

Disability Tax Guide



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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	Not a deductible business expense (IRC Sec. 262 and IRC Sec. 162)	Tax-free (IRC Sec. 104(a)(3))	
	Employee	Partnership	Employee	Deductible business expense. Not taxable income to employee (IRC Sec. 162 and IRC Sec. 106)	Benefits reported as income (IRC Sec. 105)	
	Employee	Partnership	Partnership	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))	
"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))	
<p>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 Salary Continuation Plan, therefore, will depend upon the owner's election.</p>						
"S" Corporation	More than 2% Shareholder	Corporation	More than 2% Shareholder	Not a deductible business expense (IRC Sec. 262, IRC Sec. 162 and IRC Sec. 1372)	Tax-free (IRC Sec. 104(a)(3))	
	Employee	Corporation	Employee	Deductible business expense. Not taxable income to employee (IRC Sec. 162 and IRC Sec. 106)	Benefits reported as income (IRC Sec. 105)	
	Employee or 2% or less Shareholder	Corporation	Corporation	Not a deductible business expense (IRC Sec. 265)	Tax-free (IRC Sec. 104(a)(3))	
	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))	

Business 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; it is not intended as tax or other legal advice. Clients should consult with their professional tax advisor for specific advice.