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Disability Income Insurance: Protecting Your Most Valuable Asset

Have you ever wondered how you would manage financially if you were to experience an injury or illness that left you unable to work? How long could you maintain your standard of living, pay your bills, and cover your daily expenses? The likelihood of such an event may be greater than you think. According to the Insurance Information Institute (III, 2010), 43% of all people age 40 will have a long-term (lasting 90 days or more) disability event by age 65.

To be prepared for such a situation, it is important to *plan ahead* and be proactive. To help protect yourself, you may wish to purchase an **individual disability income insurance** policy, which would replace a portion of your income in the event that you experience a qualifying disability. Consider the following when choosing among the coverage options:

- **Definition of Disability.** Carefully review the policy's definition of disability. Some policies may provide coverage if you are unable to work in the occupation in which you were employed or for which you were trained, or if you can no longer earn as much as you once did in that field. In contrast, other policies may offer coverage only if you are unable to work in *any* occupation. In other words, if you were to experience a disability but were able to work in a lower skilled, lower paying job, you may not receive benefits.
- **Residual Benefits or Partial Disability Coverage.** Under certain specified circumstances, if you become disabled and are only able to earn a *portion* of your previous income, residual or partial disability coverage pays a percentage of your benefits.
- **Guaranteed Renewable.** With this feature, the insurer cannot refuse to renew your policy prior to the policy expiration date or change any terms, except for premium cost, as long as you continue to pay your premiums on time.
- **Guaranteed Insurability.** This provision allows you to increase your coverage amount, even if you experience health changes that would otherwise prevent you from obtaining additional disability coverage.
- **Cost-of-Living Adjustment (COLA).** This feature helps protect your benefits against the effects of inflation during a long-term disability.

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Tips for Creating an Effective Estate Plan

Whether your estate plan is simple or complex, there are many details that can undermine the effectiveness of your plan. But, there are also ways of ensuring that your plan is effective. Below are ten steps to help remedy or avoid some common estate planning mistakes.

Consider using a will to transfer property to children instead of owning property jointly. Unlike a will, a transfer of an interest in your property is irrevocable, which may prevent you from changing the disposition if circumstances change before your death. Holding the title to your personal residence jointly can result in partial loss of the capital gain exclusion if it is sold before your death. Therefore, it's often recommended that you use your will to make any property transfers that will occur upon your death.

Think before gifting property to your children. Parents often regret having made outright gifts to their child if the child subsequently divorces and the ex-son- or daughter-in-law is awarded an interest in the gifted property by a court. Or, under other circumstances, the property may be taken pursuant to a legal judgment against the child. Such problems can be minimized through proper use of trusts or a business entity, such as an LLC.

Ensure your assets pass in accordance with your wishes upon your death. Many types of assets can pass to your heirs or others based upon beneficiary designations (e.g., life insurance, IRAs, brokerage accounts). The provisions of your will cannot change a beneficiary designation. Remember to account for items you've already designated when you create your will. Review your will, as well as all other beneficiary designations, when formulating your estate plan.

Understand your estate's true value for Federal estate tax purposes. Many people don't know that life insurance proceeds are included in their taxable estates if they own the policy. This could increase their total estate value to more than the amount sheltered from estate tax by the estate tax exemption ($5 million in 2011).

Consider state estate taxes in light of recent law changes. Many states have "decoupled" their estate tax from the Federal estate tax, which means your estate could be subject to tax in a state even if no Federal estate tax is due. This could result in problems that might be avoidable with proper planning. The laws of each state where you own property should be carefully reviewed to determine the potential exposure to state estate taxes and how to minimize them.

Review the portability provision of the estate tax exemption. Under the Tax Relief, Unemployment Insurance Reauthorization, and Jobs Creation Act of 2010 (2010 Tax Relief Act), the estate tax exemption may be transferred between spouses in 2011 or 2012, so that if one spouse dies in 2011 or 2012 and does not use the full exemption amount, the remainder can be used by the surviving husband or wife, if he or she also dies during this time frame. For estate planning purposes, this means that husbands and wives do not have to split assets between them, or be concerned about who holds the title on various assets. Yet, this change does not eliminate the need for planning. Because the portability of the estate tax exemption is only in place through 2012, wealthy taxpayers who currently fall within the exemption limits may still want to consider setting up a bypass trust in anticipation of future changes in the rules.

Maximize income tax basis "step-up" benefits at death. Consider holding low-basis/high-value assets to be given at your death, since the basis for capital gain computation purposes will be increased to fair market value at death. If the asset is given away, the basis remains at the property's original cost.

Specify your desired funeral arrangements. A pre-arranged funeral may relieve family members from additional stress upon your death. You can also prepare for the costs of a funeral.

Plan for a potential disability. Consider establishing advance directives, powers of attorney, and designated trustees, since costly and time-consuming court proceedings may be required in order to appoint a guardian or conservator to act on your behalf if you become incapacitated.

Review and update your estate plan regularly. Changes in the law and in your personal situation make it important to periodically review and update your estate plan so that it continues to reflect your wishes.

Early and thorough estate planning can help ensure that your thoughtful planning will ultimately be implemented. Be sure to consult with your tax, legal, and financial professionals.

Controlling Your Runaway Expenses

For many of us, the cost of living has risen faster than our income has. In some cases, consumption has increased, as well. If you are looking for ways to control both rising expenses and increasing consumption, here are some timely suggestions.

Saving Begins at Home

- You may be spending more of your income on housing than in the past. Make sure you are getting the best rates available for both your mortgage and any equity loans, and that you are deducting the maximum amount allowable under current Internal Revenue Service (IRS) rules. Shop around to be sure you are getting the best deal possible.
- Review your home heating fuel consumption for the last 12–24 months. Create a budget that reflects current prices. Regardless of fluctuations in fuel prices, conservation is essential. Check your insulation and consider installing a programmable thermostat, if you don't already have one.
- Check with your local electric and water departments for conservation programs and tips. Expect their rates to continue rising, and adjust your lifestyle accordingly.
- Examine your phone bill. Are you really using all the services you're paying for every month? Cell phone bills can become exorbitantly high due to overages or roaming charges. Review your phone use periodically to be sure you're using your services effectively.

Shopping by the Numbers

- Headed to the grocery store? Make a shopping list, get a store card for specials, clip coupons, and grab a supermarket circular to be on the lookout for weekly deals. Doing so may reduce your weekly food bill considerably.
- Clothing prices may seem sky high, but you have the power to bring them down to earth by remembering that the name brand on the garment does not necessarily mean that the clothing will wear any better or last any longer than the "no-name" variety.

Health and Fiscal Fitness

- A regular fitness program may lead to better health and fewer visits to the doctor. In many cases, the sidewalk outside your home will work just as well as the fitness club down the street. Talk to your health care provider about ways to incorporate more activity into your daily routine.
- If your doctor approves, choose "generic" medications and look for pharmacies that offer reduced rates. The same store may also offer reduced prices on prescription eyewear.

Entertainment and Dining Out

- The "necessity" of cable television is a wonder of the modern age, and the cost continues to increase. Assess your cable usage to see if all those "must-have" channels are really necessary. It may be time to sign up for fewer TV channels and take more trips to the library.
- The cost of a trip to the movie theater is another increasing expense. Enjoy Friday nights at home with the family making pizza and watching DVDs. Family game nights are another economical option.
- There are times when busy schedules make eating out a necessity. But, dining out does not need to come with a high price tag. "Two-for-one" specials and "kids eat free" offers are more common than ever.
- All the "little" expenses (banking fees, morning coffee runs, magazine subscriptions, personal care products, lottery tickets, etc.) can gradually grow until they devour the best-laid spending plans. Analyze these expenses to see which are truly necessary and which you can do without.
- The final budget-busting monster of the modern age is the credit card, with its associated annual fees and finance charges. High interest, long-term credit card debt can be expensive, so develop a "pay-off" plan to strategically lower this costly burden until you're debt free.

We may not be able to control rising prices, but we are not powerless either. If you have fallen prey to runaway spending and increased consumption, you are not alone. Develop a budget today to help control your runaway expenses and still have fun!

Tax Audits: Know Your Rights

For many taxpayers, the words "tax audit" can produce feelings of anxiety. If you receive an audit notice from the IRS, hiring a tax professional to represent you may be an appropriate strategy. However, should you choose to handle an audit yourself, the Taxpayer Bill of Rights (included in the Technical and Miscellaneous Revenue Act of 1988) allows you to record your meetings with an auditor, if prior approval has been obtained from the IRS, and to adjourn a meeting with an auditor at any time to either consult with your tax professional or to request professional representation.

The best way to be prepared for the possibility of a tax audit is to keep well-organized records of your prior years' returns along with complete, supporting documentation. Furthermore, while you may find tax theory less than exciting, you may want to try to learn as much about your tax return as possible. While these steps may have little effect on your chances of being audited, they can help reduce your anxiety level should the IRS request more information about your tax return.

disability income insurance: protecting your most valuable asset

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It is important to note that the cost of a disability income insurance policy varies according to the scope of coverage you choose, and there may be an additional premium for adding any **riders**.

The Outlook without Protection

If you don't have a disability income insurance policy, there are alternatives, although they all have shortcomings. For instance, you could self-insure. But, even if you save 10% of your salary each year, one year of disability could easily use up many years of savings. Or, perhaps your employer provides group disability insurance. Unfortunately, **employer-sponsored plans** are often limited in scope and duration, and generally coverage is not portable upon termination of employment. **Workers compensation** may be an option in some cases; however, it only covers injuries that occur on the job. Eligibility and benefits vary by state.

To qualify for **Social Security** disability benefits, specific criteria must be met, and you may have to wait several months for payments to begin. Social Security disability was not intended to be an individual's sole source of disability income. Thus, benefits are often less than what is needed to cover living expenses.

An illness or injury that reduces or eliminates your primary source of income can be a financially difficult experience. Therefore, it's important to consider disability income insurance as part of your overall financial strategy.