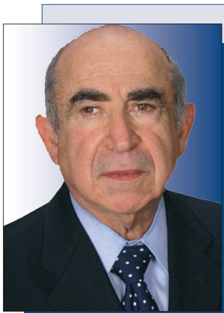
Disability Insurance Insights…



EUGENE COHEN

began his insurance industry career in Cleveland, OH, with a company that specialized in disability income protection.

In 1981 Cohen founded the Eugene Cohen Insurance Agency, Inc., Skokie, IL, which specializes in DI, life, LTCI, fixed annuities, and impaired risk cases. The agency is a member of LifeMark Partners, NAILBA, the IDIS and is a founding member of The Plus Group.

Cohen received the W. Harold Petersen Lifetime Achievement Award from the IDIS and NAILBA's Douglas Mooers Award for Excellence.

MICHAEL COHEN,

CLU is president of the Eugene Cohen Insurance Agency, helping brokers, general agents, broker/dealers and financial advisors serve their clients.

Cohen has served on carrier advisory boards and organization boards of directors. He is a member of the Risk Appraisal Forum.

*Eugene and Michael can be reached at Eugene Cohen Insurance Agency, Inc. Telephone: **800-333-4340**. Website: **www.cohenagency.com**. Emails: **michael@cohenagency.net**; **eugene@cohenagency.net**.*

BOE: That Was Easy!

The "Aha!" moment. If you are like us, we're sure you love the feeling you get when you find a solution to a problem or understand a certain product. The light bulb goes on, the excitement builds—it's that feeling that "this makes a lot of sense." That's the feeling we are told advisors get when they understand the tremendous need for BOE insurance.

BOE

Yes, another insurance acronym, which stands for Business Overhead Expense disability insurance. There may be some variations of name with different companies, but most call it BOE.

The Basic Idea

A business owner client has a prolonged sickness or injury that causes a disability and loss of work. Being the business owner, your client is still fully or partially responsible for the monthly bills and expenses of the business. A BOE disability policy is intended to create a reimbursement for those qualifying expenses.

The Market

A small business owner or professional (physician, dentist, attorney, accountant, etc.) that is ultimately responsible for paying the expenses and the employee payroll of the firm. Typically, the firms that are most susceptible to the perils of a disability would be the smaller firms in which the revenue created is dependent on the owner's ability to work. One of the key underwriting criteria will be the need for the coverage. Will the firm lose significant revenue if the owner becomes disabled? In many cases it's very obvious. For example, if a lawyer, physician, accountant or dentist has six employees and can't practice due to an injury or sickness, then the primary revenue creator is no longer creating the required revenue. If a business has a large amount of employees, say a restaurant owner of an upscale restaurant, it may be more difficult to prove a revenue loss if the owner becomes disabled. If a firm has multiple owners, then the underwriter may ask to see the operating agreement to see if there is an allocation of expenses clause or something that would indicate each owner is independently responsible for the expenses of the firm.

The Need

The owner of a business will either personally or corporately obligate themselves to pay the overhead expenses of a business. This is part of the risk and reward trade off of being a business owner as opposed to an employee. The business owner assumes more risk but can reap more rewards in return. Most business owners do not take into account the risk of becoming disabled and how that would affect their business, personal income and net worth.

Disabilities come in different shapes and sizes, but there will be a time in which the business owner will need to make a decision to continue, sell, or close down the firm. Each scenario can be different, but you can only imagine the mental anguish of trying to recover from an injury or sickness and also making life changing decisions for not only the business, but also all the dedicated employees of that business.

Take a successful attorney, physician or dentist that has five employees: Two medical or legal assistants and three office personal (front desk, secretarial /insurance filing/bookkeeping, and other clerical duties). If the revenue creator becomes disabled, which employees are kept on and which are let go? Now add some more elements, such as highly trained employees that have developed intimate knowledge of the business. It can take years to train employees on various aspects of a business—working with insurance companies, vendors, preparing the books, maintaining a database, website, and so much more. Most owners would not want to close down the practice and layoff highly valued employees if the owner feels or is told that they should be able to get back to work in the "near" future, say a year or two.

In addition, the business owner has obligated themselves for being responsible for other business expenses. It's not uncommon to have a long lease, leases that last five years or longer. In addition, some office space leases require a share of the property taxes and common expenses be paid as well. The business owner also has to maintain other common business insurance, such as: Liability insurance, workers' compensation insurance, malpractice insurance, property insurance, and health and other employee benefit types of insurance. There are other common expenses as well, such as utilities, office equipment leases for copy machines and other office equipment, computers, business software, professional dues, and postage among the many type of monthly obligations. In addition, most business owners still need other professional services that need to continue such as accounting, computer/network maintenance, and legal services to name just a few. Just reading about all these expenses can be overwhelming. Now imagine a successful client that survives a bad car accident and requires corrective surgeries and/or months, if not years, of rehabilitation. What about the client that is diagnosed with a potentially fatal form of cancer but needs to go through years of treatment before the final outcome is really known?

The Loss to the Business Owner

Eventually there will be a crossover point in the business in which the loss of revenue caused by the disabled owner will create a perilous situation for the business. For a business to create income, the revenue must exceed the expenses. If the primary revenue creator and business owner is disabled, there will be a loss of revenue. At a certain point the business owner will be forced to pay the expenses of the business out of personal savings, start to trim the expenses of the business or, even worse, shut down the business. While some may say the business can be sold, the value of a service business typically will diminish very quickly without the primary revenue creator involved. The longer the disability, the more patients and clients need to seek services elsewhere resulting in even a greater loss of value. What about hiring a person to fill in for the disabled owner? While that may be possible, it's unlikely for several reasons. The success of the firm is usually based on that revenue creator but, even so, the firm would need the "right" person. Who is going to do the professional search and conduct the interviews? It can take years to find the right person or associate. In addition, even if the right person is found, adding a new professional increases the firm's expenses tremendously. In addition, restarting a flow of revenue will have a natural delay and may be less then previous receipts. Also, the cost of a professional with the same duties as the policyowner may be an excluded expense in the BOE policy.

The Policy

Most BOE policies will usually have similar features: A waiting/elimination period, usually 30,60, or 90 days, and a benefit period, usually 12, 18 , or 24 months. A BOE policy will vary from an individual disability policy in that the monthly benefit is paid as a reimbursement of qualified expenses. In addition, there is usually a provision indicating that any monthly benefit that is not claimed in the request for reimbursement may be used later so it is not lost. For example, a client has a $10,000 per month BOE policy and a 12 month benefit. If the client has a qualifying disability and has $5,000 of reimbursable expenses, then the policy benefits may last for 24 months instead of just the 12 months. Please review the definitions and insuring agreement of any BOE policy you may propose, as policies can vary.

The Taxes

We don't provide tax advice and your client should seek individual counsel for their particular situation. In general though, it's typically accepted that the premium for a BOE policy is usually treated as a business expense. In addition, the reimbursable nature of the policy usually creates an offset of income and expenses which would normally result in a non-taxable event.

Most likely you have clients in your advisory practice that need this type of policy. Now it's up to you to educate them as well.