Life & Health Insurance Advisor

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The Coverage Gap You Might Not Know You Have (And How AD&D Fills It)

Smart consumers have health insurance to protect themselves from catastrophic medical expenses, life insurance to protect their families from the loss of a breadwinner, and disability income coverage to replace income lost due to disability. So which of these policies will cover you if you lose a limb, sight or hearing in an accident?

You might be surprised to learn that none of these policies will compensate you for the loss of a limb or one of your key senses. Yes, your medical policy would cover bills for related medical treatments. And your disability income policy would replace lost income if the loss made you unable to work. But only one type of policy will provide compensation for the loss of your limb, sight or hearing. It's accidental death and dismemberment coverage, or AD&D.

AD&D coverage provides compensation when an insured dies or loses a limb, vision, speech or hearing as a direct result of an accident. If an illness were to cause any of these serious consequences, you would generally have some warning and time to prepare yourself and your family. But when an accident occurs, it's sudden and unexpected, making the loss all the more traumatic. Although AD&D coverage can't replace your or your loved one's life, limb or senses, it can help ease the trauma.

You can buy AD&D coverage on a standalone basis or as an addition to a term life policy. For the cost of a couple of espresso drinks every month, an individual under age 65 can get coverage of up to $250,000, although you can buy limits of up to $10 million.

AD&D coverage is particularly attractive to younger individuals, who are statistically more likely to die from or suffer an accident than an illness. For these people, adding an AD&D rider to their life insurance policy might be cheaper than increasing the face value of their life policy. If you do buy an AD&D rider, the insurance company will pay a "double indemnity." This means if a covered accident causes the insured's death, the beneficiary will receive the life policy's death benefit, plus the AD&D benefits.

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This Just In

In 2008, the average benefit amount for an individual noncancellable disability income policy had reached $3,857, according to the annual survey by JHA, a leading disability reinsurer. Average annual premiums for both short- and long-term noncancellable policies reached $1,920 in the fourth quarter of 2008, according to LIMRA International, Inc.

You'll pay less — an average of $629 per year — if you buy a guaranteed renewable policy instead of a noncancellable policy. However, when you buy noncancellable coverage, your premiums remain the same for the life of the policy. With noncancellable coverage, the insurer cannot cancel your coverage or raise your rates, no matter what your health condition. With guaranteed renewable coverage, the insurer guarantees it will renew your policy, but your premiums can increase — sometimes dramatically — if your health status changes or if the carrier increases rates for all policies in your rate class. For more information on disability income coverage, please contact us.

Life Insurance for Business Owners

Most people buy life insurance to protect their families' financial future. But business owners can use life insurance coverage to protect the future of their business as well. Here's how.

Many entrepreneurs like to think the business they've worked so hard to build will live on after they retire or die. But experts estimate that more than half of all business owners over the age of 60 do not have a formal business continuation plan.

Using Life Insurance to Fund a Buy/Sell Agreement

A business continuation plan ensures that the business continues to survive, managed by the owner's chosen successor. The written agreement that spells out the terms of ownership is called a buy/sell agreement. This requires the firm or surviving owners/partners to buy out the interest of another owner/partner if he or she dies, retires or becomes disabled. Either the individual owners can buy the interest of withdrawing partners (a cross-purchase arrangement) or the business itself can buy them (an entity purchase or stock retirement agreement), using business funds.

The buy/sell agreement should also spell out the method used to valuate an owner's interest. To do this, you'll need to know how much the business is worth, allowing for future growth and inflation. For a smaller business, a financial planner or business advisor may be able to help, but a certified valuation appraiser will be able to come up with a more accurate figure.

A buy/sell agreement allows the continuation of the business, ensures heirs get a fair value for their interest and helps prevent succession struggles. This usually means one or more heirs will have to be bought out, so the plan requires some form of funding.

A life insurance policy offers significant advantages over other forms of funding:

1. Funds are available immediately. If one of the owner's heirs succeeds as manager, he or she will not have to wait for the estate to settle to obtain the funds to buy out other heirs. If the successor is a partner, he/she will not have to rely on personal savings or loans for funds.
2. When the business pays premiums on the life of its owner with taxable dollars, the benefit is tax-free.
3. You can guarantee millions in funding will be available, without relying on cash flow. A healthy individual can buy life insurance with a death benefit of $10 million or more.

Using Life Insurance to Protect the Company from Loss of a Key Employee

Life insurance can protect a business from the loss of a "key employee." The key employee need not be an owner or partner, but has special skills or experience that are vital to the firm. The firm buys a policy on the key employee's life, naming itself as the beneficiary. Policy proceeds can pay for income lost due to the key employee's death and help pay the costs of recruiting a replacement.

How much and what type of life insurance will you need to insure the life of a key employee? You can base the policy benefit amount on estimated lost earnings, the additional compensation needed to hire an experienced replacement or a combination of both.

The business takes out the policy on the life of the key person, pays the premiums and receives the benefit if he/she dies. The insured's family has no interest in the policy at all.

If the need for key employee protection is temporary (i.e., your software business is growing and you expect to be able to hire another key engineer in the near future), then buying term life insurance makes the most sense. But if you're insuring the life of a relatively young founder, then you might want to consider permanent, or whole life, insurance. With permanent insurance, the premiums will remain level for as long as the insured lives, and the policy's accumulating cash value would become an asset on the company's balance sheet.

For more information on using insurance in your business continuity planning, please contact us.

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What AD&D covers

An AD&D policy will pay benefits if the insured suffers an "accidental death." This means an unforeseen circumstance, unrelated to illness or malfunction of the body, causes the death.

To illustrate the difference between life coverage and AD&D, consider an auto accident victim. If someone suffered a stroke or heart attack that caused an accident while driving, a life policy would pay. It would also pay if another driver caused the accident. But an AD&D policy would not pay if the "bodily malfunction" — the heart attack or stroke — caused the death. It would only pay if the accident itself caused the death.

AD&D can also provide benefits for certain types of disabilities, although it is not a substitute for disability income insurance.

Many policies will pay benefits if a covered accident causes an insured to lose extremities, hearing or sight. The benefits you receive depend on the extent of loss. For example, a policy might pay half of the death benefit for the accidental loss of one hand or arm or one foot or leg. If the insured lost two or more limbs (a combination of arms and legs), the policy would pay the entire face value (death benefit).

AD&D policies may also cover the sudden loss of vision. The same principles apply. If an insured loses one eye (or its use), the policy would pay one half of the benefit. If he/she loses both eyes, then the policy will pay the entire face value.

It's important to keep in mind that AD&D policies do not cover death by any form of illegal or crime-related activities. Policies also don't cover death by suicide or death by a malfunction of the body. Most insurers exclude coverage for death or dismemberment caused by war or terrorism-related events, but some insurers will cover this at extra cost.

Because they don't cover death from illness, an AD&D policy is no substitute for life insurance. Nevertheless, it can provide valuable supplemental coverage — at a low cost — if you already have life and disability income coverage.

For more information, please call us.

AD vs. AD&D

Some life insurance companies offer AD riders, or accidental death riders. Like the AD&D rider, it will provide "double indemnity" if an insured dies as a result of an accident. However, it will not cover loss of limb, sight or vision.

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ability policies, cancer or "dread disease" policies and long-term care policies does not preclude eligibility.

- ✔ You cannot be enrolled in Medicare and you cannot have received VA benefits in the last three months.
- ✔ You cannot be claimed as a dependent on someone else's tax return. This means children cannot establish their own HSAs; however, spouses can establish their own HSAs, if eligible.

Advantages

- ✔ There is no income limit on who may contribute to an HSA.
- ✔ Even those without an income (such as a stay-at-home spouse or retiree not yet eligible for Medicare) can contribute to an HSA.
- ✔ Employers can also contribute to your account; if an employer makes a contribution, it is excluded from your income and wages.
- ✔ Contributions you make are an "above-the-line" deduction.
- ✔ You control your account. Unlike employment-based healthcare accounts, such as flexible spending accounts (FSAs) or health reimbursement arrangements (HRAs), you control your account, which remains yours even if you change jobs or retire.
- ✔ Your funds accumulate year to year. Unlike FSAs, HSAs have no "use it or lose it" provisions.
- ✔ You can invest your HSA funds into a variety of investment vehicles; funds grow tax-free.
- ✔ Even though you can no longer make contributions to an HSA after enrolling in Medicare, you can use funds in your HSA to pay eligible healthcare costs, even Medicare premiums.
- ✔ You can make a one-time transfer from your IRA into an HSA, subject to contribution limits applicable for the year of the transfer.
- ✔ Withdrawals from HSAs are exempt from federal income taxes if used for qualified medical expenses.

Disadvantages

- ✔ HSAs require enrollment in a high-deductible health plan, which has higher out-of-pocket expenses than other types of plans. Individuals unaccustomed to budgeting for routine healthcare, such as doctor visits and prescription drugs, could be in for sticker shock. However, relatively healthy individuals who are good at budgeting could end up ahead of the game after a few years due to the growth of their HSA account.
- ✔ HSA funds must be used for qualified healthcare expenses only. If you withdraw funds and do not use them for qualified medical expenses, the money will be included in gross income on your federal income tax form and subject to an additional 10 percent penalty tax. The penalty will be waived in cases of disability or death and for individuals age 65 or older.

HSAs Making Inroads in Individual Market

Unlike most medical plans, which cover you for only the term of the policy, a Health Savings Account can pay for your medical expenses now and in the future.

The 2003 Medicare Modernization Act authorized health savings accounts (HSAs), which consumers can use in conjunction with high-deductible health plans (HDHPs) to pay for qualified medical expenses. Although HSAs were slow to take off, the number of people enrolled in HSAs grew six times between March 2005 and January 2008, according to research by America's Health Insurance Plans (AHIP), a trade association. By January 2008, more than six million people had HSAs.

Although smaller employers who could not afford more traditional health benefit plans were among the first to adopt HSAs, their popularity has been increasing in the individual health insurance market as well. By January 2008, HSAs/HDHPs comprised 27 percent of new health insurance purchases in the individual market. Should you consider an HSA? The following information will help you decide.

Eligibility requirements

- ✔ You must be enrolled in a high-deductible health plan (HDHP) that does not cover first dollar medical expenses (except for preventive care). Your HDHP can be an HMO, PPO or indemnity plan, as long as it meets the requirements.
- ✔ You cannot have any other health insurance. This includes flexible spending accounts (FSAs) or health reimbursement arrangements (HRAs) that provide medical coverage, unless these accounts restrict reimbursement to certain permitted benefits such as vision, dental or preventive care benefits. Owning other types of policies that provide limited health benefits for specific purposes, such as auto policies, accidental death and dis-

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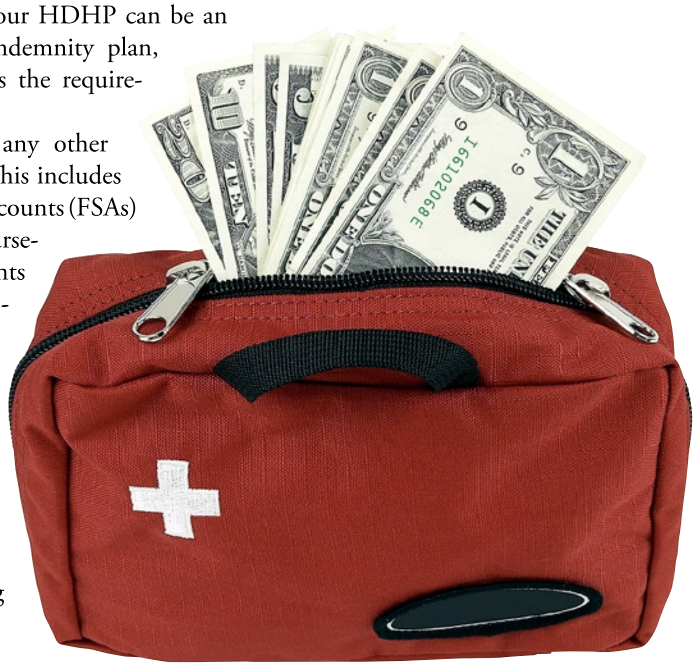

What Is a "High-Deductible Health Plan" (HDHP)?

To qualify you for enrollment in an HSA, your HDHP must meet specific criteria:

- ✔ **Minimum deductible of $1,150 (self-only coverage); $2,300 for family coverage**
- ✔ **Annual out-of-pocket maximums (including deductibles and co-pays) cannot exceed $5,800 (self-only coverage) or $11,600 (family coverage).**

These amounts are for 2009 only and are indexed annually for inflation.

Your plan can offer first-dollar coverage (no deductible) for preventive care, or a qualified medical service or benefit not intended to treat an existing illness, injury or condition. The list of "safe harbor" preventive care treatments includes:

- ✔ **Periodic health evaluations (e.g., annual physicals)**
- ✔ **Screening services (e.g., mammograms)**
- ✔ **Routine pre-natal and well-child care**
- ✔ **Child and adult immunizations**
- ✔ **Tobacco cessation programs**
- ✔ **Obesity weight loss programs**
- ✔ **Certain drugs and medications, if taken to prevent recurrence of a disease or by a person who has developed risk factors for a disease that has not yet manifested itself (such as cholesterol-lowering medications in a person who has high cholesterol levels). However, if your HDHP provides prescription drug benefit, your plan must subject prescription drug expenses to the annual deductible or you may not contribute to an HSA.**

For assistance in selecting an HDHP that meets your particular healthcare needs, please contact us.