PSG Wealth

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EMPLOYEE BENEFITS NEWSFLASH

News you need to know

Disability insurance is not just a nice to have

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As South Africans we insure everything from our homes and our cars to our business equipment and the contents of our handbags. But we often overlook one asset that's even more difficult to replace than all of the above: ourselves.

Disability insurance protects your most vital asset – the ability to work and earn an income. Keep in mind though that disability insurance policies should be tailor-made to suit your particular needs. There's no one size fits all solution.

Disability insurance unpacked

There are three different types of disability insurance: own occupation disability, occupational disability or total disability cover.

1. Own occupation disability

Many people who are partially disabled still want or need to work. Own occupation disability is the only insurance that does not penalise you for going back to work in a different occupation while on a claim.

Under this type of plan, if you cannot perform effectively in your occupation because of a sickness or injury, you will be considered totally disabled, even if you choose to do something else. However it is important to note that this is only for true own occupation disability policies and it must be indicated in the wording of your policy. In most instances, the policy will then only cover the drop in income that you have experienced due to the change in occupation.

The 'own occupation' provision of disability policies makes it easier to receive the benefit because you do not have to be completely disabled, but rather simply unable to complete the normal tasks associated with your nominated occupation.

2. Occupational disability

When it comes to occupational disability you will only be covered if you are unable to perform your specific job or a related occupation (also known as "own or similar" occupation). For example, if you are an orthopaedic surgeon and lose the use of your hand you obviously won't be able to continue practising as a surgeon. However, you can become a GP, in which case you will not receive the benefit.

There may well be a concomitant reduction in earnings associated with such a career shift, so it is always better to take out an own occupation disability policy – particularly if you are in a specialised field. It does, however, come at an additional cost. However, note that most policies will apply a combination of "own occupation" and "own or similar" occupation definitions as explained below.

3. Total and permanent disability

With total and permanent disability, you will only be covered if you are unable to work at all – regardless of what your job or occupation is.

Disability insurance can be paid in two forms

1. Lump sum benefits

These are usually expressed as a multiple of annual income, and are paid only in the event of total and permanent disability and are not meant to provide a monthly income. The amount should be used to pay off debts (like a mortgage loan), adapting your environment for your disability or investing for your future.

The lump sum you receive will normally be paid out tax free, however your insurance premiums are not tax deductible.

2. Loss of income protection

Income protection benefits are usually expressed as a percentage of your monthly (stipulated) income, and are paid on a monthly basis until the earlier of recovery, death or retirement age. The premiums will depend on your occupation, your income, the age until which you want to receive an income, your existing health status and with which company you are insured.

Protection against a temporary loss of income is another option. This is usually to cover you in the event of an accident, operation or illness that disables you temporarily, and is especially relevant to self-employed individuals. This cover typically lasts for a maximum of two years.

Most income protection cover policies will pay benefits based on the "own occupation" definition for a specified period (e.g. 24 months), after which the definition is broadened to the "own or similar" occupation-based definition described above.

With loss of income protection benefits, your premiums are taxable (in the case of employer-paid premiums, they rank as a taxable fringe benefit) but your monthly benefit payments are tax free. Not only do you have the peace of mind that comes from such cover, but there's also a welcome tax free benefit if you claim.

With permanent loss of income protection you are usually compensated from the date you are disabled to retirement age (between 60 and 70). The monthly payment is usually equal to about 75% of your most recent taxable income.

Disability cover isn't too different from any other type of insurance. It's a precautionary measure to protect you from financial damage should anything go wrong, just like motor vehicle or fire insurance. The only difference is that it might be one of the most important types of cover you can get. Even though losing a car or a house can mean financial hardship, losing the ability to work almost certainly means financial ruin.