

Federal Pension Protection Act of 2006:

Q&A on Income Tax Exclusion for Retiree Health Insurance Payments

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The Pension Protection Act of 2006 (PPA) includes a number of provisions applicable to public pension plans. Since then, we have received numerous calls and questions about the PPA, most concerning the federal income tax exclusion for certain retiree health and long-term care insurance premiums. This article addresses the most frequently asked questions regarding this income tax exclusion. It is important to understand, however, that the PPA is a new law and is quite complex. Many of the provisions of the PPA will require additional clarification from the IRS and other government agencies. The information in this article reflects FPPA's understanding of the health care premium tax exclusion based on information available at this time.

Question 1 What is the health care tax benefit under the PPA?

Answer The PPA permits eligible retired public safety officers (PSO) to exclude from federal income tax, amounts paid directly from retirement plan distributions to cover the cost of certain health and long-term care insurance premiums. The maximum amount of the exclusion in any one year is the lesser of actual premiums paid or \$3,000.

Question 2 Who qualifies as a PSO under the PPA?

Answer A PSO is defined as "an individual serving a public agency in an official capacity, with or without compensation, as a law enforcement officer, as a fire-fighter, as a chaplain, or as a member of a rescue squad or ambulance crew."

Question 3 What other eligibility requirements apply?

Answer The PSO must have separated from service as a public safety officer by reason of disability or attainment of normal retirement age. The individual's benefit must be fully or partially taxable. In addition, FPPA requires that the member's monthly benefit be sufficient to cover the full cost of the member's monthly insurance premium.

Normal retirement age is the earliest age at which a plan Member has the right to retire without the consent of the employer and receive retirement benefits based on the amount of the Member's service on the date of retirement at the full rate set forth in the plan (that is, without actuarial or similar reduction because of retirement before some later specified age).

For the Statewide Defined Benefit Plan, the Statewide Hybrid Plan, the Statewide Money Purchase Plan, and the Colorado Springs New Hire Pension Plan – Fire Component, the Normal Retirement Age is defined as age 55.

For the Colorado Springs New Hire Pension Plan – Police Component, the Normal Retirement Age is defined as age 50.

For other plans, including old hire pension plans, the "safe harbor" rule under federal regulations for Normal Retirement Age for public safety officers is generally as early as age 50 if no reduction in pension is made and the pension benefits begin upon separation from service. However, members of old hire plans should consult local plan documents or the local pension board for a final determination in the event of a full pension retirement at a younger age. FPPA does not give advice on local pension matters.

Question 4 Which FPPA members do not qualify for the benefit?

Answer FPPA believes the following members do not qualify: retired administrative support personnel; retirees receiving an early retirement benefit prior to

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reaching the plan's normal retirement age; members taking a vested retirement who, at the time of separation of service, have not reached the plan's normal retirement age; and beneficiaries.

Question 5 Who ultimately determines eligibility for the PPA health care premium tax exclusion?

Answer It is the responsibility of each individual claiming the exclusion to substantiate PSO eligibility. This responsibility also applies in the event of an IRS audit.

Question 6 When does the PPA health care premium tax exclusion become effective?

Answer The exclusion may be claimed for tax years beginning with 2007. It may only be claimed, however, to the extent that your retirement plan administrator has implemented a program for the direct payment of health insurance premiums from your retirement or disability benefit. The PPA does not require that employers or administrators implement such a program. As discussed below, FPPA already has a program in place for a number of different health care plans. In addition, the FPPA Board expanded the program in September 2007 to include third party insurance providers who comply with FPPA requirements for the payment of premiums on a group basis.

Question 7 I am a member of a money purchase plan affiliated with FPPA. May I claim the exclusion?

Answer You may qualify as a PSO, but implementation of a direct payment arrangement for your health insurance premiums is subject to implementation by FPPA's record keeper, Fidelity. At this point it doesn't appear that Fidelity is able to offer a viable option for payment of insurance premiums. FPPA will continue to engage Fidelity on this issue.

Question 8 May I claim the \$3,000 tax exclusion with respect to insurance premiums which I pay directly to the insurance carrier?

Answer No, only premium payments withheld from a member's monthly pension benefit and paid directly to the insurance carrier will qualify under federal law.

Question 9 With which health insurance providers does FPPA currently have an arrangement for the direct payment of retiree health insurance premiums?

Answer

Department	PPA Eligible Insurance available through FPPA's Insurance Premium Deduction Program
Denver Police	<ul style="list-style-type: none"> • United Healthcare HMO & HD HP (Under 65 group plan only) • Kaiser HMO (Medicare Supplement and Under 65 group plans) • PacifiCare Senior Supplement with UnitedHealthcare Rx (Medicare Supplement group plan only) • Secure Horizons HMO by United Healthcare (Medicare Supplement group plan only) • Delta Dental PPO Plan • Colonial Non-Life Insurance • Eyemed Vision

Denver Fire	<ul style="list-style-type: none"> • Kaiser HMO, Triple Opt or Out of Area (Medicare supplement - high & low option and Under 65 group plans) • Humana Comp Benefits Vision Plan • Delta Dental PPO Plan • Colonial Non-Life Insurance
Colorado Springs Police & Fire	<ul style="list-style-type: none"> • Cigna Health Network EPO or Mid Level (Under 65 and Medicare Supplement Group Plans) • Vision Service Plan (Department sponsored) • Delta Dental Plan • Colonial Non-Life Insurance
Aurora Police & Fire	<ul style="list-style-type: none"> • Kaiser HMO, HDHP, Triple Opt or Out of Area (Medicare supplement and Under 65 group plans) • Cigna Health HDHP (Under 65 Group Plan Only Superior Vision Plan) • Assurant Dental (Department Sponsored) • Delta Dental Plan • Colonial Non-Life Insurance
Pueblo Police & Fire	<ul style="list-style-type: none"> • United Healthcare HMO, POS, HDHP (Under 65 group plan only) • Aetna Dental
Greeley Police & Fire	<ul style="list-style-type: none"> • Health Insurance Choice or Standard (Under 65 group plan only) • Dental Insurance
West Metro Fire	<ul style="list-style-type: none"> • Humana Health Insurance (Under 65 and Medicare Supplements)
All Retirees (FPPA Sponsored Programs)	<ul style="list-style-type: none"> • Secure Horizons by UnitedHealthcare (Medicare supplements only) • Vision Service Plan (FPPA Sponsored Plan) • EyeMed Vision Plan (FPPA Sponsored Plan) • Delta Dental PPO • AARP Health Care Options insured through United Healthcare - Medicare Supplement Plan (effective 10/1/2007) • AARP Medicare Rx Plans insured through United Healthcare – Medicare Prescription Drug Plan (effective 10/1/2007)

Question 10 My insurance plan/carrier is not one of the plans/carriers having a direct payment arrangement with FPPA. How can I get my plan/carrier included in FPPA's program?

Answer The FPPA Board of Directors recently approved the expansion of the direct payment program to include third party insurance providers who comply with FPPA requirements for the payment of premiums on a group basis. Insurance premium payments must be made by FPPA through payroll withholding and must be paid directly to the carrier of the insured member to purchase health or long-term care insurance for the officer or the officer's spouse and/or dependents for that year. The program became effective September 2007. Information on this program including a list of participating insurance carriers and FPPA requirements for other third party carriers to enroll in this program can be found on FPPA's website at www.FPPAco.org.

Question 11 How do I claim the income tax exclusion for eligible health insurance premium payments?

Answer Beginning with the 2007 tax year, retired public safety officers should report their total pension distributions on line 16a of Form 1040. If the officer qualifies for the insurance premium exclusion, then up to \$3000 should be excluded from the taxable amount reported in line 16b of the Form 1040.

Enter "PSO" next to line 16b if you are claiming the exclusion. Instructions are available in the 1040 Instructions for 2007, page 22. When using Form 1040A, report the total pension distributions on line 12a and the taxable amount on line 12b, with the initials "PSO". When using Form 1040NR, report the total pension distributions on line 17a and the taxable amount on line 17b, with the initials "PSO". NOTE: The amount shown in box 2a on Form 1099-R does not reflect the exclusion.

Question 12 If FPPA is already withholding and making health care insurance premium payments for me, and I meet the eligibility requirements, is there anything else I need to do in order to claim the exclusion?

Answer The PPA requires that a member "elect" to have amounts withheld from the member's pension benefit in order to pay qualified health insurance premiums. FPPA believes the form already submitted by the member to his/her employer or to FPPA, authorizing the withholding and payment of premiums from the member's monthly benefit, constitutes a sufficient "election" in this regard. The election, once made, remains in effect until you cancel it in writing. The election is continued when you renew your insurance and have it deducted from your pension benefit.

Question 13 My insurance payment that I make in December is for the coverage period of January next year - will that be included on my statement?

Answer Yes, it will be included in the calculated amount of the eligible insurance premiums because it was paid for in the previous year.

Question 14 Will FPPA report to me the amount of premium payments it has paid each year on my behalf?

Answer FPPA will provide an annual statement to members. The statement will be mailed by January 31 to police officers and firefighters that have PPA eligible insurance premiums deducted from their pension benefit. The amount shown in box 2a of Form 1099-R does not reflect the exclusion. **FPPA**

This document is intended for general informational purposes only and is not intended for specific legal guidance to particular situations. The information provided herein is subject to change based upon official guidance, interpretations or determinations issued by the Department of Treasury or other federal agencies. .