

LTC Planning

Frequently Asked Questions About Long Term Care Insurance and Trusts

When could owning a long term care insurance (LTCi) policy result in something being included in the gross estate?

A: When an insured owns a LTCi policy that includes a refund of premium (the full nonforfeiture rider), the total balance that is the refund of premium is an includible asset in the insured's estate.

Can the policy owner remove the refund of premium from his/her estate by naming someone else as the beneficiary?

A: Inclusion in the gross estate is a consequence of ownership. The beneficiary designation for the refund of premium does not alter this.

Is it possible to exclude the refund of premium if the policy is owned by a trust?

A: Some insurers allow ownership of a qualified LTCi by a person other than the insured. If the owner of the LTCi policy is an irrevocable grantor trust, then the refund of premium will not be an includible asset in the insured's estate as long as the trustee is not obligated to pay the insured's long term care expenses or make any distributions to the insured.

What special provisions would need to be in a trust where the intent is to keep the refund of premium out of the insured's estate?

A: The trust should contain provisions giving the trustee discretionary power (but not the obligation) to make distributions to named beneficiaries. The insured cannot be a beneficiary.

How would the insured pay for long term care expenses if care were needed?

A: Long-term care benefits are always paid to the policy owner. If the LTCi policy is owned by a trust, then the benefits are paid to the trust if the insured goes on claim. This means the insured will need to cover his long term care expenses from resources outside the trust. However, if the trustee can make discretionary distributions to the trust beneficiaries, then another strategy may be available. IRC Sec. 2503(e) provides an unlimited gift tax exclusion for amounts paid for medical care (as defined in IRC Sec. 213(d)) of another person. This exclusion is available in addition to the annual gift tax exclusion. Furthermore, this exclusion is permitted without regard to the relationship between the donor and the donee. Apparently, as long as the trust beneficiaries pay the long term care provider directly for the insured's expenses, these payments should qualify for the unlimited medical care gift tax exclusion.

What are considerations in having a trust own a LTCi policy?

A: Only a qualified attorney can draft the trust. Consequently, there are expenses associated with drafting and maintaining the trust. The availability of resources outside the trust to pay the long term care expenses should also be considered. Additionally, if the beneficiaries do pay the insured's long-term care expenses, the IRS may apply the step transaction doctrine (based on the facts and circumstances surrounding the transaction) to collapse the transaction resulting in the inclusion of the refund of premium in the insured's estate.

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