

# Situation Critical

Michael Berton – Advisor's Edge – February 2002

**More Canadians are overcoming diseases and illnesses that were fatal 20 years ago. Critical illness insurance can come to the financial rescue.**

Dr. Steve Kilmer (not his real name) thought he was adequately insured, until he was diagnosed with cancer. A successful dentist, he relied on his financial planner to advise him about covering his risks. He and his planner believed he was well insured between his personal life and disability insurance and business overhead insurance. Now at 55, he was facing one of the most frightening experiences in his life and he wasn't sure his insurance coverage would serve his most pressing need.

Steve wanted to begin the recommended radiation therapy immediately, but in his provincial medical system he was going to have to wait in a queue. His doctor told him that he could get the treatment without a wait if he were prepared to travel to the Mayo Clinic in Rochester, New York. But that decision came with a cost. Where would he find the money? Indeed, it seemed that although he was paying for all kinds of insurance, his current needs had somehow "fallen through the cracks." To get the medical attention he wanted, Steve would have to dig deeply into his retirement savings.

Steve decided to travel to the Mayo Clinic for radiation therapy. For six weeks he went to daily treatments. This resulted in a medical tab of CDN\$50,106, plus an additional \$21,296 in expenses for food and lodging. He returned home with instructions to stay off work for another four months. At this point, he had already missed nine weeks from his busy dental practice. To maintain his business, he had to hire a locum to replace him at a cost of \$3,500 per week. As this is more than the practice normally can afford, he cannot draw any income for some time. Steve will incur more than \$200,000 in expenses over his six months off work.

Fortunately his disability and business overhead coverage will help. Under the terms of these contracts (see "Surplus or Shortfall?" at the bottom of this page), Steve can expect to begin receiving a monthly tax-free income of \$6,400 by the end of the third month as well as up to \$10,000 in office cost reimbursements by the end of the second month. The initial three months of his cash flow and business operating expenses are a very real problem, and he will have to withdraw funds from his long-term savings. As these are registered, the cost of redeeming these assets is close to double after tax.

A simple \$150,000 critical illness (CI) policy would have served Steve well in this emergency. The payment would have covered all of his immediate costs, and would have taken a great deal of pressure off his disability income at the same time. Barring any other complications, Steve would end up with a surplus of \$73,067. Rather than raiding his long-term savings to fund his medical costs, Steve could actually contribute to his savings, protect himself in the event of a relapse, reduce his re-entry workload for a short time or reduce some nondeductible debts. Although much has been said and written about the virtues of critical illness insurance in recent years, many advisors continue to overlook or ignore this essential planning tool to the peril of both their clients and their own practice.

Odds are that your clients have a better chance of suffering a catastrophic health issue than death. Canada Life statistics indicate that one in four Canadians will contract some form of heart disease, one in three Canadians will develop life-threatening cancer, more than 50,000 Canadians will suffer a stroke annually and a similar number will have multiple sclerosis. Interestingly, recent claims figures from five insurers quoted in *Insurance Journal* (September 2001) show that a majority of claimants are between the ages of 36 and 50; 62.6% are male. An unexpected critical illness represents the most likely risk to your client's financial plan.

Most advisors have been trained to evaluate the appropriate amounts of life and disability insurance coverage for their clients. While CI has elements of both of these, it functions quite differently. As a result, the determination of appropriate coverage for a critical illness is difficult to estimate and many advisors are uncertain about the level of insurance they should recommend. "The amount of coverage has to be based on your client's current financial situation and expectations for recovery," says Scott Furness, a registered health underwriter and living benefits marketing consultant at PPI Financial Group in Vancouver. "You must consider the costs of the initial medical impact, the ongoing financial impact, and lifestyle costs the client may wish to cover."

Possibly the best way to estimate coverage is to construct an emergency cash flow scenario to see what would be required in that client's individual situation. There are several areas to consider.