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If you become disabled, disability income insurance provides money to help you pay ongoing bills and avoid depleting the savings you may have accumulated for your children's education or your retirement. As with other major financial purchases, it is important to review all of the options available to you and to learn how disability income insurance works.

DISABILITY INCOME INSURANCE

Financial Protection for You and Your Family

Before purchasing an individual disability income insurance policy, evaluate your income needs as well as the benefits you may be eligible for from your employer, the government, or other programs. If you decide that you and your family will benefit from additional financial protection, a long-term disability income policy may be the right financial protection tool for you.

This guide, prepared by the American Council of Life Insurers (ACLI), outlines features and costs of individual disability income insurance and offers tips and a checklist on buying a policy.

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Consider all the sources of income you might be able to depend on should disability strike.

You may already be covered under a group disability income insurance policy through your employer or eligible for disability benefits through work, the government, or other programs. Also consider additional sources of income you might be able to depend on should disability strike: a spouse's salary; short-term emergency savings, investments, or help from your family.

If the total of these is not enough to pay your living expenses on a long-term basis, or a disability would eat away at your retirement savings or children's college fund, a long-term disability income insurance policy may serve your needs. Such coverage may be purchased as an individual policy or available under a plan offered through your employer.

EMPLOYEE BENEFITS & GROUP COVERAGE

For short-term illness or injury, your employer may offer sick leave or *short-term* disability insurance (or both). Employee sick leave and short-term disability coverage can range from a few days to six months or more, depending on the extent of benefits and the length of your employment.

Group *long-term* disability coverage—offered by some employers—replaces part of your salary if you are unable to work for an extended time. A typical group policy pays at least half your salary up to a specified limit, such as $5,000 per month. Such coverage would begin when the short-term disability benefits from your employer stop.

Benefits from group policies generally continue until either age 65 or your retirement age under Social Security or until you are able to return to work. In some policies, benefits may also be available for a specified period after your return to work.

Group coverage lasts only as long as you are employed or remain a member of the group.

SOCIAL SECURITY BENEFITS

Social Security provides long-term disability benefits based on your salary and the number of years you have worked and contributed to the Social Security system. However, Social Security replaces only a limited portion of your salary and the qualifications to receive benefits are very strict. To be eligible for Social Security disability benefits, all of these conditions must be met:

- You have been disabled for five full calendar months.
- Your disability must be expected to last at least 12 months or end in death.
- You must be unemployable at any occupation, not just your own occupation at the time of your disability.

OTHER RESOURCES

Other programs besides Social Security are sometimes available to those who have become disabled. You may qualify for:

- Workers' compensation for work-related injuries or illnesses (required in all states).
- Special disability programs for veterans injured in war, miners who develop black lung disease, railroad employees, or federal and state government workers.
- State vocational rehabilitation programs.
- Automobile insurance benefits for a disability from an auto accident.
- Temporary disability programs available in California, New York, New Jersey, Rhode Island, Hawaii, and Puerto Rico.

The amount of income you receive if you become disabled varies by policy.

INDIVIDUAL COVERAGE

If you are not covered for a long-term disability under an employer plan, or if you need to supplement that plan, an individual policy might be right for you. Not all policies are alike, however. Consider the following when shopping for a long-term disability income insurance policy:

Policy Features

- Some policies pay benefits if you are unable to perform the major duties of your *own* occupation. Other policies pay benefits if you are unable to perform the duties of *any* occupation for which you are reasonably qualified by education, training, and experience. Many policies combine these features, providing "own occupation" coverage for one or two years and "any occupation" coverage after that.
- Some policies require total disability before beginning payments while other policies cover partial disability.
- Some policies pay benefits if you become ill or injured and are unable to earn a specified amount, such as 60–80 percent of your income.
- Some policies pay "residual" benefits. These benefits make up loss of income if you are able to work but your disability prevents you from performing your normal responsibilities.
- The amount you would receive if disabled varies by policy. Policies that pay 50–60 percent of monthly salary are most common but some pay as much as 70–80 percent. Most policies do not replace commission or bonus income.
- How long you receive benefits varies by policy. Some individual policies pay benefits for a specified period, such as two or five years, while others pay benefits until age 65 or your retirement age under Social Security.
- Policies have different waiting periods (*elimination periods*) before they pay benefits. You can lower your premiums by waiting 90 days, six months, or even longer before starting to receive benefits.
- Under some policies, the insurer pays for job training or modifications to your work space.
- If you go back to work after recovering from a disability and suffer a relapse within a specific time, most policies do not impose a second waiting period.
- Some policies, as an optional benefit, offer cost-of-living adjustments to the amount you receive.
- 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.
- Most companies review an individual's medical and financial history and consider disability coverage a person already has before issuing a policy. Based on this review, an insurer may offer limited or modified coverage.
- If you purchase your own policy, disability benefits typically are not subject to income taxes. Benefits are taxed, however, if your employer pays for your coverage.
- Policies have level premiums (intended to stay constant over the life of the policy) or premiums that increase as you age. If you plan to keep your policy for the long term, a level premium policy may be best. If you are uncertain about how long you will need the insurance, a policy with premiums that increase with age may be a better choice.
- Individual long-term disability income insurance provides protection for as long as you continue to pay the premium.

Several factors affect the cost of an individual disability income policy.

COST OF A POLICY

Whether you purchase disability income insurance through an insurance agent as an individual policy or thorugh an employer or professional organization as a group policy, it is important to understand the scope of your coverage. Decide which features are most important to you—the cost of the policy will vary according to the features you select. And compare different policies—their costs and benefits—before making a purchase.

Factors that affect policy costs include:

- **Definition of disability:** A policy that pays benefits if you are unable to perform the duties of your *own* occupation is more expensive than a policy that pays benefits if you are unable to perform the duties of *any* job for which you are reasonably qualified.
- **Benefit amount:** Policies that replace a larger percentage of salary are more expensive. For example, a policy that replaces 80 percent of your salary will cost more than one that replaces 60 percent of your salary.
- **Benefit period:** The longer the benefit period, the more expensive the policy. For example, a policy with a two-year benefit period will cost less than a policy that pays until age 65 or your retirement age under Social Security.
- **Age and health:** Older people, who are more likely to become disabled, will pay more that younger people. Likewise, a person in poor health is likely to pay more than a person in good health. A policy may exclude certain preexisting health conditions from coverage.
- **Extent of disability:** A policy that pays benefits for a partial or temporary disability costs more than a policy that only pays if the policyholder is totally and permanently disabled.
- **Type of job:** A person with a high-risk occupation can expect to pay more in premiums than a person with a low-risk job.
- **Optional benefits:** Cost-of-living adjustments or the option to purchase future benefits will add to the cost of premiums.
- **Smoking/tobacco use:** Most companies give a discount to non-tobacco users or add a surcharge to the premium of a tobacco user.
- **Group discounts:** Many companies offer discounts for policies issued on more that one person at the same time or when an employer collects the premiums and pays the insurer. Women usually pay more than men for an individual policy because claim costs are higher for women. Under a group policy, however, men and women usually pay the same rate.

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TIPS ON BUYING

- **Examine how the policy defines a disability.**
- **Ask for outlines of coverage** so you can compare several policies.
- **Make sure you fully understand the policy.** A policy that does not provide the protection you need is not a good buy. Features to look for include:
  - Clear definitions of disability (*own* occupation vs. *any* occupation)
  - Amount of benefits
  - Elimination period (the waiting period before benefits begin)
  - Benefits for partial disability
  - Provisions for replacement of lost income
  - Return-to-work programs
  - Recurrent (relapse) provisions
  - Cost-of-living adjustments (or the right to purchase additional coverage)
  - Mental health/substance abuse provisions
  - Noncancellable or guaranteed renewable options
  - Exclusions or limits on coverage
- **Check that the company and agent are licensed in your state.** If you have concerns, contact your state insurance department. The National Association of Insurance Commissioners (NAIC), an organization of insurance regulators from each state, can be found online at www.naic.org.
- **Look for a company that is reputable and financially strong.** Several services rate the financial strength of companies. You can get rating information can from your agent, online, or from public or business libraries. Ratings on Web sites are usually free, but there may be a charge for ratings provided by phone. Rating agencies include:
  - A.M. Best Company, www.ambest.com or (908) 439–2200
  - Standard & Poor's Insurance Rating Services, www.insure.com/ratings
  - Duff & Phelps Inc., www.insure.com/ratings
  - Moody's Investor Services, www.moodys.com or (212) 553–0377
- **Fill out your application accurately.** Answer questions about your medical history and health completely and truthfully. If you are dishonest, the company may be able to cancel your coverage.
- **Read your policy carefully** to make sure it offers the coverage you need. For instance, some policies pay benefits only if you are disabled due to an accident, not an illness.
- **Check the date** that the insurance becomes effective.
- **Make your check payable to the insurance company,** not the agent, and get a receipt.
- **Review your policy.** You may have a "free-look" period (usually 10 days after you receive the policy) when you can change your mind. If you review your policy during the free-look period and decide not to keep it, the company will cancel the policy and give you a full refund.
- **Contact the customer service office** of your insurance company if you have a complaint about your insurance agent or company. If you are still dissatisfied, contact your state insurance department.

Checklist for Comparing Disability Income Insurance Policies

Use this checklist to compare several policies.

Company name _____

Telephone _____

Definition of disability _____

Some policies pay benefits if you are unable to complete the duties of *any* occupation for which you are reasonably qualified by training, experience, and education. Others pay benefits if you are unable to perform the major duties of your *own* occupation. Determine which definition applies to this policy:

Are benefits paid if you are unable to complete the duties of your *own* occupation?

____ Yes ____ No

How long can benefits be collected under this definition?

_____

Are benefits paid if you are unable to perform the main duties of your *own* occupation but could perform duties in another line of work?

____ Yes ____ No

How long can benefits be collected under this definition?

_____

Are benefits paid only if you are unable to complete the duties of *any* occupation for which you are reasonably qualified by training, experience, and education?

____ Yes ____ No

How long can benefits be collected under this definition?

_____

Must you meet two or more definitions of disability, for specific periods, before you collect benefits?

____ Yes ____ No

Some policies pay benefits if you become ill or injured and are unable to earn a specified percentage of your income.

Will this policy pay benefits if you are unable to earn a specified percentage of your salary?

____ Yes ____ No

What is the percentage?

_____

Is the benefit from this policy a percentage of your regular income or a flat amount?

____ Percentage of income at ____ percent

____ Flat amount of $ ____ per _____

(Policies that pay a flat benefit amount each month are common.)

Some policies pay benefits when you have a partial disability that keeps you from doing part of your job or working full time.

Does this policy provide benefits for a partial disability?

____ Yes ____ No

Although some insurance pays immediately after a policyholder suffers a disability, most policies have a waiting, or elimination, period. Elimination periods can last six months or longer.

What is the elimination period for this policy?

____ Less than one month

____ Three to six months

____ Longer than six months

For most disabilities, policies pay benefits until retirement age but shorter benefit periods are available at lower cost.

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Some policies provide a benefit to make up income if you must take a lower-paying job because of your disability.

Does this policy pay benefits if your disability results in less income?

____ Yes ____ No

Some policies have return-to-work or rehabilitation provisions that help you pay for training, modifications to your work environment, or other services that can help you return to work.

Does this policy have a return-to-work or rehabilitation provision?

____ Yes ____ No

(If a return-to-work provision is not listed, ask about such a provision.)

If you return to work after recovering from a disability, and have a relapse within a specified period, most policies do not make you to go through an elimination period before receiving benefits.

Does this policy make you wait for benefits if you experience a reoccurring disability?

____ Yes ____ No

A cost-of-living adjustment provides for periodic increases in the amount paid to you, usually corresponding to increases in the cost of living.

Does this policy provide a cost-of-living adjustment?

____ Yes ____ No

Policies usually pay benefits for a maximum of two years for disabilities from mental illness or substance abuse. (These limits usually don't apply when substance abuse or mental health problems require institutionalization.)

How long does this policy pay benefits for disabilities from mental illness or substance abuse?

_____

There are two common types of individual disability income policies: noncancellable and guaranteed renewable. Both types can usually be renewed until age 65, and neither can be cancelled by the insurer as long as the premiums are paid. Under a noncancellable policy, premiums can never be increased. With a guaranteed renewable policy, premiums cannot be raised based on an individual circumstance, but they can be increased for an entire class of policyholders.

Is this policy noncancellable?

____ Yes ____ No

Is the policy guaranteed renewable?

____ Yes ____ No

ACLI is a Washington, D.C.-based trade association, whose 373 members account for 93 percent of the life insurance industry's total assets in the United States. Its member companies offer life insurance; annuities; pensions, including 401(k)s; long-term care insurance; disability income insurance; reinsurance; and other retirement products.

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