



Disability Salary Continuation Plan

For business owners

Ameritas Life Insurance Corp.
Ameritas Life Insurance Corp. of New York



Minimizing uncertainty and maximizing life. That's our calling at Ameritas®. We focus on putting worry behind and the future ahead. A disability salary continuation plan utilizing individual disability income insurance can do just that. It protects your business if a key employee is disabled for a period of time.

A disability salary continuation plan will:

- protect against income loss for your employee
- give you a competitive edge
- provide value added benefits

See the advantages

A disability salary continuation plan offers the following advantages:

- Both you and the employee are aware of the length and amount of benefits a non-productive, disabled employee would receive, eliminating a potential precedent-setting situation.
- The amount of your financial obligation has been established prior to the onset of an employee's disability.
- Disability criteria and qualifications for receiving benefits are clearly defined. A third party, the insurance company, determines the extent of the disability, thus removing the burden from you.
- Any benefits paid to a disabled stockholder employee should be considered wages (not a dividend) by the IRS.
- Premiums are paid when all employees are actively at work providing potential earning power.
- Benefits are paid when a key employee is disabled and the potential earning power is low.
- Premium payments can be deductible as ordinary and necessary business expenses by the employer.

Not only does a disability salary continuation plan offer you a strategy to a potentially costly problem, it benefits your employees, too.

With an insured disability salary continuation plan:

- Employees are protected against loss of income due to disability.
- Only benefits paid during the first six months of disability are subject to Social Security taxation.
- Financial obligations to the Plan remain constant, regardless of the amount of disability benefits that are paid.

Just over one in four of today's 20-year-olds will become disabled before they retire.

Source: Social Security Matters, Understanding Social Security Disability Benefits, 2025.

Consider the facts and risks

The risk of total disability is greater than the risk of death between ages 20 and 65. Below are facts that illustrate the chance of becoming disabled at ages 30, 40, and 50. The more employees you have, the greater chance that one of them will become disabled before age 65. The more time your employees have until they reach age 65, the greater their chance of becoming disabled in that time.

Facts			
Chances that a 90-day disability will occur before age 65			
Age	To any 1 person	To any 1 out of 2 people	To any 1 out of 3 people
30	47%	72%	85%
40	43%	68%	82%
50	36%	59%	74%

Source: GenRe Research, Disability Fact Book, Sixth Edition, 2010.

You have options in funding a plan

Establishing a disability salary continuation plan has many advantages, but don't forget to address the critical issues of funding and administration of the plan. Should you retain all the financial risk of having to pay disability benefits out of your firm's assets, or should you transfer most of that risk to an insurance company? Most business owners choose to transfer all or some of the liability for plan funding. The information illustrated in the following chart may help you in making your decision.

Risks		
Consider...	If you (your firm) retain the entire risk...	If you transfer most of the risk to any insurance company...
FAS 112 requirements	You must meet reserving requirements for claims and carry as a liability on your balance sheet.	The insurance company assumes the risk for claims according to the terms of the contract.
Who determines when there is a claim?	You must determine whether there is a claim.	The insurance company must determine whether there is a claim.
When should the last payment be made?	You decide if and when the person has recovered.	The insurance company, with experienced disability professionals, decides if and when the person has recovered.
Can you control the cost and timing?	Large benefit checks need to be paid out by you at the worst possible time—when you're already missing a key employee.	Smaller and pre-determined premium payments need to be made by you at the best possible time—when everyone is healthy and working. And you can deduct these from your income tax as a necessary business expense.*
Who has the liability?	You have full liability.	The insurance company accepts the liability.

* Please refer to the charts on pages 4 and 5 regarding the Federal income taxation of disability salary continuation plans.

A 25-year-old worker who makes \$50,000 a year and suffers a permanent disability could lose \$3,770,000 in future earnings to age 65 assuming a 3% annual salary increase.

Actual court cases

Learn what can happen when businesses fail to implement proper plans.

Chism:

The Chism Ice Cream Company paid what it claimed was disability salary continuation to a disabled shareholder-employee for some five years before he died. The Tax Court found that there was no plan and noted the absence of anything detailed in writing. The Tax Court decided the payments were not qualified disability salary continuation benefits, but were, in the eyes of the Court, classified as informal dividends. In addition, the Company was not allowed the deduction of payments to the executive. [Est. of E.W. Chism, TC Memo 1962-6, aff'd 322 F.2d 956 (9th Cir. 1963)].

Chesapeake:

In the Chesapeake Manufacturing Company, Inc. v. Commissioner case, there had been a history of shareholder-employee withdrawals that were carried on the books of the corporation as employee advances. One of the shareholders was disabled. During this period of disability, the company took a deduction for the advances as compensation payments. However, the Court felt that these amounts could not be considered salary but were mere nondeductible "informal dividends." There was no documentation showing that at any time the stockholders, directors or officers of Chesapeake established a health, pension or retirement plan. "In our opinion the officer-stockholders in making the withdrawals here in controversy, took the money of Chesapeake for their personal and permanent use and without thought or intent at that time of making repayment to Chesapeake. Consequently we have concluded and found as a fact, that the withdrawals in issue constituted informal dividends to the officer-stockholders for the respective years involved." [Chesapeake Mfg. Co. Inc. v. Comm., TC Memo 1964-214, aff'd 347 F.2d 507 (4th Cir. 1965)].

These are only court case examples and are not to be construed as legal or tax advice.

For more information about disability salary continuation plans, consult your attorney. Your financial services representative can provide more information and can assist you in obtaining disability insurance to help meet your financial needs.

Disability insurance and federal income taxes

Disability Income and Federal Income Taxes*					
Organization Form	Coverage for	Premium Paid by	Owner/Beneficiary	Premium	Tax Treatment Benefits
Sole Proprietor	Sole Proprietor	Sole Proprietor	Sole Proprietor	Not a deductible business expense (IRC Sec. 213 and IRC Sec. 262)	Tax-free (IRC Sec. 104(a)(3))
	Employee	Sole Proprietor	Employee	Deductible business expense. Not taxable income to employee (IRC Sec. 162 and IRC Sec. 106)	Benefits reported as income (IRC Sec. 105)
	Employee	Sole Proprietor	Sole Proprietor	Not a deductible business expense (IRC Sec. 265)	Tax-free (IRC Sec. 104(a)(3))
	Employee	Employee funds received through bonus	Employee	Employee bonus is tax deductible to the business and is reported as income to employee (IRC Sec. 162 and IRC Sec. 61)	Tax-free (IRC Sec. 104(a)(3))
Partnership	Partner	Partnership	Partner	Deductible by partnership and taxable to partner as a guaranteed payment (Rev. Rul. 91-26)	Tax-free (IRC Sec. 104(a)(3))
	Employee	Partnership	Partnership	Not Deductible by partnership (IRC. Sec. 265) Not taxable to employee (IRC Sec. 106)	Benefits taxable as income (IRC Sec. 105)
	Employee	Employee funds received through bonus	Employee	Employee bonus is tax deductible to the business and is reported as income to employee (IRC Sec. 162 and IRC Sec. 61)	Tax-free (IRC Sec. 104(a)(3))
"C" Corporation	Employee and Shareholder/Employee	Corporation	Employee and Shareholder/Employee	Deductible business expense. Not taxable income to employee (IRC Sec. 162 and IRC Sec. 106)	Benefits reported as income (IRC Sec. 105)
	Employee and Shareholder/Employee	Corporation	Corporation	Not deductible business expense (IRC Sec. 265) Not taxable income to employee (IRC Sec. 106)	Tax-free (IRC Sec. 104(a)(3)) (Possible AMT tax IRC Sec. 55 and IRC Sec. 56)
	Employee and Shareholder/Employee	Employee funds received through bonus	Employee and Shareholder/Employee	Employee bonus is tax deductible to the business and is reported as income to employee (IRC Sec. 162 and IRC Sec. 61)	Tax-free (IRC Sec. 104(a)(3))
Limited Liability Company (LLC)	Since 1996, the owners of LLCs have been able to elect the taxation of their LLC by "checking" the box on IRS Form 8832. Although the majority of LLCs are taxed as partnerships, many are taxed as corporations or sole proprietorships. The income tax treatment of an LLC's disability salary continuation plan, therefore, will depend upon the owner's election.				

Disability Income and Federal Income Taxes* cont.					
Organization Form	Coverage for	Premium Paid by	Owner/ Beneficiary	Premium	Tax Treatment Benefits
Personal Service Corporation	Employee and Shareholder/ Employee	Corporation	Employee and Shareholder/ Employee	Deductible business expense. Not taxable income to employee (IRC Sec. 162 and IRC Sec. 106)	Benefits reported as income (IRC Sec. 105)
	Employee and Shareholder/ Employee	Corporation	Corporation	Not deductible business expense (IRC Sec. 265) Not taxable income to employee (IRC Sec. 106)	Tax-free (IRC Sec. 104(a)(3)) (Possible AMT tax IRC Sec. 55 and IRC Sec. 56)
	Employee and Shareholder/ Employee	Employee funds received through bonus	Employee and Shareholder/ Employee	Employee bonus is tax deductible to the business and is reported as income to employee (IRC Sec. 162 and IRC Sec. 61)	Tax-free (IRC Sec. 104(a)(3))
"S" Corporation	More than 2% Shareholder	Corporation	More than 2% Shareholder	Not deductible by the S Corporation (IRC Sec. 262, IRC Sec 162) Taxable to the More Than 2% Shareholder (IRC Sec. 1372)	Tax-free (IRC Sec. 104(a)(3))
	Employee or 2% or less Shareholder	Corporation	Corporation	Deductible business expense (IRC Sec. 162) Not taxable income to employee (IRC Sec. 106)	Benefits taxable as income (IRC Sec. 105)
	Employee or 2% or less Shareholder	Employee funds received through bonus	Employee	Employee bonus is tax deductible to the business and is reported as income to employee (IRC Sec. 162 and IRC Sec. 61)	Tax-free (IRC Sec. 104(a)(3))
Disability Overhead Expense					
Organization Form	Premium Paid by	Owner/ Beneficiary	Premium	Tax Treatment Benefits	
All forms of Eligible Business	Sole proprietor or business	Sole proprietor or business	Tax-deductible (Rev. Rul. 55-264, 1955-1 CB 11)	Reportable as income. However, overhead expenses which are deductible as ordinary business expenses will, to the extent deductible, offset the reportable benefits.	

* The information in this chart is provided as general helpful information. Please consult your professional tax advisor for specific advice.

For more information about disability salary continuation plans, consult your attorney. Your financial services representative can provide more information and can assist you in obtaining disability insurance to help meet your financial needs.

Employer versus employee paid

As an employer, should I pay the premiums for a disability salary continuation plan, or should my employees pay the premiums under a Section 162 Bonus Agreement?

Assumptions

Male 35, Non-Tobacco		
Tax Bracket Employer	(Federal and State)	21%
Tax Bracket Employee	(Federal and State)	24%
Earned Income		\$105,000
Definition of Disability	Own Occupation and Not Engaged for the entire benefit period	

Taxation of Benefits

Employee Paid Premium Bonus Section 162 (Tax Free Benefits)		Employer Paid Section 105 (Taxable Benefits)
\$5,200	Monthly DI Benefit	\$6,700
\$62,400	Annual DI Benefit	\$80,400
N/A	Employee Taxable Income	\$80,400
N/A	Employee Tax Due	\$19,296
\$62,400	Net DI Benefit	\$61,104

Employer Outlay

Section 162		Section 105
\$1,288	Premium	\$1,648
\$1,288	Bonus	0
\$ 326	Double Bonus	0
\$1,554	Gross Employer Outlay	\$1,648
\$1,288	Net Employer Outlay	\$1,302

"My wife Arlene and I are managers of a family-owned and operated business. We were very uncomfortable with the idea of having to determine the extent of a disability should a key employee suffer a debilitating injury or illness. That's one of the reasons we added a disability salary continuation plan to our benefits package. Now that burden is no longer ours, but lies with the insurance company. We feel good that we've provided an added benefit for some very important people in our lives."

Bill and Arlene R.
Managers and co-owners of a floral shop

Disability salary continuation plan specimen

A specimen disability salary continuation plan can be provided by your financial representative for review by your attorney.

This is a specimen document only. Its content, legal and tax consequences must be reviewed and approved by qualified legal and tax advisors before it is utilized for any purpose.

SPECIMEN

Disability Salary Continuation Plan

WHEREAS, (Name of Employer), hereinafter referred to as "Employer", recognizes the risk of being sick or hurt is far greater than the risk of dying during one's employment years; and,

WHEREAS, Employer wishes to provide (Name of Employee), hereinafter referred to as "Employee", an additional benefit in order to retain Employee's services and enjoy the benefit of Employee's knowledge and experience.

NOW THEREFORE, in light of the foregoing concerns and desires, the Employer hereby establishes the following Disability Salary Continuation Plan, hereinafter referred to as "Plan".

I. Plan Total Disability Benefits

All employees will receive full salary during the first ¹_____ days of total disability, fully offset by any Worker's Compensation, State Cash Sickness or other federal, state or municipal benefits. ²

A. Class A employees will receive full salary for the following _____ days, fully offset by ³ any Worker's Compensation, State Cash Sickness or other federal, state or municipal benefits, as well as benefits provided under long term disability insurance contracts for which the premium is paid for, all or in part, by the Employer.

B. Class B employees will receive no benefits from the Employer after the first _____ days of salary continuation except that if they elect to participate in the employer sponsored disability insurance plan, they may receive benefits through the insurance company underwriting the contracts. The Employer will contribute _____ of the cost of such insurance as an incentive for the Employee to participate.

II. Plan Residual Benefits

Residual disability benefits are available to Class A employees who qualify and to certain Class B employees who qualify due to income and job. Residual disability concerns the after-effects which cause an individual who returns to his/her job to have a 20% or greater loss in earned income. This income loss may be due to the Employee's being unable to perform all of his/her former duties or because the individual is not able to work for as much time as he/she did before the disability.

1. Typically 30, 60 or 90 days.
2. Use even in non-cash sickness states to avoid future changes in Plan.
3. Class A employees are typically identified by officer status, managerial responsibility or salary. Class B employees typically include all other full time employees.

III. Amount of Disability Benefits

The monthly disability insurance benefit you qualify for will be determined by the current Issue and Participation tables of the (Insurance Company), at your time of application.

IV. Definitions

Definition of total and residual disability and other provisions will be solely determined by the provisions of the disability insurance contracts underwritten by (Insurance Company).

V. Named Fiduciary and Plan Administrator

(An Officer, usually Secretary – Treasurer) is hereby designated the "Named Fiduciary And Plan Administrator" hereinafter referred to as "Fiduciary" until resignation or removal by the Board of Directors. Fiduciary shall be responsible for the management, control and administration of the Plan as established herein. Fiduciary may allocate to others certain aspects of the management and operation responsibilities of the Plan including the employment of advisors and the delegation of any ministerial duties to qualified individuals.

VI. Amendment and Termination

This Plan may be amended or terminated at any time only by the Corporation's Board of Directors.

VII. Claims Procedures

With respect to any period of uninsured disability, it shall be the obligation of the covered Employee to notify the Fiduciary of his/her disability as soon as is feasible. Such disabled Employee shall further provide the Fiduciary such proof or evidence of total disability as he or she may require. If a claim under this provision is denied, the Fiduciary shall provide, within ninety (90) days of such claim filing, written notice setting forth the specific reason for denial including specific reference to the provision of this upon which the denial is based and any additional information required to perfect the claim together with any steps required to request further review. Upon the Employee's request for review within sixty (60) days of receipt of the claim denial, Employee or his or her representative shall be permitted to review the Plan or any related documents and to submit issues and comments in writing. If this first request for review is thereafter denied by the Fiduciary, Employee may request a second review within sixty (60) days of the first review denial. In the event this second request for review is further denied, then Employee or his personal representative may submit the dispute to a Board of Arbitration. Said Board shall consist of one member selected by the Employee, one by the Employer and one selected by the first two members so selected. The Board shall operate under any generally recognized set of arbitration rules and the Employer and Employee agree that they, their heirs, successors and assigns shall be bound by the decision of the Board with respect to any controversy.

VIII. Interpretation

This Plan shall be construed to comply with Sections 105, 106, and 162 of the Internal Revenue Code, the Employee Retirement Income Security Act of 1974 and all rules, rulings and regulations pertaining to such Code and Acts.

IX. Nonassignability

This Plan and the rights, interest and benefits receivable hereunder from the general assets of the Employer shall not be assigned, transferred, pledged, sold, conveyed, or encumbered in any way by the Employee and shall not be subject to execution, attachment or similar process. Any attempted sale, conveyance, transfer, assignment, pledge, or encumbrance of this Plan or of such rights, interest and benefits, contrary to the foregoing provisions, or the levy of any attachment of similar process thereupon, shall be null and void and without effect.

X. Amendment and Termination Procedure

It is the intention of the Employer that this Plan shall continue, in effect, indefinitely. Nonetheless, the Employer reserves the right to amend or terminate this Plan at any time or times, in whole or in part, by duly adopted resolution of the Employer's Board of Directors, notice of which would be promptly given to the Employee. No such amendment or termination, however, shall affect the rights of an Employee to receive benefits hereunder for any covered disability as determined pursuant to Section IV above, which arose after the effective date hereof, but prior to the said amendment or termination.

XI. Notice of Plan Participation and Summary Plan Description

Receipt of a signed copy of this Plan shall constitute Employee's Notice of Participation as well as their Summary Plan Description.

IN WITNESS WHEREOF, the Employer has caused this Plan to be executed in its name and by its Officers hereunto duly authorized, as of _____ (Date) _____. Receipt by Employee of a copy of this Plan shall constitute receipt of Employee of the Plan's Summary Plan Description.

Employer: _____

By: _____ (Name) _____, President

Attest: _____ (Name) _____, Secretary

Acknowledgement of Receipt of Plan and Summary Plan Description

Receipt of this copy of the Disability Salary Continuation Plan and Summary Plan Description is hereby acknowledged by (Employee) this: _____ (Date) _____.

(Name) _____, Employee

(Name of Employer)

Where do you go from here?

A comprehensive, quality benefits package can help develop high morale and job satisfaction. A disability salary continuation plan can help you retain the loyalty and services of your key employees. Meet with your financial professional and discuss the benefits this type of plan can have for you, your employees and your business.



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The information presented here is not intended as tax or other legal advice. For application of this information to your specific situation, you should consult an attorney. Contact your representative for more information and assistance in obtaining life insurance and other products to help meet your financial planning needs.

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