F I S C A L   I M P A C T   R E P O R T

ORIGINAL DATE 2/06/2020
SPONSOR Trujillo, C. **LAST UPDATED** 2/13/2020 **HB** 291

SHORT TITLE Long-Term Care Insurance Tax Credit **SB**

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY20	FY21	FY22	FY23	FY24		
	($48,200.0)	($48,200.0)	($48,200.0)	($48,200.0)	Recurring	General Fund

Parenthesis ( ) indicate revenue decreases

Estimated Additional Operating Budget Impact*				R or NR**	Fund(s) or Agency Affected
FY2020	FY2021	FY2022	FY 20-22		
--	$10.3	--	$10.3	Nonrecurring	TRD-Information Technology Division
$29.3	$58.5	$58.5	$146.3	Recurring	TRD-Revenue Processing Division

* In thousands of dollars. Parentheses ( ) indicate a cost saving. ** Recurring (R) or Non-Recurring (NR).

Note: an estimated 23,000 to 27,500 returns would claim this tax credit. This would require some nonrecurring programming, developing forms and instructions and developing a procedure to verify that LTC premiums had actually been paid. TRD will report these nonrecurring costs.

SOURCES OF INFORMATION

LFC Files

Responses Received From
Office of the Superintendent of Insurance (OSI)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

House Bill 291 creates a 100 percent tax credit for the premiums paid for long-term care insurance. This is a non-refundable credit and has no roll-over features. The maximum amount of credit is limited to the amount of the personal income tax liability for the year in which the premiums were paid. The credit must be claimed within one year following the end of the year in which the premiums were paid. The Human Services Department is required to certify the taxpayer’s purchase of approved long-term care insurance. This certification is apparently annual. After the taxpayer receives the certification, this certificate is attached to the next filed tax return, which must be filed within a year of the end of the tax year in which the LTC insurance premiums are paid.

There is no effective date of this bill. It is assumed that the effective date is 90 days after this session ends (May 20, 2020). The provisions of the bill are applicable to tax years beginning on or after January 1, 2020. Tax returns for the 2020 tax year are generally filed by April 15, 2021.

FISCAL IMPLICATIONS

This bill may be counter to the LFC tax policy principle of adequacy, efficiency, and equity. Due to the increasing cost of tax expenditures, revenues may be insufficient to cover growing recurring appropriations.

Generally, estimating the cost of tax expenditures is difficult. In this case, however, the Superintendent of Insurance has reported that the premium volume in NM for LTC insurance was $47.6 million in 2017 and $46.3 million in 2018.

The OSI also reports that this tax credit would likely incentivize more people to purchase LTC insurance to offset their tax liability, although many individuals in the state have no tax liability and would receive no credit, or have insufficient tax liability to absorb the full amount of tax credit available.

Premiums depend on age and health condition at the time of initial purchase.

> An estimated LTC premium for a healthy 50-year-old man is $1,725 per year. If the policy remains in effect until this person is 95, he can spend approximately $77,625 in LTC premiums. For a healthy 60-year-old man, an estimated premium is $2,170. If he keeps the policy until he's 95, it can cost him $75,320 overall.[1]

Assume an average annual premium of $2,000 per individual. This then represents a current population of about 23,000 individuals covered by LTC. This is probably divided by about two-thirds to married couples and one third to singles or heads of household.

In order to determine the average or median tax liability, LFC staff calculated the following for the Taxable Social Security recipients. This may be the approximate population that would respond to the incentive provided by this bill.

	#	Average Tax	Approx Median
MFJ & HoH	73,154	$4,150	$3,267
Single & MFS	62,979	$2,355	$847

Thus, the single population of social security recipients (46 percent) would have a median reduction in the net cost of LTC insurance of about 40 percent ($847/$2,000) and the married population would have a median reduction of about 80 percent ($3,267/$4,000). Assuming a price elasticity of about .5 might stimulate an increase in purchasers of LTC of about 1,500 singles and 6,000 married joint and head of household filers. Further assume that 80 percent of the cost for current purchasers of LTC would be realized as a tax credit. The net general

[1] https://www.daveramsey.com/blog/who-needs-long-term-care-insurance

fund cost would then be as shown in the table, divided roughly into $36 million to buy the base and $12 million in incentivize individuals to purchase long-term care insurance. The average cost for each new purchaser of LTC is then about $6,500, or more than three times the cost of premiums for each new entrant. This incentive may grow the base, but may be a declining stimulus. The fact that relatively few New Mexicans currently are covered by LTC insurance means that the average income of New Mexicans may not be adequate to support this insurance purchase. The incentive will only make a moderate increase in the covered population and the new entrants each year will be correspondingly modest. The cost of buying the base, however, will not decrease. Therefore, the general fund cost to induce a new entrant into the pool will rise.

TRD extended the analysis to consider additional data and issues:

The Office of the Superintendent of Insurance (OSI) provided the 2017 and 2018 *Long-Term Care Insurance Experience Reports for 2018* from the National Association of Insurance Commissioners (NAIC). Among the data collected by NAIC are the associated long-term care premiums earned and inforce count by insurance company, state and year. Inforce count meaning policyholders who are current in paying their premiums. In 2017, there were 41,050 individual and group premium holders in New Mexico with the total premium amount at $47.6 million. In 2018, there were 40,011 individual and group premium holders in New Mexico with the total premium amount at $46.3 million.

TRD assumes in the first year of the credit, the current New Mexico policyholders will all qualify for the credit. TRD assumed federal adjusted gross income (AGI) for this population based on the median income of $87,500 for the national population which purchases long-term care insurance.[2] Whether filing as married-jointly or as single, the PIT liability would exceed both the average annual individual or group premium amount in New Mexico assuming the taxpayers only take the standard deduction. TRD averaged 2017 and 2018 earned premiums to arrive at $47 million for FY2021.

As discussed in the "Policy Issues" only a small percentage of Americans purchase long-term care insurance despite the fact that a majority of individuals will need some care after the age of 65. Researchers continue to research this contradiction. A study by Harvard Medical School professors, looked at the specific impact of tax incentives and the take-up rate of long-term care insurance.[3] Their study found mixed results. States with tax incentives generally had higher take-up rates compared to states with no tax incentives, but these tax incentives explained very little of over-all take-up rates. Significantly, comparing states with high and low tax incentives did not produce substantial differences, i.e. higher take-up rate of insurance with higher tax incentives. The proposed credit in this bill would put New Mexico in a category of a high tax incentive. The researchers did caution though that there sample size reduces the reliability of this finding. Other factors also influence the take-up rate of insurance: the type of benefits provided in a plan, individuals' engagement in comprehending potential future long-term care costs, and general knowledge of insurance options for long-term care. Given such uncertainty on the impact of this credit on future take-up rates for long-term care insurance, TRD has kept the revenue impact for the

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[2] "The State of Long-Term Care Insurance: The Market, Challenges and Future Innovations", National Association of Insurance Commissioners and The Center for Insurance Policy and Research, May 2016.

[3] Stevenson, David G., Frank, Richard G. and Tau, Jocelyn. "Private Long-Term Care Insurance and State Tax Incentives," *Inquiry Journal,* Vol. 46: 305-321, Fall 2009.

forecast period. TRD cautions that the cost could substantially grow given the baby boomer population which is the U.S. population born post-World War II up until mid-1964. The baby boomers started reaching the age of 65 in 2011 and are increasing the percentage of the population over the age of 65. By 2029, all baby boomers will be over the age of 65 and will represent 20 percent of the U.S. population.[4]

The Fiscal Impact in the table averages the LFC ($49,400) and TRD estimates (47,000).

SIGNIFICANT ISSUES

Information from DaveRamsey.com.[5]

- 52 percent of people turning 65 today will need long-term care at some point?
- Statistically, 89 percent of LTC claims are filed for people over age 70.
- Medicare does not cover long-term care costs.
- Medicaid does cover long-term care, but you must strip your assets and reduce your annual income to qualify. This may end up being prosecuted for a federal crime of fraud.

With only an estimated 23,000 individuals currently covered by long-term care insurance, the statistics above indicate a growing problem, particularly as the population ages.

TRD contributed an expanded consideration of this proposal:

> Under Internal Revenue Service (IRS) code and current New Mexico exemptions and credits, expenditures for long-term care insurance already qualify for a reduction in tax liability through several statutes.
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> The Internal Revenue Service (IRS) has a deduction for qualified long-term care premiums that can be included in the medical expenses deduction on Form 1040 Schedule A Itemized Deductions. The medical expenses must exceed 10 percent of Adjusted Gross Income (AGI) for 2010 and beyond in order to itemize the expenses. If the taxpayer qualifies for the IRS deduction, they will already be reducing their taxable income by that amount in their itemized deduction that flows through to New Mexico, and then would also realize a tax credit on the same expenses on the New Mexico return.
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> IRS Deduction Limits for Long Term Care Insurance Premiums (per person)[6]:

Taxpayer's age at end of tax year	Deduction Limit
40 or less	$420
More than 40 but not more than 50	$790
More than 50 but not more than 60	$1,580
More than 60 but not more than 70	$4,220
More than 70	$5,270

> New Mexico has a series of statutes providing for an exemption, credit and deduction for

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[4] The Baby Boom Cohort in the United States: 2012 to 2060 – Population Estimates and Projections, Colby, Sandra L. and Ortman, Jennifer M., May 2014, U.S. Census Bureau publication P25-1141.

[5] https://www.daveramsey.com/blog/who-needs-long-term-care-insurance

[6] https://apps.irs.gov/app/vita/content/00/00_25_005.jsp?level=advanced

unreimbursed or uncompensated medical care expenses. New Mexico statutes 7-2-5.9 and 7-2-18.13 NMSA 1978 extend an exemption and credit for individuals sixty-five years of age or older. Statute 7-2-37 NMSA 1978 allows for a deduction for all taxpayers but is contingent on filing status and adjusted gross income (AGI).

All three statutes include under the definition of medical care expenses, insurance for a qualified long-term care insurance contract. The insurance must be paid from income included in the taxpayer's adjusted gross income (AGI) for the taxable year. As with the IRS deduction, this new credit will allow an additional reduction in tax liability for the same expenses.

The National Association of Insurance Commissioners and the Center for Insurance Policy and Research produced a joint report, *The State of Long-Term Care Insurance: The Market, Challenges and Future Innovations*[7] which provides a broad range of research in this insurance field. The report summarizes the population purchasing long-term care insurance. The median income in 2010 was $87.5 thousand and 77 percent of the population has an income greater than $50 thousand. Also very importantly, this population has median assets of $325 thousand with 82 percent of the population having assets over $75 thousand. Thus the population who would financially benefit immediately from this new credit tend to be high earning individuals.

Many states have tax incentives associated with long-term care insurance premiums. These incentives range from mirroring the federal deduction outlined above at the state level to a credit similar to the proposed credit in this bill. States that have a credit tend to cap the amount of the credit. Minnesota caps the credit at $100 per beneficiary, $200 for married filing jointly. The aforementioned report, cites that the incentives tend to have too low of a benefit to incentive the purchase of long-term care insurance for middle- or low-income individuals. The credit proposed in the bill would extend the credit amount to the full amount of premiums paid in a taxable year which may serve as a substantial enough incentive for middle-income individuals. Low-income taxpayers whose other deductions and exemptions results in no taxable income will not be able to take advantage of this credit as it is neither refundable nor can be carried forward. Taxpayers who have a loss would also be unable to benefit.

States have a large financial incentive to research policy concerning long-term care and reaching middle-income individuals. The U.S. Department of Health and Human Services states that if people make it to the age 65, 70 percent of them will need some form of long-term care services at some stage.[8] Yet in 2014, only 3 percent of funding for long-term care came from long-term care insurance and 6 percent from other insurance. The largest funding source is Medicaid, 33 percent of long-term care expenditures in 2014.[9] Medicaid

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[7] "The State of Long-Term Care Insurance: The Market, Challenges and Future Innovations", National Association of Insurance Commissioners and The Center for Insurance Policy and Research, May 2016.

[8] "The State of Long-Term Care Insurance: The Market, Challenges and Future Innovations", National Association of Insurance Commissioners and The Center for Insurance Policy and Research, May 2016. Cited, U.S. Department of Health and Human Services, *http://longtermcare.gov/the-basics/who-needs-care*

[9] "The State of Long-Term Care Insurance: The Market, Challenges and Future Innovations", National Association of Insurance Commissioners and The Center for Insurance Policy and Research, May 2016. Cited the National Health Expenditures Survey compiled by the Centers for Medicare & Medicaid Services (CMS).

for many states including New Mexico represents a large percentage of state spending and is increasing in part due to long-term care expenditures. These expenditures are expected to continue increasing in the near-term as the baby-boomer population ages. Thus if this proposed credit can incentivize middle-income individuals to purchase insurance who might otherwise exhaust assets to eventually qualify for Medicaid, the state may incur savings in the long run.

This new proposed credit does not include a sunset date. TRD supports sunset dates for policymakers to review the impact of a credit before extending them, if a sufficient timeframe is allotted for tax incentives to be measured. Given the estimated cost and potential for large increases over time, a sunset date would force an examination of the benefit of this credit versus the cost.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met with the bill's requirement to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose.

ADMINISTRATIVE IMPLICATIONS

This bill is estimated to involve as many as 27.5 thousand claims for credit each year. Each claim must be certified by the Human Services Department each year and then processed and credited by TRD.

TRD notes that the certification may be assigned to the wrong agency.

HSD administers the Medicaid program but beyond that has no administration of private long-term care insurance. The certification of a policy would appear to be more appropriately handled by the Office of the Superintendent of Insurance (OSI.)

TRD's ability to increase efficiency and accuracy of credit claims would be greatly enhanced by a requirement for the Human Service Department (HSD) or as TRD suggests OSI, to upload certified taxpayer applications to TRD and include the full taxpayer social security number for taxpayer identification.

TRD notes the following specific area of administrative impact:

TRD will need to make information system changes and update forms and publications. Audit procedures will need to be updated in order to verify the eligibility of the credit. These changes will be incorporated into annual tax year implementation and cost $10,270 in workload costs for the Information Technology Division (ITD).

TRD assumes that electronic transfer of credit information will not occur before the effective date of the bill and thus an additional FTE will be required. The Revenue Processing Division (RPD) will require a Tax Examiner-A as without automation certifications must be entered manually. In addition, as returns with the credit are submitted, they will need to be manually reviewed.

TRD expects to be able to absorb the impact of these changes as outlined in this standalone bill with one additional FTE. However, if several bills with similar effective dates become law there will be a greater impact to TRD and additional FTE or contract resources may be needed in order to complete the changes specified by the effective date(s) of each bill.

TECHNICAL ISSUES

This bill does not contain a delayed repeal date. LFC recommends adding a delayed repeal date.

TRD notes, "… this credit would be available to non-residents who file a New Mexico return and purchase long-term care insurance outside of the state.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

Does the bill meet the Legislative Finance Committee tax expenditure policy principles?

1. **Vetted**: The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee, to review fiscal, legal, and general policy parameters.
2. **Targeted**: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.
3. **Transparent**: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies.
4. **Accountable**: The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date.
5. **Effective**: The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions "but for" the existence of the tax expenditure.
6. **Efficient:** The tax expenditure is the most cost-effective way to achieve the desired results.

LFC Tax Expenditure Policy Principle	Met?	Comments
Vetted	✗	
Targeted		
Clearly stated purpose	✗	None stated. Assume purpose is to provide substantial
Long-term goals	✗	None stated.
Measurable targets	✗	None stated.
Transparent	✓	Report required.
Accountable		
Public analysis	✓	Report required, but individual recipients will not be named.
Expiration date	✗	
Effective		
Fulfills stated purpose	✗	None stated.
Passes "but for" test	✗	Buys the base
Efficient	✗	See discussion
Key: ✓ Met ✗ Not Met ? Unclear		

LG/al/rl/sb/al