4 Critical Steps in Purchasing Resident Disability Insurance

[Editor’s Note: This month’s column at Physician’s Money Digest was co-written with Michael R. Relvas, CFP, who is a paid advertiser on the site and specializes in physician income protection planning. Most of the disability insurance articles published in the last 18-24 months on this site have been on the complex side, so I wanted to do something that is a bit more about the basics of disability insurance. This article is our attempt to do that. It’s that time of year when residents who don’t yet own disability insurance policies really need to get that chore taken care of.]

A medical resident’s most valuable financial asset is his future earnings ability, which is at serious risk of loss due to a personal disability. In fact, the February 2013 Fact Sheet from the Social Security Administration suggests that more than a fourth of today’s 20-year-olds will become disabled before they retire.
Step 1: Buy the right type of insurance from the right person

Many residents are offered group disability insurance through their residency program or hospital. While this insurance is better than nothing and often relatively inexpensive, group disability insurance is generally inferior to a solid individual, specialty-specific disability insurance policy for several reasons.

Unlike life insurance, where the question of death is quite black and white, disability comes in many shades of gray. The stronger definition of disability in an individual policy is simply more likely to pay in a greater number of circumstances, thus the higher cost of premiums. An individual policy is also completely portable, meaning you can take it with you upon residency completion (and often add to it without additional medical screening.) The policy is also likely to be non-cancelable—the low premiums available to a young, healthy resident will remain level throughout your entire career.

Depending on your state of residence, specialty, discounts available, health, and hobbies, the pricing of a comprehensive policy may vary significantly from one insurance company to another. Independent agents earn their commission by comparing policies from all available companies with you so that you may decide on the best policy for your situation. As such, it may be beneficial to buy your policy through an agent who is completely independent, meaning he can sell you a policy from any of the half dozen companies out there offering high quality physician disability policies.
Step 2: Buy the right amount of disability insurance

The truth is that residents generally cannot purchase as much disability insurance as they need, nor can they really afford to do so. Disability insurance is expensive, usually costing 2% to 5% of the amount of income insured; a policy that pays $15,000 per month if you are disabled may cost approximately $3,600 to $9,000 per year—a sum that most residents simply cannot afford.

A resident, however, should generally purchase as much insurance as he can—a monthly benefit of $5,000. This might not seem like much, but it is a benefit that would normally be available only to someone making $100,000, not just the $45,000 a typical resident is making.

The benefit amount may be higher ($6,000 to $7,500 per month) during the last 6 months of residency, and can be markedly higher once a contract is secured for post-residency employment. You generally want to purchase your attending level disability insurance before starting your first attending job, since the amount of individual disability insurance you can purchase may be reduced by a group policy offered by your new employer.
There are a couple of options to help residents afford disability insurance. The first is to use a graded premium schedule instead of a level premium schedule. This means that premiums are lower during the early policy years (when you are living on a resident’s income) and then increase later. This works out especially well if you are able to cancel your disability insurance upon becoming financially independent in your 50s. You may also convert from graded to level as an attending, when your cash flow is less restrictive.

The second option is a Future Purchase Option rider. This allows you to buy more insurance at a later date without having to re-qualify medically (i.e. healthy with no dangerous hobbies). Using this strategy, a resident could buy a benefit of $3,000 to $5,000 a month (with a monthly premium as low as $90) now and then increase the coverage at the time of residency graduation when his or her higher income makes the higher premiums more affordable.

**Step 3: Purchase the appropriate policy and riders**

You want to make sure your policy is specialty-specific, so if you cannot practice your specialty as the result of an injury or illness, the policy will pay benefits, even if you chose to work in a different capacity. This is especially important for a procedural specialty, where loss of even a single digit could dramatically decrease your income. If the definition of disability is not specialty-specific in the standard policy, purchase a rider to make it specialty-specific. Typical specialty-specific wording may read like this:

“Total disability is the inability, due to injury or illness, to perform the material and substantial duties of your occupation, even if you are gainfully employed in another occupation.”

Furthermore, some companies will also add the following: “If
you have limited your occupation to the performance of the material and substantial duties of a single medical or dental specialty, your specialty will be deemed to be your occupation.”

Many policies also include a 24-month limitation for psychiatric conditions, meaning if you are disabled due to mental illness the policy will only pay for 2 years, instead of to age 65. Stronger (and often more expensive) policies do not have this limitation.

Riders, like the Future Purchase Option discussed above, offer additional benefits not in the standard contract, usually for an additional premium. Since this feature allows a resident to increase his or her monthly benefit in the future, without requiring additional medical screening, it can be particularly useful for those purchasing a policy during the earlier years of residency.

Residents should also purchase a Residual Disability Rider, which allows residents to claim a benefit for a partial disability. Another important rider for a resident to purchase is a Cost of Living Adjustment Rider, which increases the monthly benefit during a claim, with intent to keep pace with increases in the cost of living. In the case of a long-term, permanent claim, you will be very glad you spent a little extra on this one.
Step 4: Go through underwriting

In order to actually purchase disability insurance you will need to submit an application to the insurance company and complete the underwriting process, which your agent is there to help with.

Throughout this process, you will be asked questions about your medical history and lifestyle, which includes dangerous hobbies like SCUBA diving, flying, skydiving, and climbing. You will also be required to complete an insurance medical exam, generally completed by a paramedic who will come to your house to take vitals and collect blood and urine samples on which a fairly comprehensive set of tests will be run.

Assuming you satisfy the eligibility requirements, your agent will generally have your policy ready for a final review and acceptance within three to six weeks. Your agent is being well compensated for his time, so do not hesitate to ask the questions necessary to have a complete understanding of your policy and be confident in your purchase. The process can be tiresome and the policy costly, so you want to be sure you buy the right policy the first time.

Following these four steps will help you get this extremely important insurance in place early in your career.

If you don’t yet have disability insurance, I’d like to hear why not.