ARE YOUR HIGHLY COMPENSATED EMPLOYEES UNDERINSURED?

PROTECT YOUR ABILITY TO EARN INCOME

For most employees, purchasing disability insurance is a low priority. Although they often recognize the value of employer-sponsored medical and life insurance, the need for disability insurance does not seem as important. Only 38% of full-time employees consider disability insurance one of the five most important benefits. Even dental and vision benefits, which are more affordable and cover less catastrophic losses, are ranked above disability insurance in importance by employees.[1] Similarly, outside of their employer-sponsored insurance benefits, people understand the importance in purchasing insurance on their personal assets such as their home, car, and other big-ticket items. However, they often overlook protecting the one asset which makes acquiring all other assets possible: **their ability to earn income.**

> **"Providing individual long term disability (LTD) policies in addition to the company's group policy can help offset the disproportionate decrease in income."**

Highly compensated employees are particularly at risk of significant financial loss should they lose their ability to earn income during a disability. Most group policies are designed to provide basic coverage to the average wage earner and are inadequate in providing enough income to support a highly compensated employee. By making an individual disability insurance (IDI) policy available as an executive benefit, employers would have a valuable tool for recruiting and retaining key employees while helping those employees protect their income in the event of a disability.

IS DISABILITY INSURANCE REALLY NECESSARY?

The odds of incurring a disabling injury are increasing: as advancements in medicine help people live longer and as the auto industry develops improved safety features, things that were once deadly now disable people instead. According to the National Safety Council, motor vehicle accidents lead to a death every 12 minutes, but lead to a disabling injury every 14 seconds.[2] By age 65, one in three working Americans will suffer from a disability lasting at least three months.[3]

The effects of a disability can be financially devastating without the income protection offered by disability insurance. A recent Harvard study indicated that almost half of all personal bankruptcies are the result of an illness or injury.[4] Furthermore, 48% of all mortgage foreclosures are the result of a disability, compared to only 3% caused by death of the primary income provider.[5]

ISN'T OUR GROUP POLICY ENOUGH?

Although 60% of full-time employees have some disability insurance through their employer, the coverage amount is inadequate for many employees. This is especially true for highly-compensated employees. The benefit amount of most group disability plans is between 50% to 70%, and there is usually a cap placed on the maximum monthly benefit. While the average employee drawing 60% disability may not meet that limit, for a highly compensated employee, that cap may be well under 60% of their salary.

Most group disability plans only cover a percentage of base salary and exclude variable compensation such as bonuses and other incentive pay, which often make up a significant amount of many executives' total income. Therefore, the same group policy that pays a full 60% of total gross income for the average employee will often pay a considerably lower percentage of total income for a highly compensated employee who relies heavily on variable compensation. Also, since the paid benefit is taxed when the premiums are paid by the employer, the compensation received during a disability is reduced even further. Figures 1 and 2 illustrate how providing individual long term disability (LTD) policies in addition to the company's group policy can help offset the disproportionate decrease in income for highly compensated employees during a disability.

Figure 1

INCOME REPLACED WITH 60% GROUP LTD BENEFITS ONLY

Employee	Base Salary	Bonus Income	Gross Monthly Income	Group LTD Benefit	Individual DI Benefit	% of Income Replaced
Employee 1	$45,000	$0	$3,750	$2,250	$0	60%
Employee 2	$65,000	$10,000	$6,250	$3,250	$0	52%
Employee 3	$100,000	$50,000	$12,500	$5,000	$0	40%
Employee 4	$200,000	$70,000	$22,500	$6,000	$0	27%

Figure 2

INCOME REPLACED WITH 60% GROUP LTD AND INDIVIDUAL DI BENEFITS						
Employee	**Base Salary**	**Bonus Income**	**Gross Monthly Income**	**Group LTD Benefit**	**Individual DI Benefit**	**% of Income Replaced**
Employee 1	$45,000	$0	$3,750	$2,250	$832	82%
Employee 2	$65,000	$10,000	$6,250	$3,250	$1,525	76%
Employee 3	$100,000	$50,000	$12,500	$5,000	$3,500	68%
Employee 4	$200,000	$70,000	$22,500	$6,000	$8,700	65%

Source: MetLife Individual Disability Presentation, 2005

OPTIONS: EMPLOYER-PAID OR EMPLOYER-SPONSORED

In making an IDI product available, the employer can opt to offer either an employer-paid plan or an employer-sponsored plan. If budget constraints prevent the employer from paying the premiums for individual disability plans, the employer can still reap the benefits of having an IDI plan in their benefits package by instead acting as a plan sponsor. In this approach, employees can purchase a plan at a discounted premium through the employer sponsorship and pay their premiums through payroll deductions. The policies are portable because the employees are then the owners of their own IDI policies.

Despite the need for individual disability insurance for highly compensated employees and the various means of offering an IDI product through either employer-paid or employer-sponsored plans, only 17% of employers offer IDI as an executive benefit, with only an additional 6% currently planning on adding that benefit within the next 18 months.[1] By making an IDI plan available, employers can equip themselves with a valuable tool that puts them ahead of the competition in the recruitment and retention of key employees.

Sources:

1. MetLife Study of Employee Benefits Trends, 2004
2. National Safety Council, Injury Facts, 2003
3. Commissioner's Individual Disability Table A
4. HealthAffairs.org, Market Watch: Illness and Injury As Contributors to Bankruptcy
5. U.S. Housing and Home Finance Agency