life due to age, injury, illness, or cognitive impairment. Notably, the cost of a private room in a nursing home can exceed $100,000 per year, and the cost of in-home health care can be even higher. In other words, it's important to have either insurance or another plan in place to pay for these rising expenses.

Of course, one option is to self-insure (i.e., saving enough to cover the costs of care

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consider.

1. HEALTH SAVINGS ACCOUNTS

A health savings account (HSA) is one of the most tax-efficient ways to save for long-term care costs. Created in 2003, HSAs provide significant tax savings, rollover of funds, and investment opportunities, making them a key element of any long-term care self-insurance plan, especially for younger individuals. HSAs also offer triple-tax savings:

1. Contributions to HSAs are made pre-tax or are tax-deductible, which means the taxable income is reduced for the individual.
2. Earnings from investments in HSAs grow tax-free, which means there's no tax on interest, dividends, or capital gains.
3. Distributions from HSAs for qualified medical expenses are tax-free, which means there's no tax on withdrawals if they're used for health care purposes.

For 2023, the maximum amount that an individual can contribute to an HSA is $3,850 and $7,750 for family coverage. If an individual is 55 years of age or older, an extra $1,000 catch-up contribution can be made. A taxpayer typically has until the tax filing deadline to contribute.

Additionally, HSAs allow individuals to roll over their unused funds from year to year. This allows individuals to accumulate and grow their tax-free savings. HSAs are also portable, which means that individuals can keep their accounts even if they change employers, health plans, or retire.

Individuals can also invest their HSA funds in various mutual funds or other securities that often offer higher returns than traditional savings accounts. This can help individuals grow their savings faster and better prepare for future medical

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plan (HDHP) with 2023 minimum deductibles of $1,500 for an individual and $3,000 for family coverage. HDHPs have lower premiums than traditional health plans because they have higher deductibles, which allows employers who offer HDHPs with HSAs to their employees to save money by reducing their payroll taxes and health care costs.

Of course, there are limitations to HSAs. An individual can't have any other health coverage, such as Medicare, so those who go on Medicare at age 65 can no longer contribute to an HSA. Also, the HSA owner can't be claimed as a dependent on someone else's tax return, and a 20% penalty applies if funds are withdrawn from the HSA for non-qualified medical expenses before the age of 65.

2. EMPLOYER-PAID LONG-TERM CARE INSURANCE

IRC Section 106 allows employers to exclude from their employees' income the cost of qualified long-term care insurance premiums, while the employer may deduct the premiums as an ordinary business expense.

To qualify for this exclusion, the long-term care insurance policy must be purchased from a qualified insurance company, and the policy must provide coverage for either skilled nursing care, intermediate care, home health care, or adult day care. The policy must have a maximum daily benefit of not more than $3,000 and must have a lifetime maximum benefit of not more than $200,000.

For example, if an employer provides an employee with a long-term care policy that includes a life insurance benefit (should the employee pass away without ever utilizing the long-term care benefit), the premium would be split into two main components: the long-term care premium cost and the life insurance benefit cost. The employer would be able to deduct both components of the premium, but only the life insurance component would be taxable to the employee.

This exclusion doesn't apply to premiums paid for long-term care insurance policies

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One provision from the act allows retirement plan participants to withdraw up to $2,500 per year from their plans to pay for long-term care insurance premiums without having to pay a 10% early withdrawal penalty. These withdrawals will still be subject to ordinary income taxation.

To qualify for this benefit, the long-term care insurance policy must provide at least three years of coverage, have a daily benefit of at least $100, and have an inflation rider that increases the daily benefit by at least 5% annually.

529 Plan Roth IRA Rollovers

Beginning in 2024, beneficiaries of 529 college savings plans will be allowed to roll over up to $35,000 of their funds to a Roth IRA, free of taxes and penalties. The 529 plan is a valuable option for those who can save more than needed for education, either intentionally or unintentionally. That's because the strategy combines the tax-free growth advantages of a 529 savings plan, including possible state tax benefits, with the tax-free growth and withdrawal benefits of a Roth IRA. For a young individual with an over-funded 529 plan, this could be an excellent long-term care self-insurance strategy.

For example, let's consider a student who rolls over $35,000 from a 15-year-old 529 plan into a Roth IRA upon college graduation at age 22. By the time this individual reaches age 67 (current retirement age), that amount will likely have grown to more than $600,000, assuming a 7% annual compounded growth rate and a $6,500 contribution per year (2023 limitation) up to the $35,000 cap.

To be eligible, the 529 plan must have been in existence for at least 15 years, the rollover is subject to the annual Roth IRA contribution limits, and only the earnings on the 529 plan funds are eligible for the rollover; original contributions and contributions made within the last five years are ineligible.

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As you can see, there are many cost-saving strategies beyond traditional long-term care insurance. Keep these strategies top of mind to provide added value to your clients as you help them prepare for life's unexpected circumstances.

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