How Critical Illness and Disability Insurance Fit Together in a Wealth Plan

Our greatest and most valuable asset is usually ourselves. Our human capital – both intellectual and physical – allows us to earn a livelihood, and live the life that each of us chooses. But when a severe disability or illness strikes, it may impact our ability to earn a living and continue with our daily lives as we did before. Insurance is all about managing this risk and is a valuable strategy to protect our income earning ability and well-being, both personally and financially.

A disability or a critical illness such as cancer, heart attack or stroke can profoundly affect one's daily living activities, but it also could have a devastating impact on finances and a financial plan. Without income protection or an emergency fund to cover costs for treatment or care, one would likely have no choice but to alter their finances and possibly access long-term savings that were designated for other goals, putting those priorities at risk as well.

There are two types of insurance that can protect one's earning ability, and provide financial assistance to help recover from an illness, disease, or disability. Disability and critical illness insurance will both pay a benefit in the case of an illness or disability, but under different circumstances. Disability insurance provides a monthly income if you're unable to work due to a disability, including an injury, serious illness or mental health issue. Critical illness insurance pays out a lump sum after the diagnosis of one of several illnesses or diseases covered by the policy.

So, is one better than the other; does one replace the other; or which one is right for you? Both serve different purposes and could fit into a well thought out wealth management plan to provide protection. In this report, we'll focus on what critical illness and disability insurance are and how they work, and then focus on how they can work together to provide protection and peace of mind for the future.

Critical illness insurance

Critical illness insurance pays out a lump sum amount to the policy owner if diagnosed with one of a specific list of illnesses and the individual survives for the prescribed qualification period, usually 30 days, or in the case of most cancers, 90 days. Upon confirmed diagnosis of a critical illness – and there are several covered by plans from leading insurance companies – the policy owner is paid a tax-free lump sum benefit which is equal to the amount of insurance purchased. Receiving this tax-free benefit doesn't affect the amount of disability benefits you may also be receiving from disability insurance coverage. You may choose to use the benefit to pay off your mortgage; supplement an income of a spouse or partner who takes time off to help support you; for specialized medical treatments; or to provide funds to sustain operation of a business while you are away and recovering. Once the claim is approved, you may use the funds however you choose to meet your needs.

Most policies cover a variety of major illnesses or diseases, the following are some of the illnesses that are usually covered. It should be noted that in order to receive the funds, the insured must meet strict and specific definitions of the illness as well as stringent requirements for a survival period after being diagnosed.

- Heart attack
- Stroke
- Coma
- Alzheimer's disease
- Blindness
- Occupational HIV injury
- Parkinson's disease
- Multiple sclerosis
- Major organ transplant
- Severe burns
- Loss of limbs
- Motor neuron disease (ALS or Lou Gehrig's Disease)
- Cancer
- Kidney failure
- Paralysis
- Deafness
- Loss of speech
- Coronary artery disease requiring surgery

Many critical illness plans can be designed to refund all or part of the premiums paid after a certain period of time, if no claims are made.

Disability insurance

Disability insurance protects your ability to earn an income, especially if you or your family are dependent on that income to meet your daily living expenses. Many employed individuals have disability insurance through their group benefit plans from their employer. Typically, such a plan will pay you a set portion of your monthly income if you are unable to work. Payments end when you start working again, reach age 65, or die. Coverage differs greatly from one employer to another, and if you're self-employed or you work for a company that doesn't have coverage, you may want to consider a private disability insurance plan.

A disability insurance plan will either cover you for "any occupation" or "own occupation." Qualifying for a benefit under a plan with an "own occupation" definition means the inability to work at your regular job. Where the definition is "any occupation," there will be no benefit paid if the insured has the ability to perform the duties of any job. Disability insurance payments from an employer plan are usually taxable, while those from a private disability insurance plan are usually tax-free.

Why they complement and not replace one another

If you don't have either disability or critical illness insurance and you have to choose between the two, you may want to consider disability insurance first. In the event of any illness or accident that prevents you from working, your disability payment will provide you with funds to continue meeting your daily expenditures. If you already have sufficient disability insurance coverage through your employer, you may want to consider critical illness insurance to complement your existing disability coverage should you happen to unfortunately encounter one of the specific illnesses covered by your plan. The critical illness insurance provides money to help pay for expenses beyond those covered by government or your employer health plan. It can also help someone manage the financial hardships that come with a critical illness diagnosis such as the cost of medical treatment, physiotherapy, renovations, home care, or for a spouse to take time off work to provide support.

There are situations where critical illness insurance may buffer for disability insurance. For instance, it may be particularly appropriate for people who are out of the workforce and therefore cannot obtain disability insurance, such as stay-at-home parents. If you are not earning an income and therefore unable to obtain disability insurance, consider critical illness insurance to cover additional costs that could arise if diagnosed with a serious illness or disease. Also, what if you're a caregiver for children or someone who is dependent on your support, and you become critically ill such that it affects your ability to continue providing care? A comprehensive critical illness policy could provide funds to cover payment to someone to perform those caregiver duties in the interim or for a short period of time until alternate arrangements are made for caregiving.

Conclusion

Critical illness insurance can help to alleviate financial worries when you are focusing on recovery, while disability insurance is designed to replace a portion of your income in the event you become disabled due to accident or sickness. Together, these two types of insurance can complement each other in a wealth plan that is tailored to protect you and your family's well-being.

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For more information, speak with your BMO financial professional who will refer you to an Estate and Insurance Advisor (Financial Security Advisor in Quebec) from BMO Estate and Insurance Advisory Services.

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