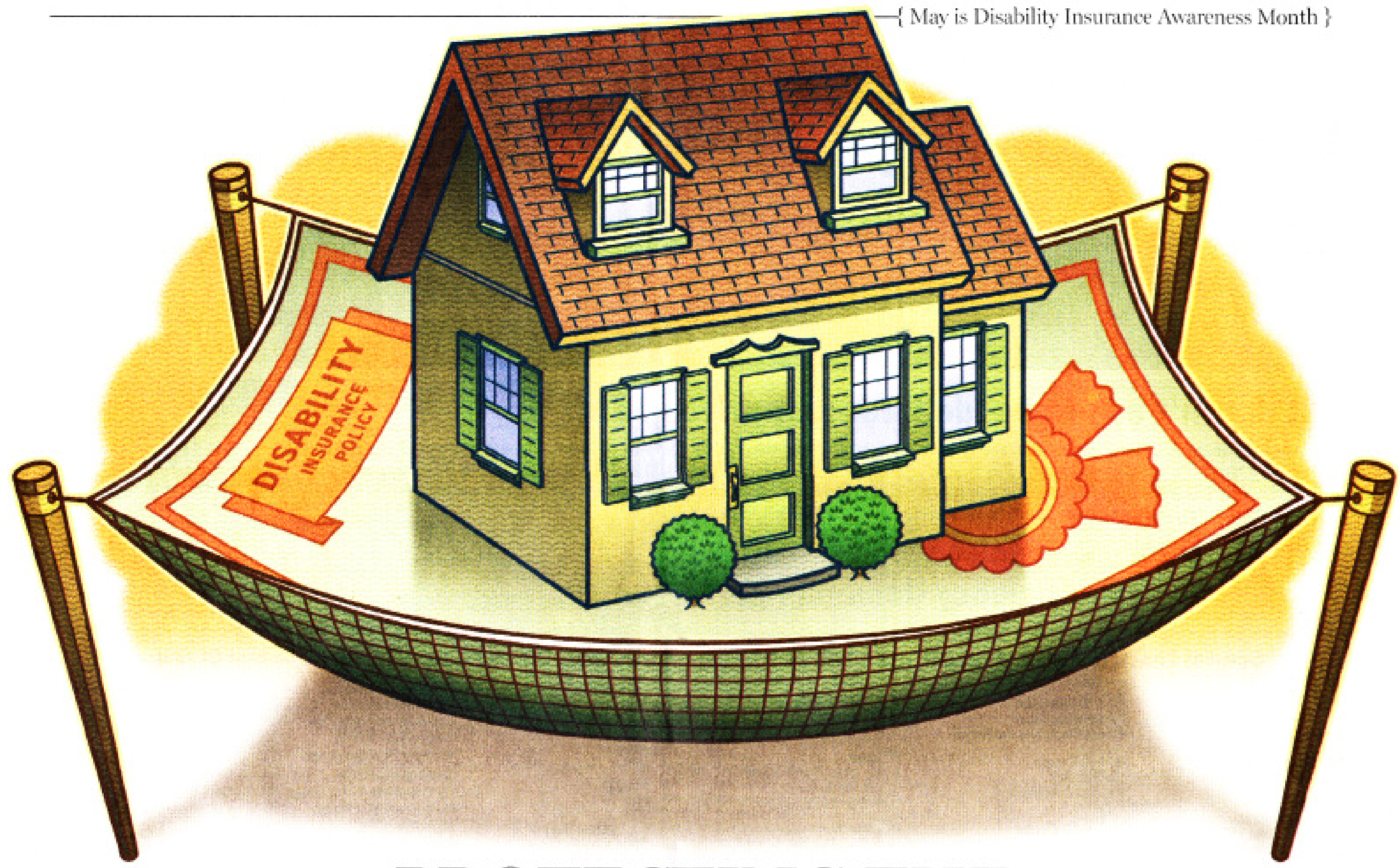
Special Advertising Section

Disability Insurance

{ May is Disability Insurance Awareness Month }



PROTECTING THE *American Dream*

For financial security, disability insurance tops the list

By Russ Banham

The private agony of losing a steady paycheck and then being unable to come up with the money for the monthly mortgage befell many wage earners in the last few years. The emotional toll in such cases was profound — individual self-esteem eroding as quickly as bank accounts depleted. Yet, job loss is not always the primary reason for losing a home to foreclosure.

A 2008 study by Harvard Law School indicates that 49 percent of home foreclosures are caused by a medical reason, such as injury or illness. According to the authors, who studied the causes of home foreclosures in four U.S. states, if the statistical patterns held nationwide, nearly 1.5 million Americans currently are in jeopardy of losing their homes because of a medical crisis.

It's not necessarily the health care costs of treating the disabling condition that undermines the ability to pay the mortgage, although this is part of the problem. The underlying dilemma, the study reveals, is that the disability gives rise to an inability to work, which generates financial stress in paying the bills, thereby causing monetary difficulties in holding onto one's home.

For some people, even a relatively short-term disability could make it difficult to pay the bills. Those without insurance run the risk of bankruptcy, home foreclosure, eviction and ruined credit down the road. Forced to sell a home in a down market, families can incur financial losses that may never be recouped.

"Every wage earner has a chance of becoming disabled and the impact is often catastrophic," says Barry Lundquist, president of the nonprofit Council for Disability Awareness (CDA), "yet most workers have not planned for the risk of a disability and most have not protected their incomes or the security of their homes."

Risk Underestimated

Despite distressing statistics, few Americans are cognizant of the risk and financial import of disability. Sixty percent of working Americans believe they have a 2 percent or lower chance of being disabled and unable to work three or more months during their careers, according to a study to be released in June by the Portland, Maine-based CDA. The actual percentage of Americans entering the work force today who will become disabled before they retire, Social Security Administration (SSA) statistics reveal, is as high as 30 percent.

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>
> — BOB RISK

This disparity between expectation and fact is unsettling, says former Oklahoma Governor Frank Keating, president and CEO of the American Council of Life Insurance (ACLI), a Washington, D.C.-based trade group. "If I said that three in ten workers will be hit by lightning so they better get life insurance, people would buy it instantly. Yet when it comes to insurance to absorb the financial brunt of a disability, few heed the risk," Keating says.

He's right: Nearly 100 million members of America's workforce lack private disability insurance. That number comprises affluent executives along with middle management and the rank and file. Despite what some think, wealthier individuals are far from immune to the financial impact of a disabling medical condition. "People have expenses to pay regardless of income level, and many saw their assets fall in value during the recession," says Keating. "Everyone has a need to protect their income in the event of a disability."

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>
> — FRANK KEATING

Perfect Storm

How prevalent is disability? SSA statistics indicate an astonishing 21.3 percent rise from 2008 to 2009 in disability insurance claims received by the federal agency, from 2,320,396 claims in 2008 to 2,816,244 claims in 2009. These figures exclude disabled workers already covered by private insurance. Factors behind the sharp increase likely include the dour economy, the persistently high unemployment rate and the aging of the working population.

The Harvard Law School study arrives at a similar conclusion, especially in terms of home foreclosure risks. The survey results indicated that respondents in many cases were beleaguered by a "perfect storm," the authors reported. "A few thousand dollars of medical bills, a few weeks of missed work, and perhaps a divorce or rising interest rate … all combined to push them over the edge into foreclosure," the study stated.

Personal bankruptcies are another dire financial consequence of medical disability — almost 350,000 personal bankruptcies each year are caused by unexpected illnesses and injuries. A Cambridge Hospital/Harvard Medical Study in 2009 backs this up, finding that 62.1 percent of all bankruptcies have a medical cause. Most medical debtors were well educated and middle class, and three-quarters of them had health insurance, the study indicated.

While the various studies underscore the risks of not protecting personal income through insurance, getting this message across has been problematic. "Many people fail to put two and two together — that the threat of disability is very real and financially debilitating. It doesn't just happen to others, but it can happen to you, too," says Bob Risk, vice president of sales at Lincoln Financial Group, a Radnor, Pa.-based financial services company.

Maybe You, Not Me

Risk makes a fine point. CDA's finding that most people rate their chances of a disability during their working careers as 2 in 100, or 2 percent, starkly contrasts with another survey result: 61 percent of respondents said they personally knew someone who'd been disabled and unable to work for three or more months. As Keating sees it, "Americans tend to be optimists about their own chances of a disability, yet the facts argue otherwise."

Lundquist shares this view: "People think a disability will happen to 'the other guy.' It's like the smoker who knows the medical risks, but figures that 'Uncle Joe lived to be 92 and he smoked, so chances are I'll live just as long.' You're gambling with your future."

Even if you think you'll never be disabled, the disability of a family member can be equally as devastating. It's not just breadwinners unable to work that wreak financial havoc. Spouses that bring in secondary incomes, should they become ill or injured, can make a swift, scathing impact on a household's financial health. When you add up lost income, possible out-of-pocket medical expenses, prolonged nursing and child care or other related costs, it isn't hard to see how disability can permanently alter a family's quality-of-life, within a relatively short period of time.

Many people also live under the assumption they could go on for quite some time before

Illustrations by Peter Hoey and Maria Hoey savings are depleted. But in reality, how long would most of us survive financially without the income provided by our jobs? Only 35 percent of study respondents said they could continue to pay living expenses and bills for a year or more if they lost their employment income. This doesn't bode well for many Americans; according to a different study, the average long-term disability absence lasts two-and-a-half years.

There are other "fingers-crossed" expectations. For example, many individuals mistakenly believe that if they suffer a disability, government-provided Social Security insurance will absorb a good part of the financial brunt. Not only is this benefit difficult to qualify for, the monthly payments are not nearly enough to satisfy aggregate financial obligations, much less the mortgage. "The average monthly check is $1,062," says Keating. "That's not a lot to live on these days."

Currently, only 3 percent of Social Security disability insurance payments exceed $2,000 a month — assuming one can obtain the benefit. To qualify for Social Security disability insurance, a person must be disabled for five full calendar months, and the disability must be expected to last at least one year or otherwise end in death. A disabled individual also must be unemployable at any occupation and not just his or her previous line of work. Consequently, a startling 65 percent of applicants for Social Security disability insurance are denied the benefit initially and those who finally do receive it often must wait several months before the checks arrive.

Pennies for Protection

Obviously, there is a need for more of us to consider protecting what we earn through disability income protection insurance. Many private insurers offer two types of disability income policies — short-term disability insurance that pays a percentage of a disabled worker's salary for 13 to 52 weeks after the so-called "elimination" or waiting period (typically 90 to 180 days); and long-term disability insurance that essentially extends the short-term policy to desired durations.

Most individual policies are either noncancellable or guaranteed renewable. With a noncancellable policy, premiums can never be increased. Under a guaranteed renewable policy, premiums cannot be increased based on an individual circumstance, but they can be raised for an entire class of policyholders.

A guaranteed renewable policy may define how a class is determined — for example, all policyholders in a state who own the same type of policy might constitute one class. It is important to know how classes are defined and the circumstances under which premiums can be raised.

Industry experts are quick to point out that the cost — if provided by employers on a group insurance basis — is about the price of a cup of coffee a day. The premium for many group policies is less than $50 a month, in some cases as low as $35 a month, depending on the insured group of employees, the insurance carrier providing coverage, the state one lives in and other factors. There is a fly in the ointment, however. Group policies, both short-term and long-term, typically pay only 50 percent to 66.66 percent of the employee's salary. For some people, the provided amount may be adequate to pay monthly bills or augment personal savings and investments.

For others, there is supplemental disability income protection insurance, which raises the salary component covered by traditional group policies. Supplemental insurance is non-taxable to the employee, whereas disability insurance that is paid for by employers is taxable to the employee, post-disability. However, several factors affect the price of supplemental disability insurance, including the policy applicant's age, health and the benefit amount.

Not everyone can purchase inexpensive group insurance, of course. Some companies simply don't offer the benefit, and many people are self-employed and unable to acquire it. In such cases, individual disability income protection insurance is an alternative. The premiums typically average 1-2 percent of the worker's annual salary, compared to about half a percent in a group insurance context, Lundquist estimates. Despite the higher cost, the insurance "is still a prudent purchase," he says. "Most people get at least a 2 percent raise a year in their salary. It makes financial sense to divert that income into protecting your overall income for the rest of your life."

In recent years, the insurance industry has unveiled several novel long-term disability insurance coverage add-ons, such as return-to-work and comprehensive rehabilitation provisions that defray the cost of training and modifications of the work environment. "Our goal is to help people get back to work at 100 percent of their previous salary, and these provisions assist disabled employees to do just that," says Risk from Lincoln Financial, which offers the provisions in its policies.

Another coverage feature in some policies is a cost-of-living adjustment (COLA) that increases monthly disability payments to correspond with annual cost-of-living increases, for a nominal additional premium.

Peace of Mind

In this anxious era of high unemployment, rising costs and the alarming growth in home foreclosures, it is soothing to have access to disability income protection insurance. Pricing in the competitive disability insurance market has been stable both during and after the recent recession.

"Pricing ebbs and flows depending on the particular employee group, but for the most part has been flat for seven to eight years," says Risk. "When you compare the cost to something like medical insurance, which everyone agrees is necessary to financial well-being, disability insurance is so incredibly inexpensive."

He adds, "Not only will disability income protection help pay the mortgage and other bills to relieve the financial stress of a home foreclosure or personal bankruptcy, it helps buyers maintain the lifestyle their families are used to."

Russ Banham has written about insurance, risk management and personal investing for CFO, U.S. News and World Report *and* Forbes. *His most recent book is* The Fight for Fairfax.

MEDICAL CONCERNS MAY LEAD TO FORECLOSURE

Seven in 10 homeowners (69%) in foreclosure had significant medical distress in the two years preceding their foreclosures.

Self-reported medical cause

50%

Unreimbursed medical bills > $2,000

37%

Lost 2+ weeks of work due to work illness/injury

30%

Used home equity to pay medical bills

13%

Currently unable to work due to medical issues

8%

Source: Robertson, Christopher T., Egelhof, Richard and Hoke, Michael, "Get Sick, Get Out: The Medical Causes of Home Mortgage Foreclosures" (August 18, 2008). Health Matrix: Journal of Law-Medicine, Vol. 18, No. 65, 2008.

Available at SSRN: http://ssrn.com/abstract=1416947