Long-Term Care Distributions

Take-Away: Treasury just provided some additional guidance on taking a distribution from a qualified plan to pay for a plan participant's long-term care premiums.

Background: The SECURE Act of 2022 (the Act) added a provision to the Tax Code that permits 401(k), 403(b) annuity, and 457(b) governmental plans to offer qualified long-term care distributions without an early-withdrawal penalty, so long as the distribution is used to pay for long-term care insurance premiums. The IRS just issued **Notice 2026-33** to provide guidance on this rule. This Notice also extends the period for a qualified plan sponsor to add this optional provision to their plan documents to **December 31, 2027.**

Notice 2026-33: Some of the key clarifications made in this Notice follow.

What is Qualified Long-term Care Insurance Contract? A long-term care contract is defined in the Tax Code. [IRC 7702B.] The definition also includes a life insurance or annuity contract with a rider or other contract provision that pays for long-term care services. The definition also covers a life insurance contract with a rider, which qualifies as a separate contract, and which provides an accelerated death benefit that pays the cost of long-term care services when the insured becomes chronically ill. Under this definition, any long-term care coverage must provide "meaningful financial assistance in the event that the insured needs home-based or nursing home care." This means that such coverage must be adjusted for inflation and provide consumer protections if the coverage is terminated.

Coverage Optional: While the Notice is not totally clear on this point, it appears that long-term care distributions authorized under Notice 2026-33 are optional to the plan sponsor. Accordingly, not all qualified plans must provide this feature.

Who is Eligible? The SECURE 2.0 Act authorizes long-term care distributions if they are used to pay premiums for coverage for the plan participant and the participant's spouse. The Act also gives Treasury the discretion to extend eligibility to any other family member. However, the Notice does **not** address any extension of coverage or eligibility for this benefit.

Annual Dollar Limit: As noted, any long-term care distributions taken during the year must be used to pay premiums for that **same calendar year**. The premium is either paid by the participant or assessed to the participant during the year. The total distributions for that year cannot exceed the *least* of the following amounts: (i) the premium paid or assessed during the year; (ii) 10% of the participant's vested account balance; or (iii) $2,600 (which amount is indexed for inflation.)

Distributions: The Act requires that long-term care distributions must satisfy the **distributable event rules** for 401(k), 403(b), or 457 plans. Thus, a qualified plan can offer a long-term care distribution as a standalone option, even to plan participants who are not otherwise eligible to receive a distribution from the qualified plan. However, there is a limitation under the Notice for 457(b) governmental plans. In the case of a 457(b) plan, the long-term care distributions can only come from amounts attributable to elective, qualified nonelective, qualified matching, or safe-harbor contributions.

No Early-Withdrawal Penalty: The Act exempts a long-term care distribution from the 10% excise tax for early distributions from the plan before age 59 1/2. The Notice clarifies (or limits, take your pick) that any premium paid using the distribution for the participant's spouse's long-term care premium is penalty-free **only if** they couple file a joint income tax return.

Not Rollover Eligible: The Act makes it clear that a long-term care distribution is not eligible as a rollover distribution. In other words, a long-term care distribution- (i) cannot be rolled over to another employer sponsored qualified plan or an IRA; (ii) the plan administrator does not have to provide a rollover notice [IRC 402(f)] to a participant who requests such a distribution; and (iii) the distribution is treated as a nonperiodic distribution that is subject to the 10% withholding rule, unless the participant elects a different or no withholding, i.e., the mandatory 20% withholding rule does not apply.

No Repayment Provision: Unlike some other payback options for qualified plan distributions under the Act, there is no extended 3-year opportunity to repay and recoup the taxes paid on a qualified long-term care distribution, such as, for example, the distribution for personal emergency expenses.

Annual Premium Statement Required: The Act requires that a distribution cannot be treated as a qualified long-term care distribution unless a long-term care premium statement has been filed with the plan administrator. The participant must request this statement from the insurance company **each year** that a long-term care distribution has been requested. The insurer must then send a premium statement directly to the plan administrator. The Notice identifies the information that must be included in the long-term care premium statement. If all the required information is in the premium statement, the plan administrator is entitled to rely on it.

Tax Reporting: The plan administrator must report qualified long-term care distributions on **Form 1099-R**, as a distribution from a retirement plan and/or insurance contract.

Conclusion: As the American workforce continues to age and live longer, and employees continue to save for their retirement with 401(k) account contributions, there is a growing urgency to find funds needed to pay for long-term care insurance. The SECURE 2.0 Act recognized this demographic change and need with the ability to tap-into a 401(k) account to help pay long-term care insurance premiums. I'm not sure that $2,600 a year will pay those annual long-term insurance premiums, but at least it is a start. It's just too bad that the long-term care insurance premium distribution is only optional for plan sponsors.

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