THE ROLE OF INSURANCE IN SPECIAL NEEDS PLANNING

Part I

Insurance often plays an important role in Special Needs Planning (SNP). Why is this? Much of it can be attributed to the requirement of planning for two generations as opposed to one. You are not only trying to provide for the quality of life you desire for your child while you are alive, but also after you are gone. That is why you don't hear the parents of a child with special needs saying they are "spending their children's inheritance."

Life insurance is a source of financial security in the event something should happen to either parent. In addition, it is often used to fund a Supplemental or Special Needs Trust (SNT). In fact, life insurance is often considered the best way to fund an SNT since the death benefit is not taxable as ordinary income. This is significant since these types of trusts are taxed at the highest federal tax rate very early on.

Let's use an imaginary couple, Bob and Carol, to illustrate the use of life insurance. Since Carol is the primary caregiver to their disabled son, Jimmy, we first need to take a different approach when calculating the amount of Carol's coverage. Carol provides many necessary services required for Jimmy's care, and should something happen to her, Bob would need additional resources to purchase those services if he is to continue working. Therefore, we would insure Carol for a larger amount than we might ordinarily for a non-working spouse.

When deciding on the type of insurance, we would consider Term insurance (least expensive) for anything that has a definite time limit. Examples of this are college, mortgages, children to a certain age, and retirement. We would consider permanent life insurance for things of uncertain duration. Funding the Special Needs Trust is one such item, since it will be funded upon the death of one or both of the parents. If we are not concerned about income for Carol or Bob upon the premature death of the other, we can consider Second-to-Die insurance, which pays a death benefit upon the death of the second insured individual. This type of insurance offers certain advantages. First, it is usually less costly than two separate policies. Also, if the health of one of the parents is questionable, it may avoid insurability issues since the insurance company is only paying upon the death of the second parent.

There are various other types of permanent insurance such as Whole Life, Variable Life and Universal Life. The details and differences are beyond the scope of this article. However, please keep in mind three things. First, a comprehensive approach will usually dictate a blend of various types of insurance. This is to both ensure that we are achieving the desired end result, as well as to keep premium costs to a minimum.

Second, insurance should be purchased as a by-product of a comprehensive approach. Many people end up with numerous policies that don't accomplish the desired goal, or they spend too much in unnecessary premiums. Calculate your current debt, your required income stream, and future goals, including the funding of the trust. Then determine the types and amounts of insurance required.

Third, if you have a life insurance policy that is more than 3 or 4 years old—especially a Term policy—have it re-evaluated. There have been significant changes in the insurance industry. You may very well be able to obtain the same or additional coverage for less.

When should you purchase insurance? As the old insurance adage goes, "before you die or become uninsurable." This has a particular relevance to me since my father was diagnosed in his early thirties with a heart ailment which made him uninsurable. Later, when he wanted to start his own business, he couldn't, due to the fact that the only insurance he could obtain was group life insurance. It also meant a smaller estate for my mother and for my brother's trust when my father passed away at the relatively early age of 58.

We often resent the cost of insurance premiums until the day comes when we are unable to purchase it. Then our desire for it becomes unbounded. My father would have paid almost any price to provide additional security for his family.

You may wish to refer to my earlier article, "How Much Is Enough" which addresses, in more detail, the factors you need to consider when calculating the funding of a trust. Then consider how you plan to fund the Special Needs Trust and provide security for your family, including your disabled child. Finally, do what many fail to do—Implement!