What Small Business Accountants Needs to Know About Social Security Disability Benefits

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What does Social Security have to do with Accounting?

Recipients of Social Security disability benefits rely on those benefits in order to live day to day. By not knowing the rules surrounding these benefits, an accountant can cause a client to lose benefits through not helping the person manage the business income. There have been cases where a Social Security disability beneficiary has lost SSA monthly payments of more than $2,000 because of monthly business earnings of $800 - $900. It is critical that an accountant understand the rules, tests and amounts that a client’s financials will be subject to, and some of the programs that can be used to reduce countable income for Social Security purposes. The accountant also needs to be aware of SSA rules so the client can be advised of possible accruals and deferrals or purchases for cash based clients which can be used to shift income between periods.

In other cases disasters occur when a small business owner, at the suggestion of his accountant, starts an IRA, Defined Benefit Plan, Keogh or other retirement instrument. In some cases this, as well as common suggestions such as a deferred income plan, can cause the loss of Social Security benefits.

The methods and suggestions we offer here are not to manipulate overall earnings, but to control income in such a way that the client can manage the timing of the eventual loss of benefits. Keep in mind that loss of benefits may cause the loss of medical benefits that may be critical to the ability of the client to maintain the business.

This paper touches on numerous concepts related to small business accounting procedures as they may affect individuals who are self-employed and receive a disability benefit from the Social Security Administration (SSA). This document is not intended to be a comprehensive statement of policies, or to give accountants all that they may need to know with respect to specific cases. This is an overview to highlight key points and potential problem areas. If the business and record keeping are set up to accommodate the individual’s disability benefits, it reduces the amount of work required for reporting to the various agencies. There are additional resource papers on specific areas which are listed in the body of this document.

Overview

There are two different Social Security benefit programs available to people who meet SSA’s criteria for being “disabled”. These two benefit programs operate in isolation of

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one another with separate and distinct rules and regulations and each program is affected by earned income very different ways.

The first program is Supplemental Security Income (SSI). This is a “means-tested” program intended to pay for the basic costs of food and shelter for people who have very little income and few resources. The SSI program contains very specific limits in the amount of unearned income, earned income and resources a person may have and still retain eligibility for the program. Fortunately, the SSI program treats earned income (from either wage employment or self-employment) rather favorably. Basically, an SSI recipient experiences a dollar-for-dollar reduction in cash benefits for unearned income, but only loses one dollar of benefit for every two dollars of earned income.

The second group receives disability benefits authorized under Title II of the Social Security Act. This type of benefit has several subgroups, but is most commonly referred to as Social Security Disability Insurance or SSDI. These benefits are NOT means-tested, but are available to individuals who meet SSA’s disability standard and who have accumulated enough work credits to establish insured status. SSDI beneficiaries are not limited as to assets or resources, and unearned income is not a factor in their benefits. However, earned income over a specified limit which SSA refers to as substantial gainful activity or SGA will eventually cause benefits to be terminated. In the SSDI program, benefits are not gradually reduced by earnings as is done in the SSI program. SSDI benefits are either paid in full, or not paid at all.

A surprising number of people receive both SSI and SSDI benefits. Reporting and management become more complicated when a beneficiary gets both types of disability benefits since two different sets of rules will apply simultaneously!

Business Structure

Business structure is one of the few areas that have some common features between the two disability programs. SSA has a large number of rules and policies they use when dealing with corporations, including small business corporations. SSA tends to view corporations very skeptically and this bias can cause problems for the business owner. In addition to the rules about the corporation, there are additional rules about payments to officers, directors and major shareholders. The way that SSA treats income generated through corporations is complex. A separate paper on this topic is available at the Venture Mentor’s website www.venturementors.biz.

The basic thing you need to know is the rules used by SSA for corporations will generally treat the business owner in the worst possible way with regards to the benefits, regardless of whether the individual gets SSI, SSDI, or both. In very few cases is it in the best financial interests of the beneficiary to establish a business using a corporate structure!

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SSI

In the SSI program, ownership of a corporation or part of a corporation is viewed as a countable asset. SSI recipients are only allowed to have $2,000 in countable resources. Once their share of the value of the corporation exceeds that level, SSI recipients lose their benefits. SSI does allow assets to be held within a business at any level, but corporate ownership is considered a personal asset.

SSDI

On the surface it appears that a corporation might be a good way for a person on SSDI to operate. The problem is that SSA has written policies which are supported by law that virtually ANY money paid out of the corporation to a director, officer or major shareholder is considered to be earned income. While SSDI is favorable to unearned income, there are rather severe limits placed on earned income. The SSA regulations also allow SSA to look into the corporation and apply corporate earnings directly to the individual.

Other structures are more favorable for a SSA beneficiary. For example, SSA does not currently have regulations or policies concerning LLCs, so they fall under the general guidelines of partnerships and sole proprietors. <u>In almost all cases, an LLC structure will be more beneficial to a business owner receiving SSA disability benefits than any other structure!</u>

Accounting Methods and Techniques

SSI

SSI beneficiaries lose $1.00 in benefits for every $2.00 net income. The SSA term is Net Income from Self-Support (NESE). Net Income is taken for a period of time and averaged for reporting to SSA. A cash basis of accounting works well for someone on SSI, because SSA is concerned with the cash received, and will reduce benefits based on the net cash in. An SSI recipient is allowed to hold any value of assets in a business as Property Essential for Self-Support (PESS). Personal resources may not exceed $2,000 for an individual or $3,000 for a married couple. Some resources, such as a vehicle and a home, are excluded from this resource test. The important point to remember is that resources in excess of the $2,000/$3,000 limit will cause termination of SSI cash benefits as well as Medicaid insurance coverage that comes with SSI.

SSDI

In the SSDI program, SSA is looking to see if gross monthly income exceeds certain dollar figures. The most important figure is “substantial gainful activity” or SGA

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because consistent earnings above this figure will eventually cause termination from benefits. SSDI beneficiaries must track self-employment income on a month by month basis, so the most advantageous accounting for SSDI recipients is the accrual method. Keep in mind that SSDI is NOT means-tested, so there is no need to be concerned about resources, assets or any unearned income.

The major considerations for this group are provisions known as the Trial Work Period (TWP), Extended Period of Eligibility (EPE) and Substantial Gainful Activity (SGA). A beneficiary is allowed a nine month Trial Work Period to test their ability to work and be assured that their benefits will continue. Income can be at any level during the TWP. Every year, SSA sets a dollar figure that triggers use of TWP months. When net earnings from self-employment exceed that figure or if the beneficiary works more than 80 hours on the business in a month, the beneficiary will have used one of the available nine TWP months. The TWP does not end until all nine months have been used within a rolling 60 month period. The TWP is important because it provides a breathing period for the business to get stable and to find out if the person is capable of running the business long-term without risking loss of benefits.

After the TWP is over, there is a second safety net known as the Extended Period of Eligibility (EPE). During this 36 month period, beneficiaries who lose benefits due to SGA level work are able to come back into benefit status again without having to re-apply. SSDI beneficiaries are allowed to work and receive a benefit check indefinitely as long as their earnings do not represent Substantial Gainful Activity (SGA). If the net business income exceeds the current SGA guideline for a period of months or shows a consistent pattern of SGA level earnings, termination will eventually occur. Keep in mind that SSDI benefits are paid in an "all-or-nothing" manner, unlike the gradual reduction of benefits characteristic of the SSI program. SSDI beneficiaries are either eligible for the full cash payment or no cash payment at all

<u>Managing net business income levels in relation to the TWP and SGA guidelines is of critical importance for many SSDI beneficiaries</u>. This allows beneficiaries to plan for the replacement income needed before cash benefits and medical insurance are lost. Failing to manage business income in relation to TWP and SGA guidelines can cause your clients severe financial distress and/or loss of critical health insurance coverage.

Social Security Work Incentives

SSI

There are some special incentives to help an SSI recipient start a business. If an SSI recipient has income other than the SSI check (including a SSDI check) there is a work incentive called a Plan for Achieving Self-Support (PASS). This provision allows the person to set aside the money for the business and SSA will ignore it for the calculation

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of the SSI check. This means that the SSI check can increase if the person is setting aside unearned income and will remain the same or decrease less if the person is setting aside earned income. PASS funds are considered to be "owner equity" for the purpose of taxes and external reporting. A business owner can reduce net earnings from self-employment (NESE) for SSA reporting purposes by setting it aside in a PASS. Depending on the individual's circumstances, PASS funds can be a lump sum, a monthly payment or both.

The next work incentive available to an SSI recipient is an Impairment Related Work Expense (IRWE). SSA allows beneficiaries to reduce countable NESE by deducting the cost of certain expenses related to the disability that are needed for the person to be able to work. These costs can include prescription drugs, transportation, special equipment and many other expenses that may be required to allow the person to work and maintain the business.

Property Essential for Self-Support (PESS) allows the business owner to have assets and cash in the business that do not count as resources or cash to the beneficiary.

1619(b) is a special provision that allows the person to retain their Medicaid medical benefits as long as they meet certain requirements. The basic requirements are:

1. The person has lost cash benefits due to their work effort.
2. All other resource and unearned income requirements of the SSI program are met.
3. NESE does not exceed the state allowable level (threshold) of earnings for their state program. (In some special cases, even this level can be exceeded)

SSDI

As discussed above, the Trial Work Period (TWP) and the Extended Period of Eligibility (EPE) are work incentives that apply to SSDI beneficiaries. There are several additional incentives available.

SSA recognized that some people with disabilities receive special assistance from agencies or others to operate their businesses. This is a form of "subsidy" which can be leveraged to reduce countable net earnings for the purposes of an SGA determination. Both "unincurred business expenses" and "unpaid help" will often need to be tracked in a business. An unincurred business expense is a contribution to a business made by others that would otherwise have to be paid for. An example is the state VR agency providing equipment to the business. A common example of unpaid help would be when a family member helps the beneficiary with accounting or sales with no remuneration. The value of those services can be deducted from NESE for SSA reporting purposes.

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Most individuals with disabilities receiving Medicare will continue to receive Medicare for at least 93 consecutive months after TWP ends. This continues even with the loss of cash benefits and is not dependent upon level of income, earnings or assets.

Other Problems and Help

Each state has a number of different public benefit or income support programs that may impact your client positively or negatively. In addition to Social Security benefits, your clients may be receiving assistance such as rental subsidies, food stamps, Medicaid services, or other special benefits for people who are disabled and of low-income. It is in the best interest of the client to have a basic understanding of how business growth, income and assets will affect each of these programs. In each state there are Benefits Planning Assistance and Outreach (BPAO) programs designed to help people make informed choices about work or employment as it may affect their benefits. Many of these Benefits Specialists are not familiar with self-employment issues and the SSA policies governing self-employment. They can help your clients understand the public benefits and, with your client's approval, this person can provide you with information that might be pertinent to your client.

Venture Mentors, LLC is involved in both the business and benefit sides of the equation. While not being familiar with state specific programs, we are knowledgeable in Social Security policies and procedures, especially in connection with self-employment, and the federal law that governs the state programs. We are happy to assist you in evaluating your client's position with regards to benefits and benefit management. We have experience tailoring business structures to meet specific needs of Social Security disability beneficiaries. It is suggested that a schedule be created and maintained so key values can be easily tracked and the client can have early warning when approaching an SSA trigger point. Information and links are available on our website at www.venturementors.biz.

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