Income Protection – Disability

Protecting loved ones from financial hardship in the event of premature death of a primary income earner is usually a high priority for most Canadians. Unfortunately, while we may be concerned with protecting our surviving family members in the event of death, frequently we fail to consider the implications of losing our income earning capability in the event of disability. Therefore, ensuring that we have sufficient disability insurance coverage in place is important in providing us with peace of mind.

Disability insurance is in essence "income replacement" insurance. It is purchased as protection against the chance (risk) of losing earned income while disabled and not being able to meet expenses. The amount of insurance you qualify for depends entirely on how much income you earn; the benefit is usually capped at 70% of gross earnings. Ask yourself – Could you pay your bills if you were unable to work because of illness or accident?

Over two million Canadians of working age are disabled. The cause for disability isn't just physical injury. Among office workers, absences for nervous disorders – including stress-triggered conditions – have become the leading cause of disability in Canada today.[1]

Types of Disability Insurance

There are three types of disability insurance policies:

1. Individual

This type of insurance offers comprehensive long-term total Individual Disability Income Protection with a wide selection of optional benefits and features, all of which can add to the premium cost. Generally speaking, the more options one chooses the higher the premiums.

Some examples of optional benefits include:

- Income tax rider to pay your quarterly tax instalment.
- Retirement protector to continue providing monthly retirement savings to a non-registered account.
- Cost of living allowance (COLA) to protect the benefit amount from changes to the Consumer Price Index.

Various plans are available designed with a selection of benefits suitable for a wide variety of clients such as business owners, employees, blue-collar workers, farmers and the middle income market.

2. Buy/Sell Policy

The Disability Buy/Sell Plan is a conditionally renewable business disability insurance policy which acts as a funding mechanism for a buy/sell agreement. A **conditionally** renewable policy provides coverage for someone in a fixed profession (Lawyer, Doctor, etc.). If this person switches professions, the policy could be discontinued or the premiums may change. The policy provides a lump-sum benefit in the event that one of the principals of the business becomes permanently totally disabled.

The Buy/Sell Agreement and Disability Policy must have the same timelines. For example, if the Buy/Sell agreement specifies that after 12 months of disability the clause kicks in and buys out the partner the Disability Policy must pay out at the same time.

The Disability Buy/Sell Plan appeals to business partners or shareholders of small privately owned businesses, and is usually coordinated with a Life Insurance Buy/Sell Policy.

3. Business Overhead Expense

This type of insurance is designed for principals of closely held businesses or practices and owners of small businesses. It is an expense reimbursement policy that covers those fixed monthly business overhead expenses required to keep the business viable until the return of the owner, after a period of disability. This allows the business operations to continue until the insured either returns to work or makes a decision regarding the future of the business.

These features, plus the fact that premiums are tax deductible as a business expense, make the Business Overhead Expense policy a key component of any business owner's financial security plan. It ensures that business continues when a disability occurs.

Disability Insurance Features & Options

Basic Features:

Total Disability Benefit
Once the elimination period is satisfied, an insured who is and remains totally disabled will receive a monthly benefit up to the maximum benefit period. Benefits paid are subject to the limitations and exclusions set out in the policy.

Return to Work Assistance Benefit
Starting from the first day of injury or illness, the insurer may provide some assistance in returning the insured to work or enhancing his or her ability to work. Assistance may include such services as: co-ordination of physical rehabilitation services; financial and business planning; vocational evaluation; education; and job placement for a new occupation.

Waiver of Premium
After the insured has been disabled for 90 days the insurer will waive premiums that come due while the insured is disabled. Premiums paid during those first 90 days will generally be refunded.

Presumptive Total Disability
If the insured irrecoverably loses sight, speech, hearing or use of two limbs, the insured will be considered totally disabled and will be paid total disability benefits for the stated maximum benefit period.

Accumulation of Days
Periods of disability from the same or related causes, separated by 12 months or less, will be accumulated and considered continuous in order to satisfy the elimination period.

Recurrent Disability
After a period of disability ends and the insured becomes disabled again from the same or related causes within 12 months, it will be considered a continuation of the previous disability.

Basic Options:

Waiting Period
The waiting period or elimination period – usually 30, 60, 90 or 120 days - represents the number of days the insured must wait before receiving a payment. The shorter the wait, the higher the premium since the insurance provider assumes a higher risk of making payments. The choice is sometimes dependent on whether or not one has sufficient cash reserves for day to day expenses at the start of the disability until the first disability payment is received. Generally, 90 days is the standard waiting period for Individual Disability plans.

Benefit Period
The benefit period (BP) could be 2 years, 5 years or to age 65. The BP ends at age 65 in most cases as this is considered the standard retirement age, therefore if the individual was not disabled they would be retiring at this point and would no longer be eligible for this income stream. In some cases the BP can become yearly renewable to age 70. The average length of disabilities is about 2.5 years at younger ages and nearly five years at older ages. Generally, the longer the potential benefit period, the higher the premium.

Riders:

There are number special provisions or extras known as "riders" that, for a price, can be added to a disability policy.

Own Occupation
The Own Occupation Rider is only available to certain occupations such as lawyers, doctors and architects and allows the insured to work in another occupation while they are totally disabled in their regular occupation and continue to receive disability benefits.

Professionals often have a significant investment in their occupation, including years of training and acquired experience. However, many feel that although they might be able to find alternative employment during a total disability, they would experience a drastic reduction in income. The Own Occupation Rider modifies the definition of total disability under the basic policy so that the insured is considered to be totally disabled even if he or she engages in any other gainful occupation.

Residual Disability
The benefits provided by this rider can contribute to financial security by helping to close the gap between earnings before the onset of the disability and earnings while either partially or residually disabled. If the insured

is not totally disabled, the Residual Disability Rider allows the choice between receiving the partial disability benefit if the insured suffers a loss of time or duties or the residual disability benefit if he or she suffers a loss of income.

Future Insurability Option

Often income rises over a person's working years and health may deteriorate. Although most people feel they fully insure themselves when they buy a disability insurance policy, they may find the original amount of disability insurance becomes insufficient as their careers progress and needs change. Unfortunately, these people may not qualify medically to buy additional coverage at a later date.

The Future Insurability Option Rider helps alleviate this problem by guaranteeing that additional coverage may be purchased on specified option dates, regardless of the person's state of health and requires only financial underwriting to guard against over-insurance.

Assessing Adequacy of Coverage

In order to determine whether or not you have adequate coverage, you first need to estimate what your daily living expenses would be if you were disabled. Then, you would have to calculate the sources of income available to you (e.g. group disability benefits, Canada Pension Plan (CPP) disability benefit) and include any other money that you could draw on (e.g. spousal income, investments). The difference would indicate whether or not you are adequately protected.

Unfortunately, most people have not taken the time to do the math and the common result is that when people become injured or disabled, they may need to:

- Dip into their retirement savings (e.g. registered or non-registered assets).
- Sell off assets (e.g. their home).
- Accept a significantly lower standard of living to manage the costs associated with a disability.

It should be noted that if an individual intends to have more than one disability plan, the benefits are integrated and capped at a percentage of normal earnings. In other words, you could not completely replace your lost income.

Government Disability Benefits

The major forms of government disability benefits are: Employment Insurance (EI), Canada/Quebec Pension Plan, Provincial Support and Workers Compensation. All have eligibility and benefit limitations.

EI Sickness Benefits

EI Sickness benefits may be paid to a person who is unable to work because of sickness, injury or quarantine. To be entitled to EI sickness benefits you must:

- Show that your regular weekly earnings have been decreased by more than 40%.
- Show that you have accumulated 600 insured hours in the last 52 weeks or since your last claim; this period is called the qualifying period.
- Provide a medical certificate indicating how long the sickness is expected to last.
- Not only prove that you are unable to work but would be otherwise available to work.
- Provide the required information/ documentation with your application (e.g. social insurance number, record of employment, banking information, etc.).

The basic benefit rate is 55% of your **average insured earnings** up to a **maximum** amount of $485 per week (2012). Your EI payment is taxable and if you work while on sickness benefits, the benefit will be reduced dollar for dollar. The benefit is payable for 15 weeks; however, you may receive up to 50 weeks if combined with regular EI benefits.

CPP Disability Benefit

The CPP disability benefit is a taxable monthly payment and is available to people who contributed recently to the Canada Pension Plan while they worked, and then became unable to work at **any job** on a regular basis because of a disability. There are also benefits for children if at least one parent qualifies for the CPP disability benefit. To qualify for a CPP disability benefit:

- You have to have earned an amount higher than $4,800 in 2011.
- You have to have made contributions in four of the last six years.
- The disability has to be **both** "severe" and "prolonged" (i.e. expected to last at least one year or result in death), and must prevent you from being able to work at **any job** on a regular basis.

The most money you can receive from the disability benefit each month is $1,185.50 (2012). Every January, there may be an increase to the CPP disability benefit to take into account any increase in the cost of living. Your benefit will stop if your condition improves to the point where you are able to work at any job on a regular basis, or you turn 65, or upon your death. CPP provides a benefit to all eligible contributors, even if they also receive disability income from other sources. However, these other payments may be adjusted if you are approved for a CPP disability benefit.

Provincial Disability Support

Benefits and rules may vary by province. The Ontario Disability Support Program (ODSP), for example, is designed to meet the unique needs of people with disabilities who are in financial need, or who want and are able to work and need support. The Income Support component of ODSP provides financial assistance to eligible people with disabilities. To be eligible for Income Support:

- You must be 18 or older,
- You must be financially eligible, and
- You must have a verified physical or mental impairment that is continuous or recurrent and is expected to last one year or more.
- The disability must make it difficult for you to care for yourself, participate in community life or to work
- You must be a resident of Ontario

If you meet the requirements, a package of forms must be completed (this includes a medical consent form) and you must also meet someone from the ODSP office to review your income and expenses. The benefit is tax free and is payable until age 65. The ODSP benefit amount can be reduced if you are receiving employment or other sources of income.

In addition to the monthly benefit, someone receiving ODSP benefits will receive a drug card entitling him or her to listed prescribed medications and a dental card entitling him or her to basic dental coverage. The rules and regulations to qualify for ODSP benefits are quite complex and the government's view is that it should be the payor of last resort.

Workers Compensation

Each province has its own form of Workers Compensation program in place that establishes minimum requirements for a safe working environment. In Ontario for example, the Workplace Safety & Insurance Board of Ontario (WSIB) has this responsibility.

To be eligible for WSIB insurance benefits, you must:

- Have a worker-employer relationship with an employer covered by the WSIB.
- Have an injury or illness directly related to your work.
- Promptly file a claim with the WSIB.
- Provide all relevant information requested by the WSIB to help in determining your benefits.
- Consent to the release of functional abilities information to your employer by the health care professional treating you (this information identifies the activities your illness or injury allows you to carry out safely, which helps your employer find safe and suitable work for you during your recovery).

Your workplace insurance entitles you to a range of benefits. The benefit most people are familiar with is the replacement of earnings you lose while disabled by workplace illness or injury (benefit for loss of earnings - LOE). The WSIB (Ontario) benefit payment is based on a percentage of the Average Industrial Wage (AIW) in Ontario; it is paid every two weeks and is adjusted for inflation each year. The benefit continues until you are no longer impaired by your work-related injury or illness, or until you no longer have a loss of earnings, or until you reach age 65.

If you are still impaired at age 65, LOE benefits stop but loss of retirement income benefits may apply.

Probability of disability before 65 that lasts 90 days or longer

Age	Male	Female
20	21%	31%
30	20%	29%
40	18%	25%
50	16%	18%
60	8%	8%

Based on 1985 Commissioners Individual Table A (for occupations involving no manual labour).[2]

Consider the following situation

Rene, a 42 year old district sales manager, has been married for 17 years to Ali and has two young children. He loves sports and plays arena football once a week.

Recently, a team-mate (Randy) sustained head injuries and it might take Randy months before returning to work.

During this time, it will be very difficult for Randy's family as he is the sole income provider.

Randy's group disability benefit will only cover 60% of his monthly income and it will be three months before the benefit starts. In the meantime, Randy's family will have to cover the mortgage and other monthly expenses such as food, utilities, and clothing. Discretionary spending will have to end, meaning that the kids' private piano lessons will have to stop. While Randy hopes to return to work quickly, the other alternative is for his spouse Sandy to go back to work. However, Sandy will need re-training.

Rene called his financial advisor to set up an appointment. Rene wanted to ensure that he and Ali have adequate disability coverage to protect their family income should one or both of them find themselves in a situation similar to Randy. Although Rene felt that his benefits through work would cover him in the event of a disability, he wanted to ensure that the financial impact to their lifestyle and future goals would not be negative.

Before the meeting, Rene's advisor sent a list of considerations for Rene and Ali to think through about long-term disability (LTD) coverage and their future plans:

1. Who are all the people that depend on you for financial support?
2. What will be your sources of income if you were to become disabled and how long would these sources of income continue? Do you have an emergency reserve in place?
3. If you were to become disabled and unable to work, would your spouse or common law partner be able to earn enough income to make up any shortfall?
4. What are the criteria to qualify for disability benefits at your employer or provider?
5. Does your coverage exclude or limit certain types of medical disorders, activities outside of work, or pre-existing conditions?
6. How much will your disability benefit pay? When do benefit payments begin and are they taxable?
7. What happens to your group disability coverage when you leave your job?
8. When do you expect to retire and how will your plans be impacted due to disability?

During the meeting, Rene's advisor reviewed his current group disability coverage. The quality of the group LTD coverage was good but only his $60,000 salary was protected; his estimated $12,000 in sales commissions was excluded. This meant that he would receive a non-taxable monthly benefit of $3,000, or 60% of his current monthly income. The benefit was non-taxable since Rene was paying the premiums. If Rene's employer had paid the premiums, the benefit would be taxable.

Rene realized that without additional coverage his family would struggle. With Ali working at home as a writer (self-employed), Ali did not have employer sponsored disability benefits. Rene's advisor recommended a few options to meet the family's needs:

1. Cost-effective disability insurance protection to complement Rene's group coverage.
2. Adding a rider to include partial disability benefits.
3. A basic income protection plan for Ali.

If Rene or Ali faces a disabling injury or illness, the additional insurance coverage will allow them to meet the following needs:

- Pay for necessary living expenses such as utilities, groceries and clothing.
- Make mortgage and car loan payments.
- Preserve their retirement savings.

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1. Statistics Canada, Participation and Activity Limitation Survey, 2001.
2. Globe & Mail, February 2003.

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