Disability Insurance: You Can't Go Home Without It

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How many of you sell Disability Insurance? Perhaps, more important, how many of you don't sell it? Some of the most common reasons are:

- It's too expensive,
- Too complicated or there are too many definitions,
- Takes too long to underwrite,
- Everyone has some sort of coverage already.

I'd ask that you keep these reasons in mind. For now, however, I would like to discuss four things with you, beginning with:

Conviction

You can't go home without it! We are all in the risk assumption business. We build relationships with our clients, educate and advise them to ultimately fulfill their needs – that's planning. We help them to secure, manage and control their financial well-being. But in order to enable clients to plan for their future, you have to have your own plan formulated. What goals have you set for yourself? How are you going to achieve them? What measures have you taken to protect yourself and your practice from circumstances beyond your control? We take it for granted that we will always be as healthy as we are today. Ask yourself first, "How can I protect myself and my business if I'm diagnosed with a critical illness?"

Who here is worth $1M? If you think you're worth it, do you have a life insurance policy in that amount? Do you have a disability policy that would secure your income should you become disabled? Remember that during your working years, your earning potential will easily exceed $1M. You can't go home without it. If you do not believe strongly enough on the merits of the coverage to warrant having your own policy, then, you can't sell it!

Responsibility

As licensed insurance agents, we all have what is called in law, a "fiduciary responsibility". Insurance is like a 3-legged stool – life insurance, in the event that the client dies too soon, retirement protection, in the event they live too long, and disability insurance, in the

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event they become disabled. If one of the legs is missing, and the client needs to sit down, he's going to fall – that's clearly our fault!

It seems inconceivable that with only 4% of all mortgage foreclosures as a result of the death of a major breadwinner and 48% as a result of the disability of the major breadwinner, we still try to avoid talking about this problem, much less its solution!

Why do clients listen more carefully when we talk about "Income replacement"? They listen because as humans, we are more attuned to our selfish needs. In order to buy life insurance, you have to love someone (because ultimately you're dead when the claim cheque is delivered!). However, to buy disability insurance, you have to love yourself and your lifestyle! Today, we are all dependent on our income for lifestyle. As insurance agents, having careers that are commission driven, using our cars often, coping with stress, are we not "prime candidates"? If you don't own it, you can't sell it!

Discuss the Need

Figures don't sell. With Disability Insurance, you have to discuss the need. A disability affects everyone in the family. If the cash flow is not available, then not only are the luxuries curtailed, but sometimes the necessities. In homes where disability strikes, 9 out of 10 marriages fail – not because the people don't love each other, but because of the stress involved in dealing with a disability, the loss of dignity, self-respect, etc.

It comes down to basics: How much money will you need in the event you become injured or ill? Where is the money going to come from? Use the chart to find the client's age and gross income, now go through it with the client: Assuming "Joe" is 35 and currently earning $5000 per month. Between now and his age of 65, he stands to earn $8,000,000. Joe, your assets (your house, your car, your boat,) are worth about $300,000 and you're paying about $3000 per year to insure them. Your most valuable asset is your ability to get up in the morning to earn a living. What measures have you taken to protect the value of your earning power ?

Age	$3,000	$4,000	$5,000
35	$2,391,799	$3,986,331	$7,972,662
40	$1,718,176	$2,863,626	$5,727,252
45	$1,190,374	$1,983,957	$3,967,914

Simplify this for your client … the premium (assuming it is $200/month) is NOT the problem!

$7,972,662

$200

Discuss the Objections

We now have to prepare ourselves to address the client's objections.

1) "I can use my savings"
Do you realize that if you saved 10% of your annual income for 10 years, 6 months of disability would deplete your savings?

2) "I could liquidate my assets"
Which asset would you sell first? Don't you think that you'll be obligated to settle for "fire sale" prices if people know you have to liquidate?

3) "I can borrow the money"
I don't believe I know of a banker who will jump at the opportunity of loaning money to someone who is unable to work! Then again, there's always family, but in borrowing money from a parent, do you not also relinquish control of your finances to that person?

4) "My spouse can work"
Does she work now? Will she be able to get back into the work force and earn the same amount of money you are currently making? If she's already working and making the same or even more than you, remember that she is also responsible for the family's needs, she is a wife, a mother and will also have to nurse her spouse. There's a cycle of stress, anger and guilt that manifests itself during total disability.

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You now know that you can't go home without it, so to understand what is available, you need to decipher a contract. It's all about choice. An individual policy, a group or employee benefit plan, an association plan – what constitutes the difference? There are four essential factors when considering Disability Insurance. The first is the definition of disability.

1) Definition of Disability – there are three distinct definitions

i) Own Occupation/Dual Definition – this is the best available definition of coverage and states that: "if you cannot perform the duties of your own occupation due to an injury or an illness, and you're under the care of a physician" you are eligible to claim.

ii) Regular Occupation Definition – this definition only differs from the above with the addition of two words …"not working". So as long as you cannot perform the duties of your own occupation and you are "not working" or "gainfully employed", you can receive policy benefits.

Let's assume your client is a neuro-surgeon and develops arthritis in his hands, which renders him incapable of performing surgery. However, due to his level of expertise, he can teach neurology at the university and earn a similar income. With an Own Occupation/Dual Definition policy, he would receive benefits from the insurer as well as his teaching income. However, should the policy contain a Regular Occupation definition, he would not be able to claim his benefits.

iii) Any Occupation Definition – this is by far the worst definition available. It stipulates that: "if cannot perform the duties of any occupation due to an injury or an illness, you're under the care of a physician and you're not working" you are eligible to claim. What constitutes "any occupation"? Where there is any element of ambiguity, there exists the potential that a claim will be declined – unlike life insurance, at time of claim the policyholder is alive, and if the claim is declined, we are the ones they blame!

The second factor is the definitions of partial and residual disability. These are often confused, but are in fact quite simple – partial refers to time whereas residual, refers to money. If an individual can only work part-time, due to an injury or an illness, the definition of "partial" would pay him part, usually 50% of their benefit. However, if that same person is self-employed and would drag him/herself into work, put in a full day but could only generate a percentage of his/her income, thereby suffering a financial loss, then the "residual" wordings would pay the differential of lost income.

The third factor comprises the contract guarantees. This is what differentiates a good individual contract from an association plan or an employee benefit plan. What is known as a non-cancellable plan in Canada, or in other countries referred to as a guaranteed renewable plan, is a unilateral plan between the insurer and the policyholder whereby the insurance company cannot change, modify or cancel the contract as long as the policyholder continues to pay premiums. For the consumer, it emphasizes the importance of control. They have the control of their policy and NOT the insurance company! A group plan, employee benefit plan or association plan can be changed by the insurance company based on the claims experience of that group, but a good quality individual policy cannot be changed.

The fourth and last factor is the exclusions. Any quality contract will have only 3 or 4 exclusions: 1) Acts of war and riot; 2) periods of incarceration 3) normal pregnancy and 4) for the first 6 months of the contract, the policy will NOT pay for donor transplant operations. When looking at inferior policies, you'll often find pages of exclusions!

An association plan or an employee benefit plan seems to be far less costly, but ultimately, you get what you pay for. For a business owner, the key issues revolve around reverse discrimination, lower income replacement ratios, and control. It is important to know that association plans are often age-banded and the initial premiums increase in term increments. The premiums are also based on the claims experience of the association. In

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Canada, we have seen increases in excess of 100% to the bar association plan as well as to the dentists' plan. Dissect the plans.

When dealing with a business owner who has an employee benefit plan in place, look at the limits of the extended health benefit. They often stipulate that the group will pay 60% or 66 2/3% to a maximum dollar amount. Now look at the earnings and the individual's maximum eligibility amount. Use the following as an example:

Assume the group pays 60% to a maximum of $3000 of monthly benefit.

President	earns $10,000/month	or $120,000/annum
Vice-President	earns $ 6,666/month	or $ 80,000/annum
Manager	earns $ 3,333/month	or $ 40,000/annum
Clerical Assistant	earns $ 1,666/month	or $ 20,000/annum

Should any of them become ill or injured, look at the effects of the group plan on each individual:

President	$3,000	or 30% replacement ratio
Vice-President	$3,000	or 45% replacement ratio
Manager	$2,000	or 60% replacement ratio
Clerical Assistant	$1,000	or 60% replacement ratio

The key people in this business are experiencing reverse discrimination. Because they are earning a larger amount, they are being penalized by the limits of their current plan. There are solutions:

1) Exclude the key persons from the group and provide them each with individual coverage (this is done to extend all of the advantages of individual coverage to the executive group or specific key employees);

2) Group Offset – a duplicate individual policy is purchased to supplement the existing group insurance. Because the individual policy is "overlapping" the group coverage, it is issued with a special amendment that ensures that combined benefits paid under both the individual and the group plans do not exceed individual issue limits. Typically the carrier will extend a 5-10% premium discount.

3) Top-Up their existing group plan with a layer of individual coverage to maximize their over-all benefit.

The last of these solutions takes into account that the definitions within employee benefit plans cover "own occupation" for the first two years and changes to an "any occupation" clause thereafter. The solution will therefore top-up the benefit with a smaller amount for the initial part of the contract and will then add a secondary layer of coverage after a 2-year elimination period. A considerable advantage is that we don't have to worry about non-insurability with the Group Top-Up approach. An employee that is declined for the additional coverage still has the base Group LTD coverage in place. This may also be an opportunity to present Critical Illness coverage as an alternate solution. As the underwriting for CI insurance is different than that for DI, individuals who may be declined disability insurance, may certainly qualify for Critical Illness coverage. Again, it's all about keeping the presentation as simple as possible for the client. Using a modification of Burt Meisel's JOB A/JOB B, you can ask the following:

JOB CHOICES

Which Job Would You Prefer?

JOB A
$100,000 salary if you CAN Work
$0 if you CAN'T Work
JOB B
$97,000 if you CAN Work
$4,500 per month if you CAN'T Work

and then wait for the response – usually, the first one to speak, loses!

How do we make these plans truly cost-effective for the business owner? By implementing what is often known as an Income Loss Replacement Plan, the business owner can pay for these contracts with pre-tax dollars. This means that as opposed to having the policies personally owned (using after-tax dollars), the corporation will be the owner of the contract, thereby making the plan tax-deductible as a business expense. Depending on your country

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of residence, there are rules of plan implementation. In Canada, it follows the Income Tax Bulletin 428 (IT-428) and requires that a Board Resolution be set up, that two or more individuals be covered often excluding the business owner's spouse (should there be a key employee who is deemed better suited to receive benefits). Some simple rules of thumb that must be followed to correctly establish an ILRP:

The employer is the owner of the individual disability contract;

- The premiums are paid by the employer and are deductible as a business expense;
- The premiums paid by the employer are not taxable benefits to the employees;
- The disability benefits under the policy will be paid directly to the employee;
- Any disability benefits received by the employee while a member of the plan will be taxable.

Since the benefits under an ILRP will typically be fully taxable to the disabled employee, the insurance company will offer increased benefit limits to offset the tax liability. This automatically results in a larger case for the advisor. (If the employee terminates employment and acquires the employer's interest in the disability policy, the insurer will often reserve the right to adjust downward the benefit amount to avoid over-insuring the employee).

A "premium refund" or "return of premium" rider can be added to disability policies, including an Income Loss Replacement Plan, and is offered by only a handful of DI carriers. For an additional premium, the policyholder is entitled to a refund of premiums if no significant claims are made during a specified return period (i.e. if claims paid are 20% or less of premiums paid during an eight year return period). The amount of the refund depends on the rider chosen, varying from 50% to 75% in today's market. The refund can, on an after-tax basis, provide a greater rate of return than traditional savings vehicles. "Mr. Client, you'll receive a cheque whether or not you become disabled!"

Plan Design and Premium Cost

Case Study: Consider the example of a male, non-smoker, age 40 with an annual income of $100,000. The product being illustrated is a non-cancelable contract assuming the insured qualifies as a 4A classification of risk, with a 50% refund. The structure would be as follows:

A Taxable Monthly Benefit:	$6,400
Elimination Period:	90 Days
Benefit Period:	To age 65
Annual Premium	
Policy (paid by employer):	$2,056.44
Premium Refund Rider:	$ 822.59
Total:	$2,879.03
Refund to the Employer:	$11,516

(representing approximately 14.5% return on investment)

Whether the policy is individually owned or corporately owned, it is beneficial for its owner as it provides quality coverage as well as a low risk high return investment. This can also lead to Split Dollar Premium Refund arrangements whereby the employer owns the individual policy under the ILRP and the employee owns the rider. For all parties, this creates an opportunity for premium savings. For the advisor, it provides for yet another method to invest the lump-sum amount for his client.

You Can't Go Home Without It. Understand the importance of Disability Insurance. The underwriting of these cases is often more stringent than that of a life insurance case. Not only are you privileged to your client's medical information, but to their personal and corporate tax returns as these are required by the insurer– what better way to build fences around your clients! This also gives you linked opportunities – the ability to discuss Critical Illness coverage, Disability Overhead Expense coverage, the funding of Buy-Sell Agreements, Long-Term care coverage and, of course, life insurance.

A comprehensive disability plan will ensure an income is provided when you are disabled, that adequate business overhead expense coverage is in place so that during

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your disability, personal income dollars do not have to be utilized to pay overhead costs. It will put back your investment and savings dollars, pay out your deferred taxes and leave you with a growing equity base to protect your retirement, thereby providing you with a decent standard of living.

Create an objective using your own conviction, emotion (as this truly is a selfish purchase), and logic. You cannot provide a service with confidence unless you believe strongly enough in it to have your own personal plan – get your own financial house in order.

MDRT has always promoted divisionalization. Surround yourself with a team of experts – specialists in estate planning, disability insurance, employee benefits, long term care, taxation … We cannot all be great at everything, but we can certainly provide the best for our clients by working with others who have an area of expertise different from our own. When you tell your client you're introducing them to someone who is an expert in a specific field, they'll look at you in a different light – as a professional who has his own practice of advisors. You'll also find that the sales which are generated by each "guru", are often far larger than those you would have anticipated – don't forget, 50% of something is better than 100% of nothing. By becoming a specialist, you'll be recognized among your peers and that makes you referable – that's how I made it here. You see, I'm a lousy prospector, but I have the opportunity of working with a team of advisors who hate disability insurance!

I would hope that you walk out of this session convinced that You Can't Go Home Without It. Looking after your needs will give you the insight to look after those of your clients. I hope that this discussion will make you more effective when dealing with disability insurance, and though every case will be different, that I have provided you with a template for executing a strategy of success for you.