

## What Should You Look for in a Disability Policy?

If you find that you need an individual disability policy over and above any other income protection you may have, here's what you need to know:



encourage workers to remain at home, limit benefits from all sources to no more than 70 to 80 percent of monthly income. Lower-paid workers can expect to receive more of their predisability incomes while higher-paid workers generally receive less.

### Definition of Disability

Policies vary. Some pay benefits if you are unable to perform the duties of your customary occupation, others only if you can engage in no gainful employment at all. Be sure to ask your insurance agent how various policies define disability.

### Extent of Disability

Some older policies require that you be totally disabled before payments begin. Partial disability sometimes is covered for a limited time but most often only if the partial disability follows a period of total disability for the same cause. Some policies may not require total disability before partial disability payment.

### "Residual" Benefits

If you are able to work but your income is reduced because you cannot fulfill all of your job responsibilities, residual benefits can help to make up the difference in your income. A standard feature in some policies (added with a rider to others), a residual benefit allows partial payment based on your loss of income without prior total disability.

### Presumptive Disability

Even if you can still perform some or all of your regular job, you are presumed fully disabled and are entitled to full benefits under specified conditions. Those conditions typically include loss of sight, speech, hearing, or use of limbs.

### Size of Benefits

Monthly benefits are calculated in terms of stable, earned income at the time of purchase. Most insurers, not wanting to provide benefits so sizable that they would

### When the Payments Begin

Today's policies allow you to decide when benefit payments begin. You can choose a waiting period at the time of application; these range anywhere from the 31st day to six months or more after the onset of the disability. Depending on how much money you have saved, and your other resources, you can reduce your premiums by electing to wait 60 days, 90 days, or even six months before you start to receive benefit payments. Remember, though, that the first check is usually not paid until 30 days after the waiting period.

### Length of Coverage

By choosing a benefit term, you will elect benefits that are payable for one year, two years, five years, to age 65, or for a lifetime. Since disability benefits are designed to replace earned income, most people do not need benefits extending beyond the working years. Electing shorter benefit periods can save premium dollars, but bear in mind that if you need this insurance at all, you probably need it most to cover a disability that permanently removes you from the work force. A lengthy disability threatens your financial security much more than a short term disability.

### Keeping Pace With Inflation

For an additional premium, you can add a cost-of-living adjustment (COLA) to basic disability income coverage. This provision increases benefit payouts by a specified percentage, generally 4 to 10 percent, after each year of disability and can be important particularly during a lengthy

period of total disability. While this is a relatively expensive option, it could be vital to maintaining your standard of living.

Most policies include a waiver of premium provision, so that you don't have to pay any more premiums after you're disabled for 90 days. Some policies offer the opportunity to buy additional disability coverage to keep pace with a rising income, without having to pass a medical examination or to submit further medical evidence of insurability.

### **What Else Do You Need to Know?**

Selecting the level and duration of benefits is only the first step. To be sure that coverage will continue, you should ask about renewability. Disability insurance comes three ways: Non-cancelable policies give you the right to continue a policy by timely payment of premiums, and the insurance company cannot change the premiums and benefits shown in the policy. Guaranteed renewable policies will be automatically renewed, with the same benefits, but the premium may be increased if it is changed for an entire class of policy-holders. Optionally renewable or conditionally renewable policies are extended at each anniversary or premium due date if the insurance company decides to do so. (Some policies are renewable to age 75 if you are still employed full time.)

In general, if you pay the premiums for an individual disability policy, payments you receive under the policy are not subject to income tax. If your employer had paid some or all of the premiums, some or all of the benefits may be taxable.

When you buy, consider a policy that pays disability benefits for both accident and illness. Some policies pay only for accidents, but you want to be insured for illness too. In fact, as you get older, it is more likely that you will need to be covered for an illness than for an injury.

### **What Kind Of Business Protection Is Available In The Event Of Disability?**

Income replacement insurance is particularly important if you own a small business. In addition to standard disability

policies, some policies have such special features as:

- Recovery benefits that pay after you return to work full time, during the period in which you are reestablishing a customer or client base.
- Overhead expense coverage that pays for certain office expenses, over and above the disability benefits that replace personal income.
- For jointly owned businesses, a disability buy-out policy disburses funds for one partner, or the business entity, to buy a disabled partner's share of the business.
- Key-person insurance, which protects a firm against the loss of income resulting from the disability of a key employee.

### **What Insurance Do You Need?**

Many people who thoughtfully protect their families against the loss of income from a breadwinner's death fail to think about what would happen if that breadwinner were unable to earn a living because of a disability. In fact, long-term disability may worsen a family's financial situation more than a wage earner's death because income stops, but expenses continue.

Consider Bob and Ann Jackson. Bob and Ann, who live in a Midwestern city, are parents of a 6-year-old girl. Bob, 31, earns \$32,000 selling computers. His monthly take-home pay is \$1,994. After staying home several years to care for their daughter, Ann is now a part-time saleswoman in a local boutique. She brings home \$338 a month. Life is uneventful for the Jacksons, until Bob becomes so ill that he can no longer work. Suddenly there is a dramatic reduction in the Jacksons' income. Because they live in a rental apartment, they have no mortgage disability insurance to cover basic housing costs. Bob isn't eligible for Social Security disability. (To be eligible, Bob would have to demonstrate that he is unable to engage in any gainful work that exists in the national economy, regardless of whether such a job exists in the area in which he and Ann live.) Bob has no prior military or civil service that might qualify him for other government disability

programs. He does not qualify for workers' compensation benefits because his illness is not job-related.

The specifics of what happens next depend greatly on whether or not Bob's employer offers group disability benefits, whether these benefits are short term (STD) or long-term (LTD), whether the policy includes a cost-of-living adjustment, and how the group policy defines disability.

If Bob's employer does provide Group LTD, Bob would be entitled to benefits under his employer's policy--probably 60 percent of his gross salary, or \$1,600 a month. Of this amount, he would have to pay \$193 in federal income taxes and \$100 in state income taxes. To continue his family's group medical policy, he will have to pay the portion of his health insurance premium that was previously paid by his employer. Under this scenario, the Jacksons' monthly income (including Ann's current salary) would be almost 30 percent less than their former income. Will this be adequate or not? The Jacksons may save money with Bob staying at home (he is no longer commuting to work, for example), and Ann may adjust to the situation by becoming the principal wage earner. Thus, the employer-provided group disability policy may well be enough.

However, not all employers provide disability benefits. What if Bob is employed by a small firm that has no group disability benefits at all? Or what if the Jackson's situation is such that they need more than they would get under the group policy? Under such circumstances, an individual disability income insurance policy might be just the right answer.

#### **What Should You Remember?**

When you are considering individual disability income coverage, a well-trained benefits consultant, financial counselor, or insurance agent can help. Ask about the following:

- What is an adequate level of benefits if you are disabled, in relation to your present and future obligations?

- How long of a waiting period should you select to fit your circumstances until benefits begin?
- How long do you want to receive disability income should it become necessary?
- What related benefits, such as partial or residual disability, are available?
- Is the policy noncancelable, guaranteed renewable, or conditionally renewable?
- How much coverage are you eligible for at your present salary?

#### **A Final Word**

Insurance policies are legal contracts. Read and compare the policies you are considering before you buy one, and make sure you understand all of the provisions. Marketing or sales literature is no substitute for the actual policy. Read the policy itself before you buy. Ask for the insurance company's ratings. The A.M. Best Company, Standard & Poor's Corporation, and Moody's all rate insurance companies after analyzing their financial records.

Ask for a summary of each policy's benefits for an outline of coverage. Good Advisors and good insurance companies want you to know what you are buying. Don't be afraid to ask your insurance agent to explain anything that is unclear. If you are not satisfied with an agent's answers, ask for someone to contact in the company itself.

*And bear in mind:* Even after you buy a policy, if you find that it doesn't meet your needs, you generally have 10 to 30 days (this varies by state) to return the policy and get your money back.

This article prepared by AHIA (American Health Insurance Association) ©2006

Brought to you By Financial Security Specialists

Visit [www.financialsecurityspecialists.com](http://www.financialsecurityspecialists.com)

Or call 808-625-3782 for an appointment or



## Disability Policy Checklist

	Policy A	Policy B
<i>How is disability defined?</i>		
inability to perform your own job?		
inability to perform any job?		
<i>Does the policy cover:</i>		
accidents?		
illness?		
<i>Are benefits available:</i>		
for total disability?		
for partial disability?		
only after total disability?		
<i>Are full benefits paid, whether or not you are able to work for loss of:</i>		
sight?		
speech?		
hearing?		
use of limbs?		
<i>The maximum benefit will replace what percentage of income:</i>		
<i>Is the policy non-cancelable, guaranteed renewable, or conditionally renewable?</i>		
<i>How long must I be disabled before premiums are waived?</i>		
<i>Is there an option to buy additional coverage, without evidence of insurability, at a later date?</i>		
<i>Does the policy offer an inflation adjustment feature: If so:</i>		
what is the rate of inflation?		
is there a maximum?		