

Ways To Deduct Health Insurance

Article Highlight:

- Itemized Deduction
- AGI Limitations
- What Insurance Is Deductible
- Above-The-Line Deduction for the Self-Employed
- Income Limitation
- Subsidized Limitation

Health insurance premiums, especially in the wake of the "Affordable Care Act," have risen dramatically and are one of the largest expenses that most individuals pay. Although the cost of health insurance is allowed as part of an individual's medical deductions when itemizing deductions, only the amount of total medical expenses that exceed 10% of the taxpayer's adjusted gross income (AGI) is deductible. The 10% limitation is reduced to 7.5% through 2016 where a taxpayer or spouse (if any) is age 65 or over as of the end of the year. Prior to the increased limitation imposed by the "Affordable Care Act," the limitation was 7.5% for everyone.

The purpose of this article is twofold: first, to remind you what insurance can be included as a medical deduction, and second, to inform you of an alternate means of deducting health insurance for certain self-employed individuals—a means that avoids the AGI limitation and allows for deduction without itemizing.

Let's start by looking at what is treated as deductible health insurance. It includes the premiums you pay for coverage for yourself, your dependents, and your spouse, if applicable, for the following types of plans:

- Health Care and Hospitalization Insurance
- Long-Term Care Insurance (but limited based upon age)
- Medicare-B
- Medicare-C (aka Medicare Advantage Plans)
- Medicare-D
- Dental Insurance
- Vision Insurance
- Premiums Paid through a Government Marketplace net of the Premium Tax Credit

However, premiums paid on your or your family's behalf by your employer aren't deductible because their cost is not included in your wage income. Or, if you pay premiums for coverage under your employer's insurance plan through a "cafeteria" plan, those premiums aren't deductible either because they are paid with pre-tax dollars.

If you are a self-employed individual, you can deduct 100% (no AGI reduction) of the premiums without itemizing your deductions. This above-the-line deduction is limited to your net profits from self-employment. If you are a partner who performs services in the capacity of a partner and the partnership pays health insurance premiums on your behalf, those premiums are treated as guaranteed payments that are deductible by the partnership and are includible in your gross income. In turn, you may deduct the cost of the premiums as an above-the-line deduction under the rules discussed in this article.

No above-the-line deduction is permitted when the self-employed individual is eligible to participate in a "subsidized" health plan maintained by an employer of the taxpayer, the taxpayer's spouse, any dependent, or any child of the taxpayer who hasn't attained age 27 as of the end of the tax year. This rule is applied separately to plans that provide coverage for long-term care services. Thus, an individual eligible for employer-subsidized health insurance may still be able to deduct long-term care insurance premiums, as long as he isn't eligible for employer-subsidized long-term care insurance. In addition, to be treated as subsidized, 50% or more of the premium must be paid by the employer.

This above-the-line deduction is also available to more-than-2% S corporation shareholders. For purposes of the income limitation, the shareholder's wages from the S corporation are treated as his or her earned income.

If you have any questions related to deducting health insurance premiums, either as an itemized deduction or an above-the-line deduction for self-employed individuals, please give this office a call.