

Self-employed individual's deduction for health insurance costs

Self-employed taxpayers can deduct 100% of their health insurance costs in computing their income taxes. This tax savings can reduce your after-tax cost of health coverage.

A brief review of the tax rules on health insurance premiums may be useful. Health insurance premiums paid by non-self-employed taxpayers are deductible as itemized medical expense deductions, but, only to the extent your total medical expenses exceed 7.5% of your adjusted gross income (AGI).

Because of the “floor” that applies to the medical expense deduction, if total medical expenses don't exceed the percentage-of-AGI limitation, no itemized deduction is available.

However, a self-employed taxpayer *can* deduct—as an “above the line” deduction, reducing AGI—100% of the health insurance costs for the taxpayer, spouse, and dependents, and for any child of the self-employed taxpayer who is under age 27 as of the end of the tax year.

Example. M, who is self-employed, pays \$4,500 in health insurance premiums and has no other medical expenses. M's AGI is \$80,000. Since 7.5% of \$80,000 equals \$6,000, M could not claim an itemized medical expense deduction for the health insurance premiums. But, since M is self-employed, M can deduct the entire \$4,500 above the line.

The health insurance deduction for self-employed individuals only applies for any calendar month in which you aren't otherwise eligible to participate in any subsidized health plan maintained by any employer of yours or of your spouse, or any plan maintained by any employer of your dependent or your under-age-27 child.

Also, the deduction can't exceed your earned income from the trade or business for which the health insurance plan was established.

These rules also apply to partners in partnerships and more-than-2% shareholders of S corporations where the partnership or corporation pays for health insurance coverage for its partners or shareholders.

The tax benefits of a self-employed individual's health insurance costs can effectively reduce your cost of health insurance. You may wish to consider stepping up your coverage in light of these savings. Please consult your tax advisor for how these rules may impact you specifically. Your individual circumstances may require further analysis or consideration of how these rules interact with other elements of your overall tax situation.