Tax help in caring for your aging parent

By Kay Bell • Bankrate.com

They took care of you for years. Now it's your turn.

Millions of adult children find themselves looking after aging parents. Tax laws offer some help, as long as you and your folks meet the criteria.

The key to Internal Revenue Service assistance in caring for an elderly relative is whether you can claim the person as a dependent. Any dependent must meet certain tests. While there is a little flexibility when dealing with children, fewer exceptions are granted when the potential dependent is older.

Despite the qualification obstacles, it doesn't hurt to explore whether you can claim your parent as a dependent. If you and your parent meet IRS requirements, you'll be able to claim an added personal exemption on your income tax return. This filing season, each exemption allows you to reduce your taxable income by $3,400.

Then there are possible deductions and credits. If you pay medical expenses for a dependent parent, you may be able to deduct some of those costs. Hire a caregiver to help you out and a credit could cut your tax bill a bit more.

Dependency hurdles

The highest dependency hurdle is the amount of income your older parent earns. A dependent parent cannot make more than the exemption amount. This is that $3,400 mentioned earlier. (Here's where kids get a break. This is not a test for a young dependent under the uniform definition of a qualifying child.)

The income barrier represents taxable income, notes John W. Roth, a federal tax analyst with CCH Inc., a national tax and business-law publisher.

"Social Security normally is excludable, but if they have other income, which in many cases means interest and dividends, some is taxable," Roth says. "So you want to start with that first in determining if the parent meets the income test.

"It's amazing how that generation has invested in stocks, bonds, savings accounts, and how quickly it can add up," says Roth. "And it's not even market-based income. If you have 10 accounts with $10,000 to $25,000 each earning even just 2.5 percent interest, it adds up."

Such disciplined saving habits mean that many adult children cannot claim mom or dad as a dependent. If, however, you and your parent meet the income standard, the next consideration is how much support you provide.

Paying for more than half
To be deemed a dependent for tax purposes, your parent must get more than half of his or her support from you.

"When the parent lives in your home, to reach the 50-percent-plus threshold, you should take into account the fair-market room rental, food, medicine and other little support items," says Roth. "This is where Social Security does come into play. If a parent is using benefits to pay for some of these support items, it goes into the calculation of whether you cover more than half of your parent's support costs.

"Say mom doesn't have $3,400 taxable income, but gets $15,000 in Social Security and uses it to pay for some medicine and buy clothes. In that case, your contribution to her support may not come up to half."

The one bit of wiggle room here is that your parent doesn't have to live with you. When a parent is able to remain in his or her own house, in an assisted living facility or a nursing home, costs you pay for parental support at those locations count toward meeting the IRS requirement.

Be careful, though, in determining what is support. Uncle Sam may not agree with what you and your parent consider vital. For example, items such as furniture, appliances or even cars can in some instances be counted as support; other times the IRS says "no." Check IRS Publication 501, Exemptions, Standard Deduction, and Filing Information for details and examples. The booklet also contains a work sheet to help you figure your support contributions.

Counting medical care and other costs
Once your parent does meet the IRS dependency tests, you can use any medical expenses you pay for mom or dad toward this itemized deduction. Because medical costs must exceed 7.5 percent of your adjusted gross income before you can claim them, a parent's added expenses could help you meet the requirements.

And the IRS offers a little leeway here. If your parent isn't considered a dependent for exemption purposes simply because he or she earned too much but met the other tests, the IRS says mom or dad could still be counted as a dependent for medical deduction purposes.

When adding up those parental medical costs, don't forget premiums for supplementary Medicare coverage or long-term care insurance. Once your parent is your dependent, some of these payments that you make can be counted toward your deductible medical expenses.

But the precise amount of long-term care policy payments that you can add to your medical expenses is limited by your parent's age. They range from a low of $290 for coverage of a parent age 40 or younger to $3,680 for a policy beneficiary age 71 or older. In between, the IRS says you can count $550 spent on a policy for someone between ages

41 and 50; $1,110 for coverage of a person from ages 51 to 60 years; and $2,950 for a dependent aged 61 to 70.

And if your dependent parent lives with you and requires continual care, Roth says, you may be eligible for another tax break. What you spend for this attention generally won't count toward the medical deduction. But if it's necessary so that you can go to work, you can claim the dependent care credit.

There is a limit to the amount of care costs you use to figure the dependent care credit; this tax year it could be as much as $3,000. Even then, you can only claim a percentage of your costs based on your income level.

"But since it's a credit," notes Roth, "it's a dollar-for-dollar tax break. There also are a growing number of elder care day facilities that would count toward the credit."

Siblings sharing support

Sometimes you don't have to shoulder the load alone. Many adult children get help from siblings in caring for mom and dad.

Not only does this help maintain your day-to-day bank balance, it also spreads out any tax breaks. Where none of you solely pays for half of a parent's support, but each contributes at least 10 percent toward parental care, take a look at the IRS's multiple-support declaration. This form helps you account for the tax implications of a shared-care arrangement.

Roth offers this example: Mom is in a nursing home. Her Social Security covers 40 percent of the facility's costs, and you and your two brothers split the remainder, each paying 20 percent. Since more than half of her support comes from her three kids, she can be claimed as a dependent -- but by only one of you. That choice is left to you and your brothers.

After you and your brothers agree that you can claim Mom as a dependent this tax year, file Form 2120, Multiple Support Declaration with your tax return. This form indicates that while several siblings contributed to mom's support, the others waive any tax-exemption claim.

You also need to get signed statements from your brothers acknowledging that they waived their tax claims. You don't have to send these documents with your 1040, but keep them in your records in case the IRS ever questions your exemption or medical deduction claims.

And the best news about a multiple support agreement is that it's not permanent.

"You can rotate it around from tax year to tax year," says Roth. "The next year, another sibling takes the responsibility and the third brother the next year. It softens the blow, but it's not going to cover all that it's going to cost you."

Plan first, then look for tax breaks
Because of the staggering (and ever-increasing) costs, Roth emphasizes that families need to preplan for parental care and the associated tax opportunities.

This is especially important when a multiple-support agreement is utilized. Make sure the year you claim Mom as a dependent, you, not your siblings, pay her medical costs so that you get the full tax-deduction benefit. Any medical payments a sibling makes, while helpful, will do neither of you any tax good.

"There really isn't a lot out there for this sandwich generation," says Roth. "However, as this group grows, so, too, will their political clout along with tax relief in the area of help for aging-parent care.

"But tax breaks won't substitute for good financial planning. It's one of the hardest things that children have to do because it deals with finances, but you need to sit down with your parents and siblings and make a plan.

"For years and years these people have taken care of you. Now that is shifting."

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