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Real Money

Serious illness can trigger financial misery

By Diana Clement

Kiwis insure lives but ignore risk of disability and the cost this entails.

People believe disability will be from an accident but statistically it's more likely to be from an illness such as a stroke or cardiovascular event.

Death brings financial disaster for many families. If the breadwinner dies without adequate life insurance, the family can be left to struggle on benefits.

They might be emotionally better off but financially in a deeper hole if the breadwinner survives illness or injury but is too disabled to work.

Mostly, in the absence of any kind of insurance payout, financial misery ensues.

Russell Hutchinson, a director of financial services management firm Chatswood Consulting, did the figures for a family with children.

In the event of death the surviving partner, if not working, could get Sole Parent Support - aka the DPB - until the youngest child was 14.

If, however, the breadwinner was disabled by some misfortune, the family would be entitled only to a Disability Allowance and Job Seeker Support, which Hutchinson worked out was nearly $100 less a week than the DPB.

"Disability means less support than death for your family, plus they have to pay to look after you," says Hutchison. This is a very important point. Hutchinson has seen cases where families have had to spend more than $50,000 on house alterations as well as buy modified cars, mobility scooters and other aids. The disabled former breadwinner also needs to be clothed and fed.

That's assuming the able-bodied partner doesn't just up and leave. It happens, says Hutchinson. One member of a couple becoming disabled can be very hard on a relationship and sometimes love is found elsewhere.

When buying insurance, we're much more likely to focus on death and ignore the spectre of disability. This can leave people in sticky financial situations, says Conor Sligo, general manager at LifeDirect.

If you want to know what you might get from Work and Income in the event of a partner dying or being disabled by illness then check out its handy calculator at tinyurl.com/WINZcalculate.

I entered details for a hypothetical family and assumed that the main breadwinner was disabled, the partner wasn't working, the mortgage was $800 a week and there were cash assets over and above the house of $50,000.

The weekly "Supported Living Payment" it estimated was $214.79, plus an accommodation supplement to cover some or all of the mortgage, but not living expenses. Not much to replace a breadwinner, although there would be a small disability living allowance to cover some of the additional costs of being disabled.

One thing that occurred to me when I was doing the Work and Income calculation was that it took into account dividends. If part of your retirement plan was to reinvest dividends as you get them, then this isn't going to happen. They will need to be taken into account in Work and Income payments.

These Work and Income figures are a real eye-opener. Yet more of us insure our possessions than ourselves, according to research carried out in 2011 by Nielsen for the Financial Services Council.

One of the main reasons we don't insure against disability, according to the survey, is that people believe disability will happen as a result of an accident and ACC will pay out 80 per cent of their wage for the rest of their working lives. But statistically, says Hutchinson, we're more likely to be disabled through illness. According to the Stroke Foundation, strokes are the leading cause of serious adult disability in New Zealand.

In the case of a stroke, cardiovascular disability or other illness ACC wouldn't pay.

"You qualify for naff-all [from Work and Income] and [yet] need $50,000 of capital expenses on the house," says Hutchinson. "It is brutal."

There is always the "it won't happen to me" belief. Yet Hutchinson says that someone aged 28 has about a 5 per cent chance of becoming "TPDed" - suffering a total permanent disability - in their working life, and there is a 9 per cent chance it could happen to either partner in a couple of the same age.

The fallback, says Sligo, is one or more of three types of insurance: income protection/mortgage repayment protection, trauma, and TPD. Income and mortgage protection provide regular payments for a period of time to cover a percentage of income or the mortgage payments.

Total permanent disablement cover is usually a lump sum payout if you're disabled. But be warned, the insurance company will argue tooth and nail that you are capable of work.

Trauma insurance pays a lump sum if the policy holder is diagnosed with certain diseases such as cancer or stroke.

Lump sum payments can be extremely useful for someone who does become disabled.

Sligo says some of the most common uses of trauma claims money are to:

• Pay for medical expenses not covered by health insurance

• Travel overseas for medical treatment

• Pay off mortgages, credit cards and other debt

• Reduce work hours and

• Bring family from overseas to help.

Only 16.5 per cent of the people surveyed for the Financial Services Council had income protection cover and the numbers for trauma and total permanent disablement are also low.

Yet 57 per cent of the people surveyed by Nielsen said they would encounter financial difficulty if the first income earner suffered a long-term illness.

More than half of the respondents were suspicious of insurance companies, leading to their reluctance to take cover.

There were also issues about comprehending the insurance cover and understanding the jargon from 43 per cent of respondents. I can understand that. Every time I use jargon such as "TPD" and "trauma" I have to think - now what does that cover? - even though I come across the words regularly.

It's no wonder people confronted with the terms for the first time go blank and put the issue of insurance in the too-hard basket before they even think what the cost of premiums might be.

Even those of us who have some cover are often under-insured, says Peter Neilson, chief executive of the Financial Services Council.

A common mistake, he says, is that husbands and wives don't understand the cost of replacing each other's roles.

The story isn't quite as bad as it sounds. Many families with mortgages do have mortgage protection insurance, says Nielson.

It is often sold by the bank and isn't perfect. It will usually cover mortgage payments for six months to two years following illness or accident (and unemployment if you're lucky), but not beyond.

These policies pay off the entire mortgage if you die. But once again there's a catch - because you're only disabled and very much alive your loved ones need to find a way to fund the mortgage after six months or two years.

The other factor that people may not think about is that someone who is in Hutchinson's words "TPDed" isn't likely to have as full a life span that they might have had as a healthy person. "It is rare for someone to be TPDed and it not affect their life span," he says.

When the person does finally die there will be a payout from the life insurance if - and only if - the family could afford to continue to pay the premiums following the disability. Not, I would hope, that any family would be looking forward to the life insurance being paid out.

The reality is that it can ease the financial nightmare.

Hutchinson points out that KiwiSaver is providing a de facto total permanent disablement insurance cover for Kiwis. That's because if you're permanently disabled, you can apply under the hardship provisions to withdraw your investment.

That might cover home modifications and other costs.

It would mean, however, that if you lived to 65 you would only get NZ Superannuation. It's Catch 22 again. Many retirees say it's difficult to live on NZ Super alone.

What's more, if you haven't made any savings for the last 10 or more years of your working life "you are still stuffed", says Hutchinson.

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