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LONG TERM DISABILITY AND YOU

BY JUSTIN Y C LEE

Background

Steven Tan suffered end-stage renal failure at age 44. His company eventually had to medically board him out after 12 months and terminated his employment as an accountant with the firm. At age 45, with impaired health and the need for regular dialysis treatment, Steven found it difficult to find a similar job paying him at a similar level before his disability. Any kind of permanent employment was difficult, given his poor health.

However, Steven was "fortunate" as he had bought disability income insurance to hedge against the risk of losing his income should he lose his job because of illness or accident.

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It's an indemnity cover

Disability income insurance is also known as long-term disability (LTD) insurance or permanent health insurance. LTD insurance helped ensure that Steven received a full, regular monthly income stream for as long as he could not work as an accountant, or until Steven turns age 60, as provided for in the policy. It helped to safeguard the upkeep of his family and eased considerably the anxieties and worries of losing not just his job, but also the means of earning a living. That meant a lot to Steven as the long-term insurance benefit payments helped to preserve his dignity of being able to provide for his family on a long-term basis, even while he was forced out of work and recuperating from his illness. The full, regular monthly income stream from the policy was non-taxable. It preserved his savings and saved him from having to go into debt, or having to turn to friends and relatives or the government for financial assistance. It helped to replace a significant portion of Steven's regular monthly income that he lost when he became totally disabled and unable to work in his own occupation (as an accountant), as a result of his illness. It also covered him in the event his total disability was caused by an accident. The key provision under the policy was whether Steven was totally disabled and unable to perform the duties of an accountant in his firm. There was no need for Steven to be totally and permanently disabled. When this key provision was satisfied, the insurance company admitted the claim and indemnified Steven against the loss of his monthly income.

Critical Differences in Definition

Steven also had whole of life, endowment and term life insurance coverage, with total and permanent disability benefits that he erroneously thought could do the same job as disability income insurance. Fortunately for him, it was pointed out to him that it was not the same after a review of all the policies concerned. The review of the terms of total and permanent disability cover was clear – it required Steven to be totally and permanently disabled and he must not be working in any occupation, ever. Such a restrictive definition (nicknamed "vegetable definition" in insurance circles) under total and permanent disability cover offered Steven very limited protection because it made the possibility of a benefit claim remote as compared to the "own occupation" definition under long-term disability insurance, which was much more generous.

An incentive to return to work

To encourage Steven to return to employment (either part-time or full-time), the policy provided for a partial disability monthly benefit that would be paid in addition to future employment income, provided the future employment income is not more that the insured regular monthly benefits. Partial disability monthly benefits are also not taxable and will cease when future employment income equals the insured monthly benefits. While in receipt of full or partial benefits, the premium due on Steven's long-term disability policy was waived. He would be called upon to resume payment of premiums on the policy only after he ceases to receive his regular (full or partial) monthly benefit payments. As provided for in the policy, the insurance company guaranteed to continue coverage under the plan in spite of Steven's ill health and even after he recovers.

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In selecting an appropriate level of benefit that matched the premium that Steven was prepared to pay, he took into account how many months of salary his employer was prepared to pay if he was ill and could not continue to work. This information was important since the duration and frequency of claims are factors that go into pricing the product premium. Generally the sooner the monthly benefits are payable, the higher the premium outlay. The monthly premium outlay would be lower if Steven's employer was prepared to pay him 6 months as compared to 3 months. Further, as this was an indemnity cover, no benefits would be paid while Steven was in receipt of a salary from his company.

As Steven was only entitled to 3 months' full pay and would be on no-pay leave after 3 months, the waiting period selected was 3 months under the policy. During this waiting period of 3 months, no regular monthly benefit would be paid to Steven. It commenced only after the third month of disability.

Benefits are inflation-protected

Steven also ensured that the regular monthly benefits were protected against inflation by adding a rider under the plan. With this rider, Steven was guaranteed that his regular monthly benefit would increase at the rate of inflation which was assumed at 3% a year. This was important to guarantee that the real purchasing power of the insured benefits did not get eroded by inflation. The best part about all these benefits was that Steven got to spend the money anyway he desired, as there were no restrictions on the use of the benefits paid to him. The insurance company had also included a small death benefit component in the plan to be paid if Steven should die on, or before his retirement age.

Steven used part of the money received to travel abroad for medical treatment and recuperation, but was mindful that the policy provided for termination of cover and benefit if he was away from Singapore for more that 180 days. He arranged his trips to ensure that he did not breach this provision of the policy.

Preferred risk

One of the crucial underwriting concerns involves the type of occupation of the insured and a measurement of the likelihood of the insured person being unable to continue working, due to illness or accident. Based on occupation, it is obvious that there are some occupations that are not acceptable while others are preferred. Generally white-collar occupations are preferred risks over blue-collar occupations.

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