

# salary continuation plans

sales idea

**Smaller firms with active owner-managers will be more likely to see the advantages of a salary continuation plan as a way to insure themselves and other key employees against disability, while using the tax code to their advantage. As a producer, you are positioned to make a possible multi-life or even a Guaranteed Standard Issue (GSI), disability insurance sale.**

The need for disability planning is real and your efforts to educate and guide business owners through the planning process are often necessary to get them to act.

A disability salary continuation plan is a corporate-sponsored benefit generally designed to replace part or all of an executive's income in the event of his or her disability. The benefit plan is generally exempt from ERISA and typically is confined to a select group of highly compensated employees. Many employers might want to continue to pay a disabled employee while he or she recovers. However, doing so without having a bona-fide salary continuation plan in place prior to the disability can create problems for the business:

- The IRS could view the arrangement as a settlement and not as salary, so the business could lose the ability to claim the payment(s) as a tax-deductible expense
- Without a plan, detailing the participants, the business might be subject to discrimination claims

The plan is a written document that sets out the plan parameters. While it does not have to be insured, usually it makes economic sense to use insurance as the funding vehicle, and the premiums are deductible to the business.

Your role is to demonstrate to business owners how and why they should develop and implement a salary continuation plan, prior to any disability occurring. You are providing valuable business planning advice, along with documents that can facilitate the design and implementation of the plan to employers and other key business strategists, such as their accountants and legal advisers.



## Questions to Develop the Need for a Salary Continuation Plan and Insuring the Plan

These questions will allow you to uncover the need and highlight the advantages to the business and the key employees. How they answer these questions will help you develop what their plan might look like.

**Question:** You have indicated that there are some key employees on your staff that you would want to be able to provide continued salary if disabled. Would you want all of this class of key employees to receive the same benefits?

**Action:** Develop class or classes of eligible employees for the salary continuation plan.

**Question:** You have indicated you want to have the same benefits for all the employees in the group. What existing employer-provided short or long-term disability programs do you currently provide to your employees? Can I assume that you and the other key employees are also covered under this group plans?

**Action:** Gather information about existing group short term disability or long term disability plans and any sick-pay or paid time off (PTO) programs currently managed by the employer.

**Question:** In order to coordinate with underlying short-term plans or PTO, and in order to maximize the premium discounts, I am recommending you have a 90-day wait on your salary continuation program for you and the other key employees. Would you agree?

**Action:** It is important to note that a salary continuation plan can be funded or unfunded. Unfunded means the employer is liable for the costs of the ongoing salary to the key employee. The use of individual disability income policies allows the employer to 'fund' the program through insurance once the elimination period is met. This can and should be stressed as very positive since the premiums are deductible as a normal business expense and the long-term exposure is passed to an insurance company, which is more able to handle the monthly costs of such a program and also provides claims management and adjudication.

**Question:** I recommend we look at self-insuring the first three months, and use individual disability income policies for you and the other key employees. Typically, I recommend the following:

- Plans with a 90 day elimination (waiting) period.
- Maximum benefit period based on the insurance carrier's Issue and Participation Limits
- Benefits to Age 65
- Residual and a Cost of Living Rider

How does age 65 sound to you?

## Developing the Salary Continuation Plan

A salary continuation plan details a business's plan should a key employee become too sick or hurt to work. This plan should be in writing, and needs to be in place prior to the disability. Ameritas Life has created sample forms for you to share with the business and their legal advisors. It is highly recommended you let the business's attorney have the sample documents and draft the plan. Within this planning process, the business owner can determine:

1. Who is covered under the plan (remember, within general discrimination rules, the employer can select, by class, the covered group under the plan)
2. How long the employee needs to be disabled prior to the disability benefits being payable
3. The benefit schedule (flat dollar amount, percentage of salary, etc.)
4. How long benefits are payable

Spelling out these items allows you to work with your client to develop a plan that meets your client's needs. More importantly, it allows employers to feel that they are in control of the process.

After developing the basic design for the employer's plan, the next step is to get the information and sample plan documents to the employer's legal counsel. The client's attorney should then draft the documents, and the company's board should approve the resolution and then notify the covered employees of the plan, in writing, as required by the regulations. Your client's attorney can provide your client with more details on this requirement.

## To Fund or Self-Insure the Plan

Once a salary continuation plan is in place, the plan is automatically considered “funded” by the employer, whether or not funding exists. If the plan is uninsured, the entire responsibility of funding falls on the business.

Depending on the business an unfunded salary continuation plan could be devastating to smaller business. In addition to the continued wages being paid to the disabled employee, it is likely that the employer may have to hire a replacement worker. In other words, the employer may have to pay two paychecks.

Self-funding the disability income insurance plan also puts the employer in the potentially difficult position of having to make claims decisions. Not only does the employer have to decide if the employee is disabled, but the employer also has to determine when they feel the employee can come back to work. The most difficult situation is when the employee and the employer disagree on the prognosis, the claim, return to work or length of disability. Imagine an untrained business owner or human resources representative having to make those judgments or handle the communication of an unpopular decision.

Salary continuation planning allows you to work with business owners and show them how to use well-established IRS rules and regulations to their advantage. It allows you to advise the employer on ways to provide meaningful benefits within their budget. The use of insurance shifts the responsibility for determining the claim validity from the employer to Ameritas Life. This provides financial support as well as initial and ongoing claim administration and service to the disabled employee.



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