HB 562

Department of Legislative Services
Maryland General Assembly
2011 Session

FISCAL AND POLICY NOTE

House Bill 562 (Delegate Hubbard)
Ways and Means

Income Tax - Credit for Long-Term Care Premiums

This bill alters the existing one-time long-term care insurance income tax credit of $500 by allowing the credit to be claimed for every year a policy is in force in the amount of $200 in the first taxable year the credit is claimed and $150 in each taxable year thereafter. This change is applicable to policies issued after December 31, 2010. The bill retains the current prohibition on the credit being claimed for individuals who were covered by a long-term care insurance policy at any point before July 1, 2000. The bill terminates the credit effective in tax year 2016.

The bill takes effect July 1, 2011, and applies to tax year 2011 and beyond.

Fiscal Summary

State Effect: General fund revenues increase by $1.4 million in FY 2012 and by $0.4 million in FY 2013, which reflects a net decrease in the amount of credits claimed as a result of decreasing the value of the credit in the first tax year. General fund revenues decrease beginning in FY 2014 as revenue losses from allowing the credit to be claimed in successive years continues to increase and is greater than revenue gains resulting from reducing the value of the credit in the first year. General fund revenues increase by $2.7 million annually beginning in fiscal 2017 due to termination of the credit. Expenditures are not affected.

($ in millions)	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
GF Revenue	$1.4	$0.4	($0.5)	($1.5)	($2.4)
Expenditure	0	0	0	0	0
Net Effect	$1.4	$0.4	($0.5)	($1.5)	($2.4)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: None.

Small Business Effect: Minimal.

Analysis

Current Law: Chapter 242 of 2000 allows taxpayers to claim a credit against the State income tax for no more than $500 of the eligible premiums paid for long-term care insurance for coverage of the individual or the individual's spouse, parent, stepparent, child, or stepchild. The credit may not be claimed by more than one taxpayer with respect to the same insured individual and can only be claimed on behalf of a State resident. In addition, the credit may not be claimed with respect to an insured individual if (1) the insured individual was covered by long-term care insurance at any time before July 1, 2000; or (2) the credit has been claimed by any taxpayer for any individual's long-term care insurance policy in any prior taxable year. Any unused amount of the credit may not be carried forward to any other tax year.

Eligible long-term care premiums are as defined under Section 213 (d)(10) of the Internal Revenue Code. The maximum premium amounts under federal guidelines for tax year 2011, based on the age of the insured, are $340 for age 40 or younger; $640 for ages 41 to 50; $1,270 for ages 51 to 60; $3,390 for ages 61 to 70; and $4,240 for ages 71 and over. These amounts are indexed according to the annual increase in the medical component of the Consumer Price Index for all urban consumers.

Chapter 242 of 2000 also mandated that the Comptroller report annually beginning in 2005 the following information about the tax credit: (1) the number of individuals who have claimed the credit, the amount allowed as credits, and the additional number of individuals covered by long-term care insurance as a result of the credit; and (2) the savings under the State's Medical Assistance Program as a result of additional individuals being covered by long-term care insurance as a result of the credit.

In addition, Chapter 7 of 1998 created a tax credit equal to 5% of an employer's cost for providing long-term care insurance benefits to employees. The credit is capped at $5,000 or $100 per employee covered. This credit may be used by an employer against the public service company franchise tax, the insurance premium tax, or individual and corporate income taxes. If the tax credit exceeds the taxes due for any taxable year, the credit can be carried forward for up to five tax years. This tax credit applies to tax years 1999 and beyond.

The federal Health Insurance Portability and Accountability Act of 1996 established favorable tax treatment for long-term care insurance similar to that granted to accident and health insurance premiums. Employee-paid premiums are treated as unreimbursed medical expenses that are potentially deductible from income along with other unreimbursed medical expenses. As such, if an individual itemizes deductions, the premiums are deductible to the extent that the individual's uncompensated medical expenses exceed 7.5% of the individual's adjusted gross income. The deduction is subject to the annual limitations described in Section 213 (d)(10).

Background: Long-term care typically provides for the medical, social, personal, and supportive services needed by people who have lost some capacity for self-care because of a chronic illness or condition. This includes services provided by nursing homes, hospices, and at-home care but does not include medical care for acute conditions. The population of long-term care recipients includes the elderly, the functionally and developmentally disabled, and individuals suffering from mental disorders such as dementia and Alzheimer's.

Due to the aging of the population, long-term care utilization is expected to increase significantly in the near future. The Kaiser Commission on Medicaid and the Uninsured estimated that of the $169 billion in long-term care spending in 2005, a little less than three-quarters was for nursing home expenditures. In fiscal 2012, State Medicaid nursing home expenditures are projected to total $1.1 billion. In addition, State expenditures for nursing home patients at the State's chronic disease hospitals totaled $19.7 million in fiscal 2010. A recent University of Pennsylvania study noted that the heavy burden on governments to finance long-term care has prompted proposals to make long-term care more affordable through tax incentives. The study concluded that the effectiveness of these proposals in stimulating long-term care insurance depended on the availability of Medicaid and the price elasticity of the insurance. A tax subsidy that reduced the cost of insurance by one-half was estimated to increase the number of long-term care insurance policies by less than 5%.

Chapter 242 of 2000 established a one-time $500 tax credit for the purchase of new long-term care insurance policies in an attempt to promote purchases of these policies. The number of returns claiming the credit and the number and amount of credits claimed are listed in **Exhibit 1.**

Exhibit 1
Long-term Care Insurance Tax Credits
2000-2009

Tax Year	Returns	Credits	Amount Claimed ($ in Millions)	Average Credit Claimed
2000	2,537	3,658	$1.6	$442
2001	5,185	7,032	3.0	433
2002	8,691	12,367	5.1	409
2003	12,756	18,964	8.4	445
2004	6,221	10,238	4.5	442
2005	8,470	11,751	5.3	447
2006	6,192	8,210	3.6	440
2007	6,089	7,778	3.3	431
2008	5,172	6,735	2.9	426
2009	5,081	6,527	2.7	421
Total	**66,394**	**93,260**	**$40.5**	**$434**

The amount reported above is less than the amount that has been reported in past annual reports issued by the Comptroller's Office due to improved data collection and analysis efforts and taxpayers claiming the credit in error. Not included Exhibit 1 is approximately $4.2 million in credits that the Comptroller's Office determined were claimed in error through tax year 2004, representing 8,400 credits and an 18.6% overclaim rate. In 2004, the Comptroller's Office determined that the credit had been claimed more than once for any given insured individual by many taxpayers. Procedures were put in place in 2005 to prevent that from occurring again, including an expansion of the data collected from these returns. In a handful of instances in 2005, credits were claimed in excess of $500 or were claimed for an individual who was not the taxpayer's spouse, child, or parent. According to the Comptroller's Office, these errors were virtually eliminated in tax year 2006 returns because they are now addressed before the return is fully processed.

Most of the credits have been claimed on behalf of individuals between 51 and 64 years old. Through tax year 2005, slightly less than one-quarter of the credits were claimed for an individual who is less than 50 years old (including 691 credits for insureds under 21 years old) and slightly less than one-fifth were claimed on behalf of insureds who were 65 years old and older. Sixty-three percent of credits were claimed on behalf of the taxpayer, 35% on behalf of the taxpayer's spouse, and the remaining 2% on behalf of a taxpayer's parent or child. A majority of the credits were claimed on a return with Maryland adjusted gross income in excess of $100,000.

In addition to reporting data on the amount of credits claimed in each year, Chapter 242 also required the Comptroller's Office to report the savings under the State medical assistance program as a result of additional individuals being covered by long-term insurance as a result of the credit. The report states that although the additional number of individuals who are covered by insurance as a result of the credit is unknown, little if any savings to the State are likely at this point.

State Revenues: The bill alters the existing tax credit beginning in tax year 2011 by allowing individuals to claim the credit for every year the policy is in effect at a maximum of $200 in the first year and $150 annually beginning in the second year, instead of allowing a one-time credit of $500 as provided under current law. This change is applicable to individuals who were not covered by long-term insurance at any time before January 1, 2011. As a result, general fund revenues will increase by an estimated $1.4 million in fiscal 2012 and by $438,000 in fiscal 2013. State revenues will decrease beginning in fiscal 2014 as revenue losses from allowing the credit to be claimed each year the policy is in effect are greater than revenue gains resulting from decreasing the value of the credit in the first year.

This estimate is based on the following facts and assumptions:

- It is estimated that, under current law, a total of $2.7 million in credits will be claimed annually beginning in tax year 2011.
- An average credit of $421 was claimed in tax year 2009 – it is assumed that the maximum credit proposed by the bill will be claimed in each year.
- The price elasticity of long-term insurance policies is estimated to be -0.08.
- The estimated number of policies in force in successive years is based on the renewal rates of long-term care insurance policies as reported by the Society of Actuaries.

The bill terminates the credit beginning in tax year 2016. As a result, general fund revenues will increase by $2.7 million annually beginning in fiscal 2017.

The bill provides a substantial incentive for individuals to buy long-term care insurance by subsidizing a significant portion of the premium. As a result, revenue reductions could be higher than estimated.

Additional Information

Prior Introductions: Similar bills were introduced in the 2010 session. HB 382 received a hearing in the House Ways and Means Committee, but no further action was taken. Its cross file, SB 460, received a hearing in the Senate Budget and Taxation Committee, but no further action was taken.

Cross File: None.

Information Source(s): Comptroller's Office, Internal Revenue Service, Kaiser Commission on Medicaid and the Uninsured, Society of Actuaries, University of Pennsylvania, Department of Legislative Services

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