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**DECIPHERING DISABILITY INCOME INSURANCE:  
UNDERSTANDING POLICY FEATURES**

**BY JEFF SADLER, CLTC, CSA**

**Course Reading Assignment**

**CHAPTER I**

**I. INTRODUCTION**

The concept of income protection is fairly easy to understand. However, there are always hurdles to clear, be it affordability, insurability and the willingness of many to simply gamble that it will never be a problem for them.

People spend weeks, months and years trying to build up their income, putting in the extra time, taking the promotions that come along, all focused on a current or future financial goal, be it a house, a new car, the kids' college education, or a retirement villa in Spain. The spotlight shines so bright on these financial objectives that it is easy to overlook the one key element that makes it all possible – the ability to work and earn an income.

If you read news online or watch TV, I'm sure you've seen a story about someone who led a normal life until an unforeseen occurrence turned the lives of their family upside down. Disability is just that kind of life-changing event.

In today's performance-based economy, few Americans feel any real sense of security. The Great Recession has been here for some time now, and the country's growing financial problems do not project a rosy future anytime soon. Unemployment figures have remained high throughout it and despite catchy phrases like "jobless recovery," double-digit numbers here persist.

But disability can be permanent unemployment: when no earned income is projected for the future. Imagine the bills, the loss of a home, of savings, of college funds, of prom gowns, and wedding dresses. No more trips to Dairy Queen after little league games. The stress on a marriage and a family is overwhelming. A lifestyle can be altered overnight.

Consumers simply aren't aware of the disability risk. They receive their medical benefit booklets from work, take them home, place them in a desk drawer and assume they have adequate coverage. Individuals are conditioned to think about medical insurance benefits, but not about what happens to income should an injury or illness extend for a protracted period of time. Doctors and hospitals get paid, but what about your own bills?

Disability Income (DI) sales can often come down to the ability to comprehend and explain the policy definitions. While the need is simple, the actual policy and design can be quite intricate.

Former President Clinton taught us that even the word "is" can be misconstrued, so the language in a DI policy is a veritable minefield of verbal traps. Varying definitions are jam-packed into a dozen or so pages, an array of qualifiers that leave many wondering about the "what ifs" of a disability.

Example: Two people. Same disability. One is a medical sales representative, the other a carpenter. Both are in car accidents, fracturing several bones, and are hospitalized. Each is in rehabilitation, with physical therapy prescribed. The salesperson returns to work within a month, sore, with two separate casts on, but able to drive. The carpenter, though at the same point of recovery as the salesperson, cannot wield the tools of the trade, and the inability to work continues. This will be true for another few weeks.

Disability can be so dramatically different for two people with the same condition or two individuals in the same line of work with different health problems. This is why the language of a disability policy is often intentionally vague. The open-endedness of some of the definitions makes it impossible to answer some of the more specific questions a prospect might ask. This lack of clarity, while frustrating, is well intended. Language that is too precise may not leave any flexibility for allowing a claim to continue if it takes some unexpected path.

DI insurers pay out millions in claim benefits each year. Don't let the indistinct words and phrases put you off the vital task of providing income protection for your clients.

In comparing and evaluating any disability income product, you will have to look at both the price and the policy definitions and features. Looking at premium alone won't help you unless all the features of both plans are identical. Each provision has a cost and it will be vital to sort out the various parameters and definitions of a plan before focusing the price.

There are certain key elements that will be a part of every DI sale, so once you learn the language it will be easier to see the patterns of their usage.

## CHAPTER I REVIEW QUESTION 1 (check answer at end of reading assignment)

(Ref: Chapter I, Page 2, Para 6)

Why is the language of a disability policy so often intentionally vague?

- a. Because the insurance companies are following legal precedent
- b. Because a disability can be so dramatically different for two people with the same conditions**
- c. To allow insurance companies to avoid paying unnecessary claims
- d. The language is not intentionally vague. It is simply part of a legal contract.

## CHAPTER II

### II. THE MONEY PROVISIONS

It's always easier to explain disability income products to people when highlighting the "money provisions" of the contract. These are the policy features that actually have a potential quantifiable claim payout amount.

By explaining the DI policy in this fashion, the prospect can better see the total potential dollars at stake. There's much more to a DI policy than the monthly benefit amount, and focusing on these money provisions illuminates this for the individual.

These product features include:

- Total disability definition
- Residual disability definition
- Presumptive total disability provision
- Waiver of Premium
- Rehabilitation provision
- Automatic Indexing
- Optional features

For example, if a 35-year-old person is considering buying a \$6,000/month disability benefit, with a 90-day elimination period and an age 70 benefit period, the various policy definitions and provisions can now be illustrated with dollar signs, as follows:

Total Disability Benefit Potential:  $\$6,000/\text{month} \times 12 \text{ months} \times 35 \text{ years (age 35 to age 70)} = \$2,520,000$ . That's over \$2 million in potential benefits being purchased.

Residual Disability Benefit: Percentage of that \$2.52 million dollars based on actual earnings loss once claimant returns to work.

Presumptive Total Disability Benefit: \$18,000 (3 extra months in addition to the Total Disability benefit for potential waiver of elimination period.

Waiver of Premium: Savings of \$ \_\_\_\_\_ (annual premium cost x 35 years potential)

Rehabilitation: Cost of rehabilitation program if agreed to by insurer

Automatic Indexing: 3% of \$6,000/month each year for 5 years = extra \$900/month (\$6,000 x 3% x 5). That is \$10,800 per year for potentially 30 more years after indexing, which equals \$324,000.

These are the more common money provisions within a DI policy. What you have done in the illustration above is to replace the language with dollar values. This is the point of the need you are filling. You are providing a funding vehicle to replace income. The bound pieces of paper you deliver in the form of a policy will be transformed into cash at the time of claim. You are merely projecting the dollar potential of this protection.

This makes the premium amount seem more reasonable in light of the benefit potential each policy represents. It's easy to see a \$1,000,000 life insurance face amount and compare it to the premium. It's quite another to see the prospective value of \$2,520,000 from a \$6,000/month policy, but that's the potential dollar amount that could be paid if the insured is disabled within the first year of owning the policy.

Keep this dollar transformation in mind as you study the policy language detailed in the next few paragraphs. While this will show you how the definitions work, it is the bottom line of how much each are worth that must be properly communicated to the prospect.

### III. THE MAJOR PRODUCT FEATURES

#### Renewability

On the face page of the policy you bring back to your client is the contract's renewal provision. This indicates the terms under which the policy will be continued and what strings are attached to both the insured and the insurer. It's important enough to have on the front of the policy, so let's deal with it first.

There are two primary renewal provisions in individual disability income contracts. If your policy doesn't contain one of these two renewal definitions, then the odds are stacked in favor of the insurer, an unnecessary concession.

**Guaranteed Renewable:** Under this policy provision, the insurer is required to continue the policy and its benefits in force as long as the insured pays premiums on time. This provision generally lasts until age 65.

The insurance company does have one option in its potential favor with this provision. It can increase premiums in the future, if it can (a) justify the rate hike to the state insurance department, and (2) rates are raised for all policies within a particular class. Because of this ability to increase premiums, the insurer is able to post lower reserves for this coverage and pass the savings associated with this action along to the customer. Thus, the cost of this renewal provision is less than the non-cancelable version discussed below.

This type of renewal language has enjoyed a renaissance of sorts in the past few years as some insurers, burned by non-can claims results in the 1990s, sought to staunch the bleeding by reintroducing this policy definition that gave them the opportunity to adjust premiums if claims experience went south on them.

There were many who welcomed the return of this provision, where an individual now could choose between this lower-cost (at least initially) feature and the more expensive, guaranteed premium non-cancelable parameter. Historically, this provision has not seen much adjustment in the rates, so agents have a higher confidence level in saving dollars without potential future effect than in say, a long-term care policy.

However, as they say in securities-related transactions, past performance is not indicative of future results, so be sure to properly explain the potential future rate adjustment under a GR policy. These increases aren't automatically scheduled nor are they likely to happen frequently. Actuaries still price the GR plans to last the full renewal period (to age 65), and will only adjust the premiums if experience turns out to be worse than expected.

It does represent a premium savings, however, so be sure and review your choices for a client with that in mind. For example, a person buying a \$5,000/month policy with a 90 day elimination period and an age 67 benefit period with a residual benefit attached could be charged \$2,135 annually for a Guaranteed Renewable policy versus \$2,629 for the same Non-Cancelable plan. In an age where every household dollar matters, this kind of savings could be more important than ever.

**Non-cancelable:** This is the most liberal of the renewal choices. Non-can means, as it does with GR policies, that the carrier must continue to renew the policy for a stated length of time (usually to age 65) as long as the premiums are paid by the insured on time. What sets it apart is that the premium cannot be changed throughout this guaranteed renewal period. Once purchased, the price will stay the same, a guarantee not found in other health insurance-type products.

Because of this guarantee, non-cancelable policies are the most expensive type of continuance provision. But, if one can afford the premium, why not lock in the rate? That the premium you quote in your DI proposal will not change for many years regardless of the insured's health or insurer experience, is certain to appeal to many consumers.

Non-cancelable policies have long dominated (and for the most part still do) the individual disability market. Many are attracted to the rate guarantee, especially if it's affordable. Many agents still emphasize the singularity of the non-can renewability, a buying consideration not available with other forms of disability-related coverage, be it long-term care, major medical, Medicare Supplement or other health insurance-type plans.

What happens with renewability after age 65? People are working longer than ever before today, and even Social Security has raised their retirement age for full benefits to age 67 for many consumers. There are conditions in most policies to continue the coverage. Generally, the individual insured must still be working, must accept a new benefit period (usually 2 year maximum), pay a new, recalculated premium, and may even have to furnish evidence of both

work continuance and income level. There is even some consideration being given to increasing issue ages to recognize the delayed retirement habits of today's older workers, so simply because the renewal provision terminates at age 65, it doesn't mean the coverage must cease.

### Definitions of Injury or Sickness

To be eligible for any monetary benefits under the DI contract, there must be a disability. That seems obvious, but in any event, the insurer must define what constitutes this disability requirement. In DI plans, there are definitions for injury (or accident) and sickness (illness) to satisfy this need. If a person is injured or sick in some way, the disability clock is triggered under the policy and then it remains only to judge the depth of the disability in accordance with other definitions (more on this shortly).

**Injury (or Accident):** This is usually defined as "accidental bodily injury that occurs while the policy is in force." This covers the wide range of accidents that could occur. Even though this is the least likely disability (versus sickness), many prospects have a higher belief in this possible occurrence when considering buying DI because it can be an unexpected event that one can't anticipate. This is easier to justify the purchase of the coverage than considering the possibility of a future sickness.

**Sickness (or Illness):** A sickness is any illness or disease first manifested (makes itself known) while the policy is in force. It includes complications due to pregnancy or childbirth. It also includes normal pregnancy or childbirth after a disability period of 90 days. This definition covers both physical and mental conditions, although the mental portion of this definition could be modified, either in the policy or by a rider, limiting coverage to 24 months, and lowering the price of the policy as a result.

### Definitions of Disability

Arguably the most important words in the contract are the definitions of disability that qualify an insured for claim benefits. An injury or illness triggers the examination of these definitions to see if eligibility can be established and payments made after satisfaction of the elimination period.

The two primary definitions are total and residual disability. These are often separate choices that one can select over the other based on the type of work and income earned and the likely course of one's disability when it happens.

These definitions may also be written together, a more expensive proposition but an opportunity to cover all possible disability contingencies that might arise and often in the most liberal way possible.

## CHAPTER II REVIEW QUESTION 2 (check answer at end of reading assignment)

(Ref: Chapter II, Page 6, Para 6)

Which of the following are the two primary definitions of disability?

- a. Total and Partial
- b. Total and Residual**
- c. Conclusive and Inconclusive
- d. Physical and Mental

## CHAPTER III

### IV. TOTAL DISABILITY

*What it is:* A benefit eligibility provision that measures **physical** ability to perform work after an injury or illness.

*Who should consider:* Employees whose income would not be cut back if they were able to return to work in any capacity following a disability; any working individual whose income would not be affected unless they were fully unable to work; any specialist for whom a disability impairing their ability to work in their field would mean a substantial income setback. This type of policy is used in many group situations.

*Types of definitions:* Generally, most definitions have **two** tests that an insured would have to satisfy to become eligible for disability insurance benefits.

The first test measures your ability to work in your field. This definition language is generally phrased as “the inability to perform the duties of your occupation.” Some policies might say the “substantial and material” duties, or the “important” duties, but it essentially means the same for claims adjudication purposes.

**NOTE:** The “own occupation” definition of total disability under a DI contract has only this one test of total disability. While expensive, there are certain high-earning, specialized professionals (CPAs, pharmacists, architects, executives, some MDs and attorneys) who should consider buying this most liberal definition of total disability available.

The second test can vary considerably. The second test might only be applied *after* a certain amount of time during which only the first test is used to measure disability eligibility, such as 2 or 5 years. Wording of second definitions:

1. You are not engaged in any gainful occupation. This is usually applied together with the first test, but as worded does not force you to work in another occupation.
2. You are unable to perform the duties of any gainful occupation by which you are suited based on education, training, experience and with regard to prior earnings. This is an

ability test based on your projected physical recovery, but wouldn't force you into "any work that exists in the national economy" as the Social Security definition does.

## V. RESIDUAL DISABILITY

*What it is:* This is a definition that mainly measures your loss of earnings after a disability, emphasizing your **economic** recovery rather than just your physical improvement. It may also be called *partial or proportionate* disability.

*Why it's important:* Most disabilities today are generally resolved by a successful return to work, and this definition both encourages a return to work and provides policy benefits that can make that return financially feasible.

*Who should consider:* Any worker who will suffer an income loss upon a return to work and for whom it will take some time to return to the earnings level that had been attained prior to disability. Self-employed, small business people typically fit this description.

*Types of definitions:* Like the total disability definition, this type of policy may have one or two tests to measure eligibility for disability benefits.

The first test measures income loss, typically requiring a minimum 15 or 20 percent loss of earnings following an injury or illness. See "how income is measured" below for more details.

The second test may be a physical one; that is, in addition to the minimum income loss, the disabled policyholder must also be unable to perform one or more of the important duties of one's occupation, **or** be able to perform all of the duties but on a less than full-time basis. Either one will satisfy the second test.

*How income is measured:* When considering this definition, be sure to find out from the insurer how they measure income. Is it cash basis (income when received) or accrual (income when earned, but not necessarily in hand)? What type of records would you have to furnish to validate the income loss? It is better to understand that initially, so that you can advise your clients properly as to what accounting the insurer will ultimately require from them during a claim.

*Other residual definition considerations:*

Prior earnings: Insurers will look back prior to your disability a certain period of time (up to 60 months) to accurately measure your prior earnings. This is a key figure in the income loss calculation. Generally, the longer the look-back period is the better. A choice of a two periods is also generally beneficial to the insured.

Substantial loss of earnings: If the insured loses 75-80 percent of prior earnings after a disability, usually the full total disability monthly benefit paid without the earnings loss calculation.

Minimum benefit: 50 percent of the total disability monthly benefit is paid for the first six months of the claim.

Return to work: Also called a Recovery Benefit, this provision uses only the first test for an initial period of time (12, 24 and 36 months are common) allowing the insured to work full-time for a period and still be eligible for benefits based on earnings loss only. Some DI carriers have a “full” recovery benefit where this is an earnings-only test for the full benefit period.

While this seems like a lot of definitions to digest, these are necessary in order to compute lost earnings. Otherwise, how would it be established? An example will help see the importance of this before we define the variables.

As you study this chart, you should notice the incentive built into this policy feature to encourage as early a return to work as feasible.

Month	Prior Earnings	Current Earnings	Loss of Earnings	X	Total Disability Benefit	=	Residual Disability Benefit
1	\$5,000	\$ 500	90%		\$3,000		\$3,000
2	\$5,000	1,000	80%		3,000		3,000
3	\$5,000	1,500	70%		3,000		2,100
4	\$5,000	2,000	60%		3,000		1,800
5	\$5,000	2,000	60%		3,000		1,800
6	\$5,000	2,500	50%		3,000		1,500
7	\$5,000	2,750	45%		3,000		1,350
8	\$5,000	3,000	40%		3,000		1,200
9	\$5,000	3,250	35%		3,000		1,050

What are the variables in the above calculation? There are: prior earnings, current earnings and loss of earnings.

If the insured was totally disabled, the benefit payable would be \$3,000/month. If the individual returns to work, as most desire, the total money coming into the household is now the current earnings plus the residual disability benefit that is computed. In month four of our example above, that equals \$3,800 (\$2,000 current earnings plus \$1,800 benefit), or \$800 more than the total disability benefit is paying. There is no penalty for going back to the job. In actuality, the established formula ensures that the individual will always end up with more money by returning to work.

There are many variables to the residual disability benefit. But they are necessary to properly assess income loss and fairly pay disabled insureds the money they are due.

### Other Policy Provisions

Naturally, there is much more to a disability income policy than total or residual disability definitions. There are several other important parts to a policy, some of which have already been labeled above as “money provisions.”

#### **VI. ELIMINATION PERIOD**

This is the number of days that an insured must meet the definition of total (or, when present, residual) disability before benefits will commence. In some DI plans, it is referred to as the *waiting period*.

You should read your DI policy carefully to see what days of disability count towards the elimination period. Generally, if the insured purchases both total and residual disability as definitions in the contract, either of those types of disability days will count.

There may also be the opportunity in the contract to accumulate days towards fulfilling the elimination period. With many plans having 90-day elimination periods now, this could be more important. For example, if an individual is disabled under the policy for 50 days and then recovers, that person is still 40 days short of qualifying for benefit payments. Let’s say following the return to work that, within two months, the insured is disabled again from the same medical condition. The accumulation provision (usually found in the policy under the paragraph entitled *recurrent disability*) allows the claim to resume at day 51 rather than start over as it recurred within a six-month period, a distinct advantage to the claimant.

#### **VII. PRESUMPTIVE TOTAL DISABILITY**

Disability of a catastrophic nature will create problems for an insured and family. In some cases, the DI insurer will loosen the reins a bit in its requirements to prove total disability. These concessions, and what initiates them, can be found in the presumptive total disability definition in the contract.

In general, if the insured has experienced the total, permanent and irrecoverable loss of hearing, or sight, or speech, or the use of two limbs, then the insurer requires no other proof of disability. This supersedes the other disability definitions in the contract. What makes this a money provision in the policy is that the elimination period is usually waived as well. This means, with a 90-day elimination period, an extra three months of benefits. Since you know the amount of the total disability monthly benefit, this number is easily quantifiable as an additional benefit.

Some insurers have made this clause a detached benefit in the policy paying a *separate* monthly benefit or lump sum *in addition* to the total disability monthly benefit. In any event, this money provision recognizes that such disabilities as included in this contractual language are serious and will result in substantial financial hardship for the disabled insured and family.

### CHAPTER III REVIEW QUESTION 3 (check answer at end of reading assignment)

(Ref: Chapter III, Page 7, Para 1 and Page 8, Para 2)

What are the primary factors that distinguish Total Disability from Residual Disability?

- a. **Economic versus Physical**
- b. Elimination Period versus Concurrency Period
- c. Recurrence Period versus Accumulation Period
- d. Physical versus Mental

## CHAPTER IV

### VIII. AUTOMATIC INDEXING

Many DI policies include an inflation adjustment in their policies to help the monthly benefit keep pace, at least initially, with inflation. The increase to the monthly benefit occurs annually and is usually valid for the first five years. The insured need do nothing other than pay the additional premium (benefit increases are calculated at attained age rates) for the extra coverage.

Here is an example of how this provision works:

<u>Year</u>	<u>Monthly Benefit</u>	<u>% increase</u>	<u>New monthly benefit</u>
1	\$6,000	3% simple	\$6,180
2	6,000	3% simple	\$6,360
3	6,000	3% simple	\$6,540
4	6,000	3% simple	\$6,720
5	6,000	3% simple	\$6,900

In this example, the indexing factor used was a simple increase of 3 percent annually. Some DI insurers tie the indexing to the CPI increase, with no guaranteed rate, while others have lower or higher guarantees. Some indexing is also done on a compounded rather than a simple basis.

This feature was instituted to help policyholders keep their benefit levels within reasonable distance of their incomes. Many people receive raises each year, but don't equate that with a need to increase their income protection under DI coverage. This makes it easy – the insured doesn't have to think about it – only pay the premium for the additional coverage.

As you can see from this example, this provision can increase the benefit amount considerably over time. If no one paid attention to the upward changes in an insured's income, the policyholder in the 5<sup>th</sup> year would still have a \$6,000/month policy rather than the 15 percent higher level (\$6,900) that the automatic increases facilitated.

The insured has the right to refuse an increase and not pay the additional premium for it. Usually there is a limit to the refusals (two is most common) before the provision is suspended and no more automatic increases are made.

At the end of five such increases, the insured must furnish the insurer with financial evidence that justifies the increases that have been made to date. In our example, the individual would have to show tax returns that substantiated the new benefit level of \$6,900. If the evidence was sufficient, the index feature would renew for another five years (depending on age). If not, the \$6,900 would stay at that level but there would be no new increases. No medical evidence of insurability is ever required.

## **IX. REHABILITATION**

In the late 1970s, following the widespread introduction of the residual disability benefit in the individual disability market, a new policy provision was added to many contracts – rehabilitation. This feature was offered in the same spirit as residual, emphasizing a return to work and signaling a willingness on the part of the insurer to help with this process if it made sense for all concerned.

Medical technology was also improving dramatically at that point, and more people were considered targets for recovery following a major disability rather than being permanently disabled or worse.

This also plays into the usual claimant psychology. An insured who is totally disabled generally wants to return to work. The residual disability benefit encourages this financially as already illustrated. The rehabilitation clause further advances this cause by helping to retrain a disabled person to help effect that return.

The policy language is typically vague, stating that if all parties agree, the insurer will pay for the reasonable expenses of a program of occupational rehabilitation. These expenses can include assessments, examinations, vocational testing, training programs, books, tuition and even living expenses *in addition to* the total disability monthly benefit. Thus it is another of our money provisions.

Generally, the carrier will not place a dollar limit on this offer, but will make the overall decision about funding the costs of the program based on their opinion that it might change a total disability claim into a residual one or, even better, a full financial recovery, thus ending the claim.

An example illustrates the types of costs and savings involved. If a disabled insured has a \$6,000/month total disability benefit, payable to age 67 and is disabled from performing his occupation at age 40, the benefit payout, if nothing changes, is \$1.95 million if the monthly benefit amount remains level. If the claimant is willing to undergo rehab with the opportunity to work at a new job where residual disability calculations will take over, the expenses to be reimbursed under the contract are relatively minor in comparison.

If the program costs \$20,000, and the insured is back to work within two years and earning income again, the ultimate savings to the insurer could be a million dollars or more. That's worth every cent

of rehab coverage to them. For the claimant, it is a cost-free opportunity to be a productive member of the working world again. Don't underestimate what this means to people psychologically. The majority of people are going to jump at this opportunity.

This feature has seen a growing utilization over the years. Claim departments today are now fully staffed with rehabilitation specialists coordinating just such endeavors on behalf of both insurer and insured. Emphasis on this provision is not without merit.

#### **X. WAIVER OF PREMIUM**

This provision is built into the contract, unlike life insurance where it is an optional benefit. It addresses the situation where an individual is disabled and unable to earn an income but is still required to pay a premium for this disability income policy.

Obviously, that doesn't make much sense, so insurers built in a premium waiver after a stipulated period of time, usually 90 days or the elimination period, if longer. At that point, future premiums coming due are waived as long as the individual remains disabled under the terms of the contract. In addition, any premium paid during the initial 90 days (or elimination period, if longer) is refunded to the claimant.

If a policy includes both total and residual disability definitions, either or both of these types of disability days can satisfy the time period before waiver is triggered. It is another money provision that you can quantify by determining the potential refundable premium.

Understanding how the Disability Income policies work is important so that you can explain them properly to a client and design the policy and features that best fit their needs. Highlighting the "money" provisions will go a long way in accomplishing this task.

#### **CHAPTER IV REVIEW QUIZ – QUESTION 4** (check answer at end of reading assignment)

(Ref: Chapter IV, Page 11, Para 3)

The Automatic Indexing feature was instituted to help policyholders

- a. keep their premium levels within their budgets
- b. keep their benefit levels near their income levels**
- c. automatically increase their benefit limit each year
- d. reduce the elimination period each year

## **CHAPTER IV REVIEW QUIZ – QUESTION 5** (check answer at end of reading assignment)

(Ref: Chapter IV, Page 13, Para 2)

Once the premium waiver goes into effect future premiums coming due are waived as long as

- e. the individual remains disabled under the terms of the contract**
- f. the individual maintains at least 50% disability
- g. the individual passes the medical insurability test
- h. the individual remains disabled but works a minimum of 20 hours per week

## **CHAPTER V**

### **XI. UNAUTHORIZED ENTITIES**

Unauthorized entities engaging in insurance are a serious and growing problem in Florida for consumers and agents. Consumers are substantially harmed with these entities failing to pay claims and defrauding through deception. Agents are unwittingly (sometimes knowingly) representing these entities and placing clients and themselves at risk. Florida law is violated under the guise of these unauthorized entities claiming to be ERISA exempt or some type of association plan that claims to not be insurance or to be exempt from Florida regulation. All of this is simply not true! This is a problem in the state of Florida and other states.

The problem of unauthorized entities selling unauthorized products originated in the health insurance arena, although the problem now seems to be spreading into property-casualty arena as well. These unauthorized entities promised low health insurance premiums, a promise fueled by skyrocketing health insurance premiums with legitimate health insurance carriers. In the current market, low health insurance rates just do not exist. The public and certain agents, apparently, were ripe for the picking by these scam artists. Remember, these are scams and the intent is to collect as much premium as possible without having to pay claims, or very few claims.

Unsuspecting licensed insurance agents are also vulnerable to this type of scam because representatives of the unauthorized entity will contact the licensed agents and send them (or give them in person) printed marketing materials touting the unauthorized entity and their bogus products which, again, gives the impression of legitimacy and credibility.

Maybe the agent is asking too many questions of the representative – is just a little too inquisitive – about who they are, where they're located, how long they've been in business, etc. The agent may even question the legitimacy of the product. Some of the scam artists are telling agents that their products do not have to be authorized by the Department because the plan is an ERISA plan, or that the plan is part of a MEWA (multiple employer welfare arrangement) or it's to be sold to labor unions – all the while stating that under any of these previously-mention circumstances, the products do not have to be approved or authorized by the Department.

The representative of the unauthorized entity might say, “It doesn’t require approval, because this is an ERISA plan.” Or, “It doesn’t require approval because this is plan is part of a MEWA plan.” Or “This plan doesn’t require approval because it’s for labor unions.” None of this is correct! Any product which contains an insurance component is required, by law, to receive authorization of that component by the Department before it can be sold in Florida. Any legitimate company representative who approaches you about selling and representing their products should not mind the scrutiny you put them under by verifying their status with the Department.

**626.902 Penalty for representing unauthorized insurer:**

(1) In addition to any other penalties provided in the insurance code:

(a) Any insurance agent licensed in this state who in this state represents or aids an unauthorized insurer in violation of s. 626.901 commits a felony of the third degree, punishable as provided in s. 775.082 or s. 775.083.

(b) Any person other than an insurance agent licensed in this state who in this state represents or aids an unauthorized insurer in violation of s. 626.901 commits a felony of the third degree, punishable as provided in s. 775.082, s. 775.083, or s. 775.084.(2) In addition to the penalties provided for in subsection (1), such violator shall be liable, personally, jointly and severally with any other person or persons liable therefore, for payment of taxes payable on account of such insurance under s. 626.938.

Agents or any other persons are prohibited from representing or aiding an unauthorized insurer. If an agent or any other person represents an unauthorized insurer, they are subject to severe penalties, including possible civil and criminal action. Agents are subject to suspension or revocation of their licenses and/or monetary penalties for violation of the unauthorized insurer law. Agents can be held liable for claims and losses not paid by unauthorized insurers. Agents who represent or aid an unauthorized insurer commit a felony of the third degree.

Don’t be fooled by phony products that sound too good to be true! Investigate before you sell or buy these plans. Check to see if an entity or plan is an authorized insurer by calling the Department of Financial Services at 877-693-5236 or 850-413-3089.

**CHAPTER V REVIEW QUIZ – QUESTION 6** (check answer at end of reading assignment)

(Ref: Chapter V, Page 14, Para 2)

The problem of unauthorized entities selling unauthorized products originated in which segment of the insurance and financial services industry?

- a. Property and Casualty
- b. Life insurance
- c. Stock market
- d. Health insurance**

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**CHAPTER REVIEW QUIZ ANSWERS:**

1. B
2. C
3. A
4. B
5. A
6. D