What is the tax treatment for an annuity with a long-term care rider?

Under the Pension Protection Act, annuities issued after December 31, 2009 may include a qualified long-term care insurance rider. Under these rules, inclusion of the rider will not trigger taxable distributions as premiums are deducted from cash value for long-term care premiums, although such charges will reduce investment in the contract.[[1]](#footnote-1) In addition, all long-term care benefits paid under the rider (whether attributable to gains or cost basis) will be tax-free and are excludable from the recipient’s gross income (and not reduce investment in the contract).

In order to qualify for favorable treatment, the long-term care insurance policy must conform to the “qualified” long-term care insurance requirements of IRC Section 7702B. In a private letter ruling, the IRS analyzed the federal income tax treatment of a particular company’s long-term care insurance rider to be offered with certain annuity contracts by an insurance company with respect to taxable years beginning after December 31, 2009, and ruled that the rider will constitute a qualified long-term care insurance contract.[[2]](#footnote-2)

1. IRC Section 72(e)(11); IRS Notice 2011-68. [↑](#footnote-ref-1)
2. IRC Secs. 72, 104, 7702B. [↑](#footnote-ref-2)