Adviser Fact Sheet

Zurich Wealth Protection and Active Ongoing Income Clause fact sheet – for risk advisers

Fact explained: ongoing income clause

You want to provide certainty to your clients. The key to certainty is ensuring your clients have the right level of cover and understand the implications when it comes time to make a disability claim. Part of that process may include talking to your clients about ongoing income at the time of application.

What is the 'ongoing income' clause?

The ongoing income clause is used by Zurich when underwriting applications for Zurich Wealth Protection and Zurich Active Income Protection policies.

If your client is a business owner and their business is likely to continue to generate income even while they are unable to work due to illness or injury, Zurich may apply an ongoing income clause to the policy when the policy is issued.

The benefit payable, when the ongoing income clause is applied, is proportionately linked to the loss suffered; that is, the difference between the client's 'pre-disability income' and 'post-disability income'.

Why is it important for your clients?

Income protection policies are designed to cover income which your client may lose due to illness or injury. The purpose of income protection is to cover the different levels of loss your client might experience.

If your client's business income is likely to continue while your client is unable to work, we would look at placing an ongoing income clause so that benefits are proportionate to the loss actually experienced. This enables your client to obtain income replacement cover based on their full income rather than part of it – which is important in the worst case scenario when there is no post-disability income.

Start the conversation and give your clients peace of mind

Here is a checklist to help you assess whether your client's business income is likely to continue, and for how long. If you think your client may receive ongoing income through their business, you can then start a conversation about ongoing income with your client and give them peace of mind.

It is important to have a conversation with your clients about ongoing income at the time of application, so they fully understand the level of protection they are applying for. This can also help to ensure they are covered for the worst case scenario in the event of a claim.

What is the nature of the business?

- How does the business generate its income?
- What type and number of different income streams are there?
- What is the size of the business (for example, physical size, geographical location of operations, turnover, gross profit, net profit)?
- What is the business and ownership structure?
- How many full-time and part-time employees are there?
- What are the roles, duties and contribution of other owners and staff in the business to income generation?
- What are the roles and duties of the applicant?

These initial questions about the nature of the business will help determine the likelihood of ongoing income in the event of a disability claim.

More Specific Questions

In the event the client is unable to work:

1. Would the business continue to operate after 30 days?
2. Would the business likely seek a locum or replacement for the client?
3. Would the business continue to generate revenue?
4. Would the business continue to make a profit?
5. How much of a profit would the business likely make and for how long?

If based on the answers to the above questions, your client's business would likely continue to operate, generate revenue and make a profit, can this be managed by increasing the waiting period? If not, it is likely an ongoing income clause may apply.

How does the clause work?

To determine the benefit to be paid where the ongoing income clause applies, Zurich will apply a partial disability formula.

The benefit payable is a proportion of the monthly benefit, calculated as follows:

$$\frac{\text{Pre-disability income} - \text{Post-disability income}}{\text{Pre-disability income}} \times \text{the monthly amount we would pay if the client was claiming for a Total Disability benefit without an ongoing income clause.}$$

Where the ongoing income clause applies it will most likely be a 6 month ongoing income clause, meaning the clause will not apply until after 6 months on total disability claim. For the first 6 months on total disability claim the amount we would pay will be the monthly amount we would pay if the client was claiming for a total disability benefit without the ongoing income clause.

Pre-disability income and post-disability income are calculated by applying the same A-B = C plus add-backs methodology used to calculate insurable income for business owners (this is the same process that is undertaken at the underwriting stage using the Zurich Income Protection Calculator).

The formula calculates a percentage to multiply by the monthly benefit (mb) amount ie the monthly amount we would pay if the client was claiming for a total disability benefit without the ongoing income clause.

Using the formula means the benefit amount calculated is related to the loss of income suffered by the client (regardless of whether it is a partial or total disability claim).

This means that when the post-disability income is zero (because the business has no income or has been sold), 100 per cent of the benefit amount will be payable to the client.

Ongoing income clause: case study

Ray Brown is a 50 per cent owner of an established business with 10 staff. Ray, his business partner and four staff contribute directly to income generation in the business to varying degrees. Ray's business earnings (after A-B=C plus add-backs) are $240,000 per annum (pa), which supports a benefit of $180,000 pa or $15,000 mb ($240,000 x 75%). In the event of a total disability claim and assuming Ray's pre-disability income (before the claim) is $20,000 per month (equivalent to $240,000 pa) the effect of the 6 month ongoing income clause (compared to no ongoing income clause) is shown in the table below.

Scenario			6 Month Ongoing income clause		No Ongoing income clause	
Claim Month	**Business status Description**	**Post-disability income**	**Benefit paid**	**Replace ratio**	**Benefit paid**	**Replace ratio**
1-3	Ray is unable to work. Profits dip slightly.	$16,000 pm	$15,000 mb	155%	$15,000 mb	155%
4-6	Staff begin to lose confidence, absenteeism rises and clients start going elsewhere. Profits dip further.	$12,000 pm	$15,000 mb	135%	$15,000 mb	135%
7-9	Staff and clients are now losing confidence in the business. More clients are going elsewhere. Profits dip even further.	$9,000 pm	$8,250 mb	86%	$15,000 mb	120%
10-11	Staff start to get poached by competition and more clients going elsewhere. Profits are slumping now.	$5,000 pm	$11,250 mb	81%	$15,000 mb	100%
12	Ray sells his share of the business to his business partner or, worse-case, the business becomes insolvent.	0	$15,000 mb	75%	$15,000 mb	75%

The table shows that the benefit payable, when the 6 month ongoing income clause is applied (from month 7 onwards), is proportional to the loss Ray suffered. In other words, the benefit paid after 6 months on claim is linked to post-disability income (while Ray is unable to work and is on claim). Please note these numbers are used for illustrative purposes only, each situation will be different.

For more information about Zurich visit zurich.com.au or call Tony Baker, Financial Underwriting and Claims Manager on +61 2 9995 1941 or call 1800 280 130

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