



EQUITABLE

# Covering the costs of long-term care

White Paper

## **7702B vs. 101(g)**

A discussion of riders on  
a life insurance policy

# A long life is a gift when you have the proper advice, planning and sound financial strategies to enjoy it.

We're living longer. Retirement can last quite a long time — upwards of 30 years. And nearly half of all Americans will need some type of long-term care in their lives.<sup>1</sup> As America's population ages, we can help them focus on what they might need later — sustainable income and protection for their assets as they age. The older people get, the more likely they are to develop health conditions that require ongoing care or support. That support can be expensive, whether it is provided by loved ones who give up their jobs to care for aging parents or by outside sources. With long-term care costs reaching ever-higher levels, long-term care insurance policies or riders can help make sure clients have the means to pay for care, protect their assets and provide a legacy for their children or community.

## With long-term care costs reaching ever-higher levels, what are clients to do?

An informative and insightful brochure by Dr. Sandra Timmermann, Ed.D, titled *Connecting the Dots Between Aging at Home and Long-Term Care Protection*, provides relevant and practical information that can help you start a conversation with your clients about the importance of planning for these issues.

This paper adds to our support by helping you understand the details of two different types of life insurance riders that are available to you: 7702B and 101(g) riders.

## The median annual costs in 2023<sup>1</sup>



<sup>1</sup> Source: Genworth 2023 Cost of Care Survey.

## Paying for long-term care

How clients plan for potential long-term care costs will often depend on their current standard of living and the guidance they receive from their advisors. Their options include:

- **Self-insurance.** If they have sufficient assets, or simply hope they won't need long-term care, clients may choose to pay for long-term care expenses out of pocket. However, for most, self-insurance is not an attractive option. After all, a lengthy stay in a nursing home can quickly drain even substantial assets, jeopardizing the family's financial security and depleting any legacy they might want to leave loved ones.
- **Government programs (Medicare or Medicaid).** Government programs are of little help to many. Medicare covers few of the expenses we associate with long-term care and Medicaid is only available to those who have few, if any, assets.
- **Some form of long-term care insurance.** To make sure clients have the means to pay for long-term care, protect their assets and provide a legacy for their children or community, many turn to long-term care insurance policies or life insurance with a rider that will help pay for long-term care costs.



### Two insurance options available today

Which type of insurance is best for your clients? The answer will vary, so it is important to understand all the choices. No one type of insurance is better than the other; each has its pros and cons.

#### Stand-alone LTC insurance policies

Stand-alone long-term care insurance policies that insure against potential long-term care expenses.

#### Life insurance with a rider to help cover long-term care expenses

Life insurance-based products that include long-term care benefits.

## 1 Stand-alone LTC insurance policies

At one time, stand-alone long-term care insurance policies were the primary solution for insuring against potential long-term care expenses. Early generations of these products often provided rich benefits and were popular for a number of reasons, among them:

- Lifetime cost of living adjustments to protect against inflation.
- Policies may qualify for state Long-Term Care Partnership programs, a joint federal-state program where applicants for Medicaid are permitted to keep one dollar of assets for every dollar of long-term care insurance coverage paid on their behalf.
- Premiums may be deductible for income tax purposes.
- Premiums pay only for long-term care coverage — no additional costs for other insurance benefits that may not be wanted.

Stand-alone long-term care insurance remains an important option for clients. The marketplace has changed, however. Clients may find that fewer insurance companies offer these products and some of the popular features found in earlier-generation products have been limited or are no longer available.

## 2 Life insurance with a rider to help cover long-term care expenses

Life insurance-based products that included long-term care benefits may be an attractive alternative. Broadly speaking, there are several types of life insurance-based products. So-called “linked benefit” or “hybrid” products are typically funded with a single premium. Alternatively, traditional permanent life insurance policies may include a rider designed to pay for long-term care expenses. Using permanent policies with a rider is the focus of this article. Of course, offer this as a potential solution only when the client has a need for life insurance coverage.

### These riders can help clients pay for long-term care expenses by:

- “Accelerating” payments of the life insurance policy death benefit in the event the insured becomes chronically ill and satisfies certain conditions. In other words, it pays some portion of the policy’s death benefit before death occurs, so there is only one pool of money available for the client.
- Allowing those accelerated payments to be used for long-term care costs.
- Clients must qualify medically separately for both the life insurance coverage and a long-term care rider.

### Any remaining death benefit that is not accelerated can then be paid out to beneficiaries upon the insured’s death

Since many people need life insurance to provide for family members, replace lost income or pay debts and taxes anyway, the ability to use life insurance for another purpose is often very appealing. It’s a simple, flexible and often a lower-cost strategy. If it turns out that long-term care services are not needed, the life insurance policy cash values can be used to help supplement income, or the unaccelerated policy death benefit can be paid out to designated beneficiaries upon the insured’s death, as income tax-free life insurance proceeds.



### Two main categories of riders

There are generally two main categories of riders, depending on how the benefit is being paid.

#### 7702B long-term care riders

Qualified long-term care insurance benefits under Internal Revenue Code section 7702B.

#### 101(g) chronic illness riders

Accelerated death benefit for chronic illness under Internal Revenue Code section 101(g).

## 1 7702B long-term care riders

**Section 7702B** is the primary tax code authority when it comes to long-term care insurance — whether it’s a stand-alone policy or a long-term care rider on a permanent life insurance policy. Section 7702B defines a qualified long-term care contract and treats it as an accident and health insurance contract.

## 2 101(g) chronic illness riders

Section 101 of the tax code outlines the tax treatment of life insurance death benefits. Section 101(a) provides that, with certain exceptions, life insurance death benefits are excluded from income. Under section 101(g) of the code, payments from a life insurance contract insuring a chronically ill person that are received prior to the insured's death are treated as if they were paid as a death benefit – tax-free. However, benefits paid in excess of the per diem limit will generally be included in income. There is an important exception to this tax-free treatment for business-related policies. Section 101(g)(5) of the code states that if the insured is a director, officer or employee of the policyowner, or is financially interested in any trade or business of the policyowner, accelerated benefits would not be excluded from income.

**First, let's look at how these riders are similar or different from each other.**

## What do these riders have in common?

For both long-term care riders and chronic illness riders:

### **Benefits are received by the clients, income tax-free, up to IRS limits.**

Because benefits are considered an acceleration of a life insurance policy's death benefit, which is tax-free to the recipient, benefits for long-term care are treated similarly.

### **Clients must qualify for benefits.**

That means, to receive benefits, the client must be considered chronically ill, as defined by the policy. A chronically ill individual is defined as any individual who has been certified by a licensed healthcare practitioner as:

1. being unable to perform (without substantial assistance from another individual) at least two activities of daily living for a period of at least 90 days due to a loss of functional capacity
2. having a level of disability similar (as determined under regulations prescribed by the Treasury Secretary in consultation with the Secretary of Health and Human Services) to the level of disability described in clause (1), or
3. requiring substantial supervision to protect such individual from threats to health and safety due to severe cognitive impairment.

### **The rider will pay some stated percentage of the death benefit.**

The rider typically pays 1%, 2% or 3% of the policy death benefit each month, once the insured becomes ill and qualifies for benefits and long-term care. If, for example, the insured becomes chronically ill, she may be eligible to receive a monthly benefit of up to 2% of the policy's death benefit, after a waiting period of 90 days. If her death benefit is \$1,000,000, she would be able to receive up to \$20,000 per month in benefits to help pay for long-term care costs.

#### **Taxation of these riders**

To understand the tax issues associated with 7702B and 101(g) riders, read our LTCSR Tax Planning Perspective.

## How are the riders different from each other?

There can be significant differences in how benefits are paid when an insured is eligible for benefits, and the level of consumer protection provided to the buyer.

### Long-term care riders

#### Will pay if conditions are temporary.

It may sound counterintuitive, but a chronic illness doesn't have to be permanent for benefits to be paid out under a long-term care rider.

#### Are treated as a separate long-term care accident and health insurance contract.

Because it's treated like an accident and health insurance contract, 7702B rider benefit payments are generally income tax-free. However, if the taxpayer receives benefits in excess of the per diem limit, those "excess benefits" will be considered income for tax purposes, but only to the extent they exceed actual unreimbursed qualified long-term care expenses. Those per diem limits are indexed for inflation and are \$420/day in 2025.

Unlike a stand-alone LTC insurance policy, LTC riders are not generally eligible for state LTC partnership programs or for HSAs, and are not a permissible deductions for income taxes.

#### Must include consumer protections.

The National Association of Insurance Commissioners (NAIC) Long-Term Care Insurance Model Act and Long-Term Care Insurance Model Regulation, as enacted by the states, establish requirements for certain consumer protection provisions that must be provided under these riders. These provisions include consumer protections relating to non-cancellability, unintentional lapse, minimum standards, disclosure, reinstatement and nonforfeiture, among other things – and provide considerable peace of mind for clients and financial professionals alike.

They also establish rules for marketing these products, as well as training and licensing requirements for those who sell them.

#### Can be referred to as "long-term care" insurance.

Riders designed to comply with all these various requirements of IRS Section 7702B are sometimes simply referred to as qualified riders. Agents and other financial professionals can refer to them as "long-term care insurance" when communicating with clients and prospects. Because long-term care insurance is considered a form of accident and health insurance, selling agents and financial professionals must be accident- and health-licensed.

#### May be either indemnity or reimbursement models.

Long-term care riders can use:

- An indemnity payment model, which pays up to the maximum benefit amount specified in the contract regardless of expenses incurred.

**For example**, a \$500,000 policy with a maximum monthly rider benefit of 2% of the policy's death benefit would pay up to \$10,000 per month to the policyowner regardless of expenses incurred. If actual expenses in the first month were \$15,000, the rider would pay \$10,000. If, in month 2, expenses dropped to \$4,000, the rider could still pay up to \$10,000. As a result, an indemnity rider enables an individual to pay for expenses that are associated with long-term care, but are not considered qualified expenses and not reimbursable under a reimbursement-type rider, including costs of home modification and medical equipment, such as walkers. For most indemnity riders, individuals simply need to qualify and demonstrate there's a plan of care and periodically be recertified. There may be no additional paperwork, though individuals should consult with their carrier for particular claims requirements.

## Long-term care riders (cont.)

**May be either indemnity or reimbursement models.**

- A reimbursement payment model, which reimburses the policyowner for expenses incurred by the insured. After the insured qualifies for benefits, the policyowner must submit receipts for qualifying expenses to receive benefit payments. A reimbursement rider will never pay more than the qualified long-term care expenses that were incurred.

**For example**, a \$500,000 policy with a maximum monthly rider benefit of 2% of the policy's death benefit could pay up to \$10,000 per month to the policyowner, but no more than expenses incurred. If actual expenses in the first month were \$15,000, the rider would pay \$10,000. If in month 2, expenses dropped to \$4,000, the rider would pay no more than \$4,000. A reimbursement contract also requires periodic paperwork to document the actual expenses included, which can take time on the part of an ill individual or a family member.

**Charge an additional current fee.**

Therefore, when benefits are paid from the rider, there is then a dollar-for-dollar reduction in the death benefit.

### Choose your benefit amount

Some indemnity-style riders allow the policyholder to select the monthly benefit amount, up to the maximum allowable. That gives them the flexibility to use more of the death benefit for lifestyle enhancements, travel before the condition worsens, or leave more of the death benefit for loved ones later.

## Chronic Illness riders

**May or may not pay if conditions are temporary.**

The definition of a chronic illness is the same for a chronic illness rider as it is for a long-term care rider. However, while all long-term care riders allow for conditions to be either permanent or temporary, some chronic illness riders will only pay if the condition is permanent. Here's why:

- In about 45 states, insurance companies are members of the Interstate Insurance Product Regulation Commission (IIPRC), which allows them to get faster approval on products if they file a product that complies with the adopted standards.
- In 2007, the IIPRC defined a "qualifying event" (when benefits would be paid) as a terminal or permanent condition. Therefore, most chronic illness riders paid only if the condition was permanent.
- In 2015, the IIPRC amended their standards to include temporary conditions as qualifying events on chronic illness riders. So, since then, some insurance companies have introduced chronic illness riders that allow temporary conditions. However, most still have permanent condition stipulations. This may be because accepting only permanent conditions means the insurance company will have fewer claims and can offer the rider at a reduced cost. You should exercise care in selecting a chronic illness rider if you want the ability for temporary claims.

**Are not required to offer consumer protections, like those under long-term care riders.**

Because chronic illness riders are not considered long-term care riders, they don't have to abide by the same rules.

## Chronic Illness riders (cont.)

### Cannot be referred to as “long-term care” insurance.

Because they are not subject to long-term care insurance regulations, they do not qualify as long-term care insurance, therefore, cannot be called “long-term care” in marketing or other material. They may be referred to as accelerated death benefit riders, chronic illness riders or, simply, nonqualified riders. Because these riders are not considered a form of accident and health insurance, selling agents and financial professionals do not need to be accident- and health-licensed to sell them.

### Use an indemnity payment model.

Since these riders simply accelerate the death benefit, it makes sense that they use only indemnity payment models, which provide a certain amount of money to the insured each month, once the need for long-term care has been established.

### Business-related policies do not receive tax-free treatment of benefit payments.

Although benefits are generally tax-free up to the per-diem limits, business-related policies with a chronic illness rider are not eligible. Specifically, tax-free treatment does not apply to benefits paid to a business where the insured is a director, officer or employee, or if the insured is financially interested in any trade or business carried on by the taxpayer. Of course, these are the individuals whom a business would most want to insure for death benefit and long-term impairment purposes. Therefore, the use of a chronic illness rider as part of a key person insurance arrangement or buy-sell agreement can be problematic, because any benefits received under the rider would be included in the business policyowner’s income.

While there is not a specific exclusion for long-term care riders, the tax treatment for business-owned contracts is also not specifically discussed in the tax code. This would be up to the discretion of a business’ tax preparer.

### May not charge a current fee, but may take more when benefits are used.

Chronic illness riders may be structured similarly to long-term care riders, with a current charge. However, some chronic illness riders do not charge for the rider currently, but instead pay for it by discounting the remaining death benefit in the policy at the time there is a claim under the rider. The result is a greater than dollar-for-dollar reduction in the policy death benefit for payments made under the rider. These discounted death benefit riders are sometimes promoted as “free.” If clients don’t use the rider, it doesn’t cost them anything. But, it may cost them more in reduced death benefits if they use it.

## The comparison chart that follows on the next page illustrates the differences between the long-term care rider and the chronic illness rider.

There is an additional current charge for a tax-qualified Section 7702B long-term care insurance. When benefits are then paid from the rider, there is then a dollar-for-dollar reduction in the death benefit.

<sup>2</sup> This may vary depending on the state.

<sup>3</sup> Though treated as a long-term care contract, there remain some important distinctions between a 7702B rider and a stand-alone long-term care insurance contract. For example, 7702B riders are not generally eligible for state LTC partnership programs. Also, rider charges are not eligible for HSAs, nor are they a permissible deduction for income taxes.

## Long-term care rider vs. chronic illness rider

	Long-term care rider	Chronic illness rider
Covers temporary claims	<b>Yes</b>	<b>Maybe</b> New regulations allow chronic illness riders to pay claims if the condition is temporary. However, most chronic illness riders still require the condition to be permanent.
Qualifies as long-term care insurance	<b>Yes<sup>3</sup></b> Clients may be more familiar with the term “long-term care” that can be used in marketing and sales materials.	<b>No</b>
	<b>Includes required consumer protection provisions:</b> The following provisions protect the policy from lapsing unintentionally due to a client’s physical or cognitive impairment. While chronic illness riders may include some of these benefits, they are not required.	
Unintentional lapse protection required	<b>Yes</b> Clients and their families can rest assured that someone close to the client will receive a notice of nonpayment of premiums before the policy lapses. This protects against unintentional policy lapses.	<b>No</b>
Lapse protection while on claim required	<b>Yes</b> Clients don’t have to worry about paying premiums while the policy is on claim.	<b>No</b>
Reinstatement provision required	<b>Yes</b> If clients become cognitively impaired and didn’t realize that premium payments were due, their policy can be reinstated with proof that the insured was cognitively impaired.	<b>No</b>
Nonforfeiture provision required	<b>Yes</b> Clients can receive benefits on a lapsed policy if they would have qualified for benefits before the lapse.	<b>No</b>
Includes a charge only if your client uses the rider	<b>No</b> There is an upfront charge for the rider that guarantees a dollar-for-dollar reduction in death benefit by the amount of LTC benefits paid. The cost of coverage is known at time of policy issue. <sup>2</sup>	<b>Maybe</b> Some of these riders have an upfront charge. Others have no upfront charge, but charge a back-end fee by reducing the death benefit by an amount greater than the amount of chronic illness benefits paid. These fees may vary and are not known at policy issue, making planning more difficult.
Tax-free treatment for business-related policies	<b>Yes</b> Benefit payments can help employers buy out an insured’s share of the business, finance finding a replacement for a key person or offset losses due to a key employee’s incapacity.	<b>No</b>
Requires a health insurance license	<b>Yes, in most states</b> This additional credential lets you build credibility with high-net-worth clients and understand more about how long-term care works (such as how it interacts with Medicare) through continuing education courses.	<b>No</b>
Normal tax treatment for Modified Endowment Contracts (MECs)	<b>Yes</b> Rider charges are not considered distributions, not taxable.	<b>No</b> Rider charges are considered distributions, taxable up to the gain.
Accelerated Death Benefits	<b>Yes</b> Tax-free up to greater of per diem limit or actual eligible long-term care expenses incurred.	<b>Yes</b> Tax-free up to per diem limit only.

# Why the right rider matters



## Planning scenarios

### 1

#### **Scenario 1: Consumer protection for aging clients — meet George and Claire.**

Individuals who need the protection provided by a long-term care rider are inherently more vulnerable. The consumer protection features included in every qualified long-term care insurance rider are especially important and can mean the difference between having care or not. In the scenario below, George and Claire each own a life insurance policy on which they have included a rider that will assist them with expenses in the event they become chronically ill. George's policy includes a Section 7702B long-term care rider, while Claire's policy includes a Section 101(g) chronic illness rider.

#### **George's long-term care rider includes consumer protections he needs as he ages.**

George suffers an accident and becomes cognitively impaired. As a result, he doesn't remember to pay the premium on his policy, and the policy is at risk of lapsing. Fortunately for George, his long-term care rider included unintentional lapse protection provisions. When he applied for coverage, he designated his daughter, Susan, to receive a notice in the event his premiums went unpaid. So, when George didn't pay his premium on time, a notice was sent to Susan, advising her of the nonpayment of premium on her father's policy. Ordinarily, Susan would have intervened and made sure premiums were paid. But Susan had moved several times and the notice was not forwarded to her current mailing address. Therefore, George's policy inadvertently lapsed. However, George's policy also included a mandatory reinstatement provision, which enabled the insurer to reinstate his coverage once they learned from Susan that George was cognitively impaired. George's policy, upon reinstatement, made payments to George to assist with his long-term care expenses.

#### **Claire's chronic illness rider does not include consumer protections.**

Claire had become increasingly forgetful before becoming chronically ill and, as a result, neglected to pay the premiums on her policy. A nonpayment of premium notice was sent to her home, but her policy did not provide her an option to name a third party to receive a nonpayment notice, so no one else was aware of the situation. As a result, her policy lapsed. Unlike George's policy, Claire's policy did not have a reinstatement provision. She was not able to reinstate her policy, even if it could be shown that it was her cognitive impairment that caused her failure to pay premiums on time. Unfortunately, Claire has no benefits to assist her in the payment of long-term care expenses.

## 2

### **Scenario 2: Business-owned policy.**

A business may need to purchase life insurance on the lives of its owners and key employees for reasons such as key person, executive benefits or business succession. What about including a chronic illness or long-term care rider on the policy? As discussed earlier, Section 101(g)(5) of the code specifically denies income tax-free treatment to rider benefits received from a 101(g) rider as part of a business-related policy. In business situations then, where the parties wish to provide both life insurance and long-term care protection, a 7702B policy is the safer bet.

### **MHG Corporation used life insurance and a long-term care rider for protection and executive benefits.**

MHG, a successful high-tech consulting group, was lucky enough to have Tony, their most successful sales vice president, on staff. Tony has been responsible for bringing in as much as 40% of the company's new accounts, and the business had become dependent on Tony's continued success and contributions. MHG recognized the need for life insurance to protect the company in the event of Tony's death, and they were concerned that if Tony needed long-term care due to an unforeseen illness or injury, the company would suffer a loss in revenue and incur considerable expenses in finding a replacement. They decided that a long-term care rider on the policy, while not covering the broad range of conditions that disability insurance would cover, would help them provide some coverage, packaged with life insurance.

Because benefits payable to the company from a chronic illness rider would be taxable, MHG purchased a policy with a long-term care rider. Therefore, if Tony should become chronically ill, MHG could apply for benefits which can be used to offset lost revenue and cover the costs of finding Tony's replacement.

MHG also provided a nonqualified deferred bonus to Tony, payable at his retirement (or death, if that occurs sooner) in a lump sum. They intend to pay at least a part of that bonus with the life insurance policy. By transferring the policy to Tony at his retirement, Tony will acquire valuable life insurance protection, policy cash values that can be used to supplement his retirement income or, if needed, long-term care benefits that can be provided through the rider.

## **Summary**

The growth in life insurance-based solutions to pay for long-term care expenses has provided consumers with many additional options. While there are some similarities between long-term care riders and chronic illness riders, they can vary greatly in how they pay out benefits, what types of conditions are covered and the consumer protections they provide. It is wise for consumers to learn all they can about these options, so that they can understand how they work and decide which will best fit their particular situation.

The Long-Term Care Services<sup>SM</sup> Rider is available with Equitable universal and variable universal life insurance policies. It is designed for clients who need both life insurance protection and a relatively affordable, effective way to pay for potential long-term care costs. The Long-Term Care Services<sup>SM</sup> Rider is available for an additional charge and does have restrictions and limitations. Clients may qualify for the life insurance but not the rider.

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