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CORRESPONDENCE MEMORANDUM

DATE: February 17, 2004

TO: Group Insurance Board

FROM: Marcia Blumer, Program Manager
Group Life Insurance Program

SUBJECT: Amendments to Wisconsin Public Employers Group Life Insurance policy and Administrative Agreement

Staff recommends that the Wisconsin Public Employers (WPE) Group Life Insurance policy and Administrative Agreement be amended as written in the attached proposed amendments. The following is a summary of the proposed changes.

<u>Determining Beneficiaries for WPE Group Life Insurance claims</u>

The proposed changes affirm that the Department of Employee Trust Funds (DETF) is responsible for maintaining beneficiary information and determining the eligible beneficiary(ies) for life insurance claims. This is not a change in responsibility or procedures. The proposed language change simply clarifies DETF's role in determining beneficiaries.

<u>Living Benefits</u>

The proposed changes to Living Benefits are recommended by Minnesota Life Insurance Company (MLIC) to assure that the provision complies with the Health Insurance Portability and Accountability Act of 1996 (HIPAA).

According to Tom Solyntjes, MLIC Manager of Group Contracts, a new IRC section 101(g) included in HIPAA excludes from gross income amounts received from a life insurance contract, provided the insured is either terminally ill or chronically ill. In essence, this confirmed what the insurance industry had assumed for accelerated benefits for the terminally ill, i.e., that they are treated like payment from a life insurance contract and are considered income-tax free.

The provision of benefits to the terminally ill under the WPE group life insurance policy currently meets the HIPAA requirements. However, the benefits that pay for those confined on a skilled, intermediate or custodial care basis do not meet the HIPAA requirements for payments to chronically ill.

The rules pertaining to payment to the chronically ill are quite complex. HIPAA has a very specific definition of a "chronically ill" person, generally relying on the inability to perform at least two activities of daily living. Benefits paid to a chronically ill insured must be limited to amounts

Reviewed and approved by Tom Korpady, Division of Insurance Services.

Signature ______________________ Date __________

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paid for costs incurred for qualified long-term care services and the terms of the contract must satisfy other requirements for long-term care contracts in IRC 7702B. Per diem or other periodic payments, without regard to expenses incurred for qualified long-term care services, are also excludable from taxation, subject to a dollar cap of $175 per day (indexed), reduced by the amount of reimbursements and payments received by anyone for the cost of qualified long-term care services for the chronically ill individual. Amounts in excess of the dollar cap, with respect to which no actual costs were incurred for long-term care services, are fully includable in income without regard to rules relating to return to basis under IRC section 72. MLIC is not prepared to administer such complex rules to provide tax-free benefits to the chronically ill.

By having the non-compliant custodial/intermediate/skilled care provisions included in the policy with the terminally ill benefit, the entire provision may be denied the exclusions from income tax provided by HIPAA. To avoid the risk of non-compliance, we recommend removing the confinement option from the Living Benefits provisions. Although this change will remove the possibility of using Living Benefits for custodial care, a review of past claims shows that most, if not all, claims paid have been to terminally ill employees.