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Reduce group disability plan litigation risk with two simple steps

Written by Rona Birenbaum, financial planner, Caring for Clients on Wednesday, April 27th, 2011 at 6:20 pm



Group medical benefits programs are an invaluable part of a total compensation package for employees and can serve as a safety net if there is ever a serious health situation.

Despite these benefits, there are financial risks for any employer who provides group health benefits. Here's an example of one such case:

A business owner's 40-year-old employee was left disabled from a serious car accident. The owner is thankful that disability benefits were included in the company group medical benefits plan. But he is shocked to find out that the company — and the insurance

company — is being sued by the disabled employee for an additional \$2,000 per month.

How can such a valuable employer benefit end in a lawsuit?

If an employee is fully disabled for the rest of their working life, the disability benefits can easily exceed \$1 million. In spite of the value of the coverage, and its financial importance in the event of a disability, most employees have a limited understanding of how the coverage would work for them in the event of a claim. Many will not be aware of insurability requirements for disability benefits.

A number of insurers are building in insurability requirements to be eligible for the maximum benefit under the plan. A basic amount of coverage is in place without medical evidence. The basic coverage amount can be much less than the employee is eligible for based on their salary level. This is one way that insurers and employers keep plan costs under control. Medical evidence must be submitted by the employee and assessed by the insurer before the maximum benefit is approved.

For example, a recent plan that I reviewed had the following features:

- | Benefit: 66.67% of monthly earnings rounded to the next higher \$1
- | Maximum Benefit: \$5,000/month
- | Benefit Period: Age 65
- | No Evidence Limit: Evidence of insurability is required for amounts in excess of \$3,000.

So, based on the above limits, once a member of the plan, the employee automatically qualifies for 66.67% of salary coverage until their salary exceeds approximately \$54,500. Unless they provide evidence of insurability, once they pass this income threshold, they will not be eligible for the maximum benefit under the plan. It is capped at \$3,000.

I asked the client that is a member of the above plan how much disability coverage they have through work. They answered, "two thirds of my salary from what I recall". This client earned \$75,000 and thought that he was covered for about \$4,200 per month. He was shocked to find out that at best he would get \$3,000 because he had not provided evidence of insurability when his salary was increased beyond \$54,500. He was incensed that his employer did not notify him of the requirement.

Employers may feel that giving a new employee the benefits booklet fulfills their obligation to educate and inform. I think that there is a risk that an employee could sue their employer if they were not notified when evidence of insurability became necessary to access the maximum coverage amount. The cost of defending such a suit is reason enough to put safeguards in place.

To reduce the risk of employee frustration and possibly litigation, business owner clients should do the following two things:

1. Have each employee sign an acknowledgement that they have read and understood the benefit program features and benefits.
2. Where insurability requirements are triggered by a compensation threshold, ensure that employees are notified when they attain the relevant thresholds. Keep evidence of the notification on file.

With these steps an advisor and employer can help encourage employees to spend more time reading through their plan documentation so they fully understand what their benefits are should a serious accident occur. Being diligent with notifications can also reduce the business owner's risk of lawsuits.

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