

Coping with Disability

Protecting your income & assets



Could you pay your bills if you were unable to work? The first insurance priority for many Canadians is often life insurance, but the adverse impact of losing your ability to earn income if you're injured or ill should not be overlooked. To ensure you are able to maintain your lifestyle and continue to support those who depend on you, it is important you make certain your income is protected as this is your most valuable asset.

Disability insurance (DI) is designed to protect your income. The purpose of DI is to provide an income stream while you are unable to work during an extended illness or injury. Protecting your income may involve disability insurance coverage in the form of an individual DI policy or perhaps group insurance.

For employees, the benefit amount is normally based on your base income. Other income types, such as a bonus, overtime, and profit sharing are often not included/insured. If your employer is paying the insurance premium then the disability benefit payment will be considered by the Canada Revenue Agency (CRA) as a taxable benefit. For self-employed people, who buy their own DI policies, the benefits are typically received tax-free. In calculating a disability benefit for a self-employed person, it is typically based on net after-expenses income.



Four Basic Types of Disability Insurance

1. Group coverage

Group insurance is commonly available to employees through their employer. According to the Canadian Life and Health Insurance Association's (CHLIA) 2016 publication of life and health insurance facts, 4.6 million Canadians have access to short-term disability insurance, and more than 10 million to long-term disability insurance through group plans offered by their employers.

Coverage is available as long as you are working for the employer. The policy costs are pooled for the group of employees, regardless of occupation. Premiums are generally lower than the premiums for an individual coverage policy, since coverage is not as comprehensive as personally owned DI. Claims are also pooled. Each claim on an employer's policy has the potential to increase costs for the entire group.

Group policy contracts are usually re-negotiated between the insurance company and the employer on an annual basis. Current year's claims and expenses are priced into the following year's premiums.

Most group plans have a "total" disability definition for paying a claim. This means the insured is unable to perform the important duties of his/her occupation as a result of an injury or illness. Benefits may not be payable if an employee can return to work part-time.

Benefits may not be payable if an employee can return to work part-time.

Group disability policies set a maximum benefit amount for all employees. The maximum benefit doesn't always reflect the incomes for higher-earning employees since most group plans do not include bonus income (or commission income) when calculating the benefit amount.

2. Individual coverage

Individual disability insurance involves long-term income protection. Premiums are often guaranteed for the life of the policy. The insurance company cannot cancel the

policy unless the applicable premiums are not paid. This type of coverage is customizable to fit your needs and budget. Once in place, the coverage can follow you if you change employer (or occupation).

Individual disability coverage provides customized options such as:

- **Future income option:** Allows you to increase coverage in future years, as your income grows, without having to prove your good health again.
- **Own occupation:** This rider assumes that you cannot perform the substantial duties of your regular job. With this rider, you could transition to a totally different occupation where you could earn an income over and above the disability benefit that you are receiving. This is for select occupations only.
- **Cost of Living Allowance (COLA):** Applies a cost of living factor based on the Consumer Price Index to your benefit, while you are on claim. This limits the negative impact of inflation on your benefits.
- **Return of premium:** A portion of your premiums may be refunded to you at future intervals if you have not had a claim on your policy in a specific period of time.
- **Retirement protector:** Provides a monthly benefit, while you are on claim, which is intended to be deposited into a retirement savings program.

3. Coverage for buy/sell agreements

When a business owner of an incorporated business or partnership is unable to work for a period of time (for example, one or two years) as a result of a disability, a provision in a detailed buy/sell agreement may outline what should occur with that person's shares or interest (e.g., the shares are to be sold to other shareholders). Sometimes a disability insurance policy is used as a funding mechanism for buy/sell agreements.

This is intended for different situations, for example, professionals such as lawyers and doctors and shareholders of small privately owned businesses. The disability benefit would be used by the corporation

to purchase the disabled shareholder's portion of the business. This can be structured as a lump-sum benefit, monthly benefit, or combination of each. The benefit would be taxable, so the benefit payment method can be structured to be paid in the most tax efficient method. The benefit would also be structured to mirror the language used in the buy/sell agreement.

4. Business overhead expense coverage

This type of disability coverage assists a company with the ability to continue paying monthly expenses if you, the business owner, are injured or ill and unable to work. Expenses covered during your disability period includes, but are not limited to rent, utilities, employee salaries, leased equipment, etc. This type of disability coverage is designed to help ensure there is a functioning business for you to return to after your recovery.

The company owns, pays for and receives the policy benefit when there is a claim. The policy premiums may be deducted as a business expense; however, benefits would be taxable as income when received by the company. Coverage typically runs for 24 months, to allow you, the business owner, time to return to work or consider other options.

Inadequate disability insurance protection may lead to financial hardship.

Assessing Adequacy of Coverage

Inadequate disability insurance protection may lead to financial hardship. You may have to:

- Dip into your savings and investments
- Sell treasured assets
- Adjust your standard of living

In order to determine whether you have adequate coverage, a licensed insurance advisor can help determine the options for your needs and objectives. Other factors that are typically reviewed include: present coverage, such as existing disability insurance policy, Canada Pension Plan (CPP) disability benefits and Workers Compensation Benefits.

Here are some of the key metrics used to determine disability insurance premiums:

- **Age:** Premiums increase in relation to age. Benefits are not paid out after the insured turns 65.
- **Gender:** The premiums for women are usually higher as they are more likely to file claims.
- **Smoking status:** Smokers pay more for DI.
- **Occupation:** This can mean "own occupation" (refers to your specific occupation) or "any occupation" (which means that the insured will not receive benefits if he or she is able to work at any occupation for which they are reasonable qualified).
- **Elimination period:** Comparable to a deductible, this is the time between the onset of a disability and the time you are eligible for benefits (usually 90 days). The longer the period, the lower your premiums will be.
- **Benefit period:** The period of time you receive benefits from the insurance carrier.
- Additional features/riders chosen.

If you have more than one disability policy, it is important to know how the policies work together. In other words, at the time of a claim, the benefits may or may not integrate seamlessly. Therefore your policies may not provide as much coverage as you expect.

Concluding Thoughts

Reviewing your insurance coverage to make sure you and your loved ones are protected, should you become disabled, is an integral part of the wealth planning process. Consider reviewing your circumstances with a licensed insurance advisor.



The information contained herein has been provided by TD Wealth and is for information purposes only. The information has been drawn from sources believed to be reliable. The information does not provide financial, legal, tax or investment advice. Particular investment, tax, or trading strategies should be evaluated relative to each individual's objectives and risk tolerance. TD Wealth represents the products and services offered by TD Waterhouse Canada Inc., TD Waterhouse Private Investment Counsel Inc., TD Wealth Private Banking (offered by The Toronto-Dominion Bank) and TD Wealth Private Trust (offered by The Canada Trust Company). All insurance products and services are offered by life licensed advisors of TD Waterhouse Insurance Services Inc., a member of TD Bank Group. All trademarks are the property of their respective owners. © The TD logo and other trade-marks are the property of The Toronto-Dominion Bank.