

EFFECTIVE DATE

Pub. L. 98-369, div. A, title II, §221(d), July 18, 1984, 98 Stat. 772, as amended by Pub. L. 99-514, §2, title XVIII, §§1825(e), 1899A(69), Oct. 22, 1986, 100 Stat. 2095, 2848, 2962, provided that:

“(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section [enacting this section and amending section 101 of this title and provisions set out as a note under section 101 of this title] shall apply to contracts issued after December 31, 1984, in taxable years ending after such date.

“(2) SPECIAL RULE FOR CERTAIN CONTRACTS ISSUED AFTER JUNE 30, 1984.—

“(A) GENERAL RULE.—Except as otherwise provided in this paragraph, the amendments made by this section shall apply also to any contract issued after June 30, 1984, which provides an increasing death benefit and has premium funding more rapid than 10-year level premium payments.

“(B) EXCEPTION FOR CERTAIN CONTRACTS.—Subparagraph (A) shall not apply to any contract if—

“(i) such contract (whether or not a flexible premium contract) would meet the requirements of section 101(f) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954],

“(ii) such contract is not a flexible premium life insurance contract (within the meaning of section 101(f) of such Code) and would meet the requirements of section 7702 of such Code determined by—

“(I) substituting ‘3 percent’ for ‘4 percent’ in section 7702(b)(2) of such Code, and

“(II) treating subparagraph (B) of section 7702(e)(1) of such Code as if it read as follows: ‘the maturity date shall be the latest maturity date permitted under the contract, but not less than 20 years after the date of issue or (if earlier) age 95’, or

“(iii) under such contract—

“(I) the premiums (including any policy fees) will be adjusted from time-to-time to reflect the level amount necessary (but not less than zero) at the time of such adjustment to provide a level death benefit assuming interest crediting and an annual effective interest rate of not less than 3 percent, or

“(II) at the option of the insured, in lieu of an adjustment under subclause (I) there will be a comparable adjustment in the amount of the death benefit.

“(C) CERTAIN CONTRACTS ISSUED BEFORE OCTOBER 1, 1984.—

“(i) IN GENERAL.—Subparagraph (A) shall be applied by substituting ‘September 30, 1984’ for ‘June 30, 1984’ in the case of a contract—

“(I) which would meet the requirements of section 7702 of such Code if ‘3 percent’ were substituted for ‘4 percent’ in section 7702(b)(2) of such Code, and the rate or rates guaranteed on issuance of the contract were determined without regard to any mortality charges and any initial excess interest guarantees, and

“(II) the cash surrender value of which does not at any time exceed the net single premium which would have to be paid at such time to fund future benefits under the contract.

“(ii) DEFINITIONS.—For purposes of clause (i)—

“(I) IN GENERAL.—Except as provided in subclause (II), terms used in clause (i) shall have the same meanings as when used in section 7702 of such Code.

“(II) NET SINGLE PREMIUM.—The term ‘net single premium’ shall be determined by substituting ‘3 percent’ for ‘4 percent’ in section 7702(b)(2) of such Code, by using the 1958 standard ordinary mortality and morbidity tables of the National Association of Insurance Commissioners, and by assuming a level death benefit.

“(3) TRANSITIONAL RULE FOR CERTAIN EXISTING PLANS OF INSURANCE.—A plan of insurance on file in 1 or more

States before September 28, 1983, shall be treated for purposes of section 7702(i)(3) of such Code as a plan of insurance on file in 1 or more States before September 28, 1983, without regard to whether such plan of insurance is modified after September 28, 1983, to permit the crediting of excess interest or similar amounts annually and not monthly under contracts issued pursuant to such plan of insurance.

“(4) EXTENSION OF FLEXIBLE PREMIUM CONTRACT PROVISIONS.—The amendments made by subsection (b) [amending section 101 of this title and provisions set out as a note under section 101 of this title] shall take effect on January 1, 1984.

“(5) SPECIAL RULE FOR MASTER CONTRACT.—For purposes of this subsection, in the case of a master contract, the date taken into account with respect to any insured shall be the first date on which such insured is covered under such contract.”

INTERIM RULES; REGULATIONS; STANDARDS BEFORE REGULATIONS TAKE EFFECT

Pub. L. 100-647, title V, §5011(c), Nov. 10, 1988, 102 Stat. 3661, provided that the Secretary of the Treasury would issue regulations under subsec. (c)(3)(B)(i) of this section and provided for a standard for contracts issues before the effective date of those regulations.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§1101-1147 and 1171-1177] or title XVIII [§§1800-1899A] of Pub. L. 99-514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99-514, as amended, set out as a note under section 401 of this title.

TREATMENT OF FLEXIBLE PREMIUM CONTRACTS ISSUED DURING 1984 WHICH MEET NEW REQUIREMENTS

Pub. L. 98-369, div. A, title II, §221(b)(3), as added by Pub. L. 99-514, title XVIII, §1825(d), Oct. 22, 1986, 100 Stat. 2848, provided that: “Any flexible premium contract issued during 1984 which meets the requirements of section 7702 of the Internal Revenue Code of 1954 [now 1986] (as added by this section) shall be treated as meeting the requirements of section 101(f) of such Code.”

§ 7702A. Modified endowment contract defined

(a) General rule

For purposes of section 72, the term “modified endowment contract” means any contract meeting the requirements of section 7702—

(1) which—

(A) is entered into on or after June 21, 1988, and

(B) fails to meet the 7-pay test of subsection (b), or

(2) which is received in exchange for a contract described in paragraph (1) or this paragraph.

(b) 7-pay test

For purposes of subsection (a), a contract fails to meet the 7-pay test of this subsection if the accumulated amount paid under the contract at any time during the 1st 7 contract years exceeds the sum of the net level premiums which would have been paid on or before such time if the contract provided for paid-up future benefits after the payment of 7 level annual premiums.

(c) Computational rules

(1) In general

Except as provided in this subsection, the determination under subsection (b) of the 7 level annual premiums shall be made—

(A) as of the time the contract is issued, and

(B) by applying the rules of section 7702(b)(2) and of section 7702(e) (other than paragraph (2)(C) thereof), except that the death benefit provided for the 1st contract year shall be deemed to be provided until the maturity date without regard to any scheduled reduction after the 1st 7 contract years.

(2) Reduction in benefits during 1st 7 years

(A) In general

If there is a reduction in benefits under the contract within the 1st 7 contract years, this section shall be applied as if the contract had originally been issued at the reduced benefit level.

(B) Reductions attributable to nonpayment of premiums

Any reduction in benefits attributable to the nonpayment of premiums due under the contract shall not be taken into account under subparagraph (A) if the benefits are reinstated within 90 days after the reduction in such benefits.

(3) Treatment of material changes

(A) In general

If there is a material change in the benefits under (or in other terms of) the contract which was not reflected in any previous determination under this section, for purposes of this section—

(i) such contract shall be treated as a new contract entered into on the day on which such material change takes effect, and

(ii) appropriate adjustments shall be made in determining whether such contract meets the 7-pay test of subsection (b) to take into account the cash surrender value under the contract.

(B) Treatment of certain benefit increases

For purposes of subparagraph (A), the term “material change” includes any increase in the death benefit under the contract or any increase in, or addition of, a qualified additional benefit under the contract. Such term shall not include—

(i) any increase which is attributable to the payment of premiums necessary to fund the lowest level of the death benefit and qualified additional benefits payable in the 1st 7 contract years (determined after taking into account death benefit increases described in subparagraph (A) or (B) of section 7702(e)(2)) or to crediting of interest or other earnings (including policyholder dividends) in respect of such premiums, and

(ii) to the extent provided in regulations, any cost-of-living increase based on an established broad-based index if such increase is funded ratably over the remaining period during which premiums are required to be paid under the contract.

(4) Special rule for contracts with death benefits of \$10,000 or less

In the case of a contract—

(A) which provides an initial death benefit of \$10,000 or less, and

(B) which requires at least 7 nondecreasing annual premium payments,

each of the 7 level annual premiums determined under subsection (b) (without regard to this paragraph) shall be increased by \$75. For purposes of this paragraph, the contract involved and all contracts previously issued to the same policyholder by the same company shall be treated as one contract.

(5) Regulatory authority for certain collection expenses

The Secretary may by regulations prescribe rules for taking into account expenses solely attributable to the collection of premiums paid more frequently than annually.

(6) Treatment of certain contracts with more than one insured

If—

(A) a contract provides a death benefit which is payable only upon the death of 1 insured following (or occurring simultaneously with) the death of another insured, and

(B) there is a reduction in such death benefit below the lowest level of such death benefit provided under the contract during the 1st 7 contract years,

this section shall be applied as if the contract had originally been issued at the reduced benefit level.

(d) Distributions affected

If a contract fails to meet the 7-pay test of subsection (b), such contract shall be treated as failing to meet such requirements only in the case of—

(1) distributions during the contract year in which the failure takes effect and during any subsequent contract year, and

(2) under regulations prescribed by the Secretary, distributions (not described in paragraph (1)) in anticipation of such failure.

For purposes of the preceding sentence, any distribution which is made within 2 years before the failure to meet the 7-pay test shall be treated as made in anticipation of such failure.

(e) Definitions

For purposes of this section—

(1) Amount paid

(A) In general

The term “amount paid” means—

(i) the premiums paid under the contract, reduced by

(ii) amounts to which section 72(e) applies (determined without regard to paragraph (4)(A) thereof) but not including amounts includible in gross income.

(B) Treatment of certain premiums returned

If, in order to comply with the requirements of subsection (b), any portion of any premium paid during any contract year is returned by the insurance company (with interest) within 60 days after the end of such contract year, the amount so returned (excluding interest) shall be deemed to reduce

the sum of the premiums paid under the contract during such contract year.

(C) Interest returned includible in gross income

Notwithstanding the provisions of section 72(e), the amount of any interest returned as provided in subparagraph (B) shall be includible in the gross income of the recipient.

(2) Contract year

The term “contract year” means the 12-month period beginning with the 1st month for which the contract is in effect, and each 12-month period beginning with the corresponding month in subsequent calendar years.

(3) Other terms

Except as otherwise provided in this section, terms used in this section shall have the same meaning as when used in section 7702.

(Added Pub. L. 100-647, title V, § 5012(c)(1), Nov. 10, 1988, 102 Stat. 3662; amended Pub. L. 101-239, title VII, §§ 7647(a), 7815(a)(1), (4), Dec. 19, 1989, 103 Stat. 2382, 2414; Pub. L. 106-554, § 1(a)(7) [title III, § 318(a)(1), (2)], Dec. 21, 2000, 114 Stat. 2763, 2763A-645; Pub. L. 107-147, title IV, § 416(f), Mar. 9, 2002, 116 Stat. 55.)

Editorial Notes

AMENDMENTS

2002—Subsec. (c)(3)(A)(ii). Pub. L. 107-147 repealed Pub. L. 106-554, § 1(a)(7) [title III, § 318(a)(2)]. See 2000 Amendment note below.

2000—Subsec. (a)(2). Pub. L. 106-554, § 1(a)(7) [title III, § 318(a)(1)], inserted “or this paragraph” before period at end.

Subsec. (c)(3)(A)(ii). Pub. L. 106-554, § 1(a)(7) [title III, § 318(a)(2)], which substituted “under the old contract” for “under the contract”, was repealed by Pub. L. 107-147. See Construction of 2002 Amendment note below.

1989—Subsec. (c)(3)(B). Pub. L. 101-239, § 7815(a)(1), substituted “benefit increases” for “increases in future benefits” in heading and amended text generally. Prior to amendment, text read as follows: “For purposes of subparagraph (A), the term ‘material change’ includes any increase in future benefits under the contract. Such term shall not include—

“(i) any increase which is attributable to the payment of premiums necessary to fund the lowest level of future benefits payable in the 1st 7 contract years (determined after taking into account death benefit increases described in subparagraph (A) or (B) of section 7702(e)(2)) or to crediting of interest or other earnings (including policyholder dividends) in respect of such premiums, and

“(ii) to the extent provided in regulations, any cost-of-living increase based on an established broad-based index if such increase is funded ratably over the remaining life of the the contract.”

Subsec. (c)(4). Pub. L. 101-239, § 7815(a)(4), substituted “of \$10,000 or less” for “under \$10,000” in heading and “the same policyholder” for “the same insurer” in concluding provisions.

Subsec. (c)(6). Pub. L. 101-239, § 7647(a), added par. (6).

Statutory Notes and Related Subsidiaries

EFFECTIVE DATE OF 2000 AMENDMENT

Pub. L. 106-554, § 1(a)(7) [title III, § 318(a)(3)], Dec. 21, 2000, 114 Stat. 2763, 2763A-645, provided that: “The amendments made by this subsection [amending this section] shall take effect as if included in the amend-

ments made by section 5012 of the Technical and Miscellaneous Revenue Act of 1988 [Pub. L. 100-647].”

EFFECTIVE DATE OF 1989 AMENDMENT

Pub. L. 101-239, title VII, § 7647(b), Dec. 19, 1989, 103 Stat. 2383, provided that: “The amendment made by subsection (a) [amending this section] shall apply to contracts entered into on or after September 14, 1989.”

Amendment by section 7815(a)(1), (4) of Pub. L. 101-239 effective, except as otherwise provided, as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100-647, to which such amendment relates, see section 7817 of Pub. L. 101-239, set out as a note under section 1 of this title.

EFFECTIVE DATE

Pub. L. 100-647, title V, § 5012(e), Nov. 10, 1988, 102 Stat. 3665, as amended by Pub. L. 101-239, title VII, § 7815(a)(2), Dec. 19, 1989, 103 Stat. 2414, provided that:

“(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section [enacting this section and amending sections 26 and 72 of this title] shall apply to contracts entered into on or after June 21, 1988.

“(2) SPECIAL RULE WHERE DEATH BENEFIT INCREASES BY MORE THAN \$150,000.—If the death benefit under the contract increases by more than \$150,000 over the death benefit under the contract in effect on October 20, 1988, the rules of section 7702A(c)(3) of the 1986 Code (as added by this section) shall apply in determining whether such contract is issued on or after June 21, 1988. The preceding sentence shall not apply in the case of a contract which, as of June 21, 1988, required at least 7 level annual premium payments and under which the policyholder makes at least 7 level annual premium payments.

“(3) CERTAIN OTHER MATERIAL CHANGES TAKEN INTO ACCOUNT.—A contract entered into before June 21, 1988, shall be treated as entered into after such date if—

“(A) on or after June 21, 1988, the death benefit under the contract is increased (or a qualified additional benefit is increased or added) and before June 21, 1988, the owner of the contract did not have a unilateral right under the contract to obtain such increase or addition without providing additional evidence of insurability, or

“(B) the contract is converted after June 20, 1988, from a term life insurance contract to a life insurance contract providing coverage other than term life insurance coverage without regard to any right of the owner of the contract to such conversion.

“(4) CERTAIN EXCHANGES PERMITTED.—In the case of a modified endowment contract which—

“(A) required at least 7 annual level premium payments,

“(B) is entered into after June 20, 1988, and before the date of the enactment of this Act [Nov. 10, 1988], and

“(C) is exchanged within 3 months after such date of enactment for a life insurance contract which meets the requirements of section 7702A(b), the contract which is received in exchange for such contract shall not be treated as a modified endowment contract if the taxpayer elects, notwithstanding section 1035 of the 1986 Code, to recognize gain on such exchange.

“(5) SPECIAL RULE FOR ANNUITY CONTRACTS.—In the case of annuity contracts, the amendments made by subsection (d) [amending section 72 of this title] shall apply to contracts entered into after October 21, 1988.”

CONSTRUCTION OF 2002 AMENDMENT

Pub. L. 107-147, title IV, § 416(f), Mar. 9, 2002, 116 Stat. 55, provided that: “Paragraph (2) of section 318(a) of the Community Renewal Tax Relief Act of 2000 [H.R. 5662, as enacted by section 1(a)(7) of Pub. L. 106-554] (114 Stat. 2763A-645) [amending this section] is repealed, and clause (ii) of section 7702A(c)(3)(A) shall read and be applied as if the amendment made by such paragraph had not been enacted.”

§ 7702B. Treatment of qualified long-term care insurance**(a) In general**

For purposes of this title—

(1) a qualified long-term care insurance contract shall be treated as an accident and health insurance contract,

(2) amounts (other than policyholder dividends, as defined in section 808, or premium refunds) received under a qualified long-term care insurance contract shall be treated as amounts received for personal injuries and sickness and shall be treated as reimbursement for expenses actually incurred for medical care (as defined in section 213(d)),

(3) any plan of an employer providing coverage under a qualified long-term care insurance contract shall be treated as an accident and health plan with respect to such coverage,

(4) except as provided in subsection (e)(3), amounts paid for a qualified long-term care insurance contract providing the benefits described in subsection (b)(2)(A) shall be treated as payments made for insurance for purposes of section 213(d)(1)(D), and

(5) a qualified long-term care insurance contract shall be treated as a guaranteed renewable contract subject to the rules of section 816(e).

(b) Qualified long-term care insurance contract

For purposes of this title—

(1) In general

The term “qualified long-term care insurance contract” means any insurance contract if—

(A) the only insurance protection provided under such contract is coverage of qualified long-term care services,

(B) such contract does not pay or reimburse expenses incurred for services or items to the extent that such expenses are reimbursable under title XVIII of the Social Security Act or would be so reimbursable but for the application of a deductible or coinsurance amount,

(C) such contract is guaranteed renewable,

(D) such contract does not provide for a cash surrender value or other money that can be—

(i) paid, assigned, or pledged as collateral for a loan, or

(ii) borrowed,

other than as provided in subparagraph (E) or paragraph (2)(C),

(E) all refunds of premiums, and all policyholder dividends or similar amounts, under such contract are to be applied as a reduction in future premiums or to increase future benefits, and

(F) such contract meets the requirements of subsection (g).

(2) Special rules**(A) Per diem, etc. payments permitted**

A contract shall not fail to be described in subparagraph (A) or (B) of paragraph (1) by reason of payments being made on a per diem or other periodic basis without regard

to the expenses incurred during the period to which the payments relate.

(B) Special rules relating to medicare

(i) Paragraph (1)(B) shall not apply to expenses which are reimbursable under title XVIII of the Social Security Act only as a secondary payor.

(ii) No provision of law shall be construed or applied so as to prohibit the offering of a qualified long-term care insurance contract on the basis that the contract coordinates its benefits with those provided under such title.

(C) Refunds of premiums

Paragraph (1)(E) shall not apply to any refund on the death of the insured, or on a complete surrender or cancellation of the contract, which cannot exceed the aggregate premiums paid under the contract. Any refund on a complete surrender or cancellation of the contract shall be includible in gross income to the extent that any deduction or exclusion was allowable with respect to the premiums.

(c) Qualified long-term care services

For purposes of this section—

(1) In general

The term “qualified long-term care services” means necessary diagnostic, preventive, therapeutic, curing, treating, mitigating, and rehabilitative services, and maintenance or personal care services, which—

(A) are required by a chronically ill individual, and

(B) are provided pursuant to a plan of care prescribed by a licensed health care practitioner.

(2) Chronically ill individual**(A) In general**

The term “chronically ill individual” means any individual who has been certified by a licensed health care practitioner as—

(i) being unable to perform (without substantial assistance from another individual) at least 2 activities of daily living for a period of at least 90 days due to a loss of functional capacity,

(ii) having a level of disability similar (as determined under regulations prescribed by the Secretary in consultation with the Secretary of Health and Human Services) to the level of disability described in clause (i), or

(iii) requiring substantial supervision to protect such individual from threats to health and safety due to severe cognitive impairment.

Such term shall not include any individual otherwise meeting the requirements of the preceding sentence unless within the preceding 12-month period a licensed health care practitioner has certified that such individual meets such requirements.

(B) Activities of daily living

For purposes of subparagraph (A), each of the following is an activity of daily living: