Overhead Expense (OE) Summary

Why Self Employed Financial Advisors Need Overhead Expense Insurance Coverage

OE insurance is a disability policy that pays the **fixed overhead** of the insured's business during periods of disability. The first question that needs to be answered is **do you need it?**

Whether your compensation is derived from fee-based planning, fee-based money management, commissioned insurance products, commissioned investment products, or some combination of these compensation methods, your income will not stop when you become disabled. Licensed staff can service established accounts resulting in revenue continuing to flow into your business. Many commissioned insurance products and annuities have renewal streams that are vested and continue for the life of the policy. Therefore, many financial advisors think they do not need OE insurance coverage because their renewals and ongoing fees will always be enough to cover office overhead, even during periods of total disability. Consider the following:

- New clients are only created **if you are there** to create them. If you are not there to generate new business, as your existing clients terminate policies, your gross revenues decrease.
- Licensed staff may be able to write add-on business on existing accounts, but cannot bring in new accounts. If they could they would not be staff, they would be full-time marketers.
- If a client has a problem or question they may not be satisfied working with your staff and move their coverage to another advisor, if you aren't there to answer it for them.
- If a large client cancels or moves their coverage the financial impact will be significant.

The result of these issues is that during periods of total disability your gross revenues are reduced, which **hits your bottom line profit first**. Hypothetical example:

If you gross $30,000 per month, have $16,000 of monthly expenses, and net $14,000 a month, a $10,000 drop in gross revenues does not reduce your overhead…it **reduces your profit** to $4,000 that month ($20,000 revenue **-** $16,000 expenses = $4,000 profit).

So, how does OE insurance help?

OE insurance reimburses you for expenses you incur while totally disabled. **This allows you to take revenue out as profit that would otherwise be used for paying overhead**. If you had $5,000 of OE insurance in the example above, you could use the OE insurance to pay overhead and pass an additional $5,000 of revenue through to yourself as income. If you also carry $4,000 of disability insurance, **your income would only drop $1,000 per month** ($4,000 profit + $5,000 OE insurance pass through + $4,000 DI = $13,000 payable to you), even though your gross profit was reduced by $10,000 per month.

Do you need OE if you are partially disabled?

This is a very good question. In large part, it depends on how long you've been in business and how your practice is structured.

- If you are working part-time you probably won't lose a lot of clients. Therefore, your revenue will not drop much and will probably be in excess of your fixed expenses.
- Even if your new business fees/commissions are significantly reduced, what new business you bring in plus the revenues from your renewals should be in excess of your fixed expenses.
- If you have professional staff and/or partners that continue to cover your duties while you are out of the office (which is manageable if you are working part-time), your gross revenues may drop a very small amount.
- Even if your practice is primarily first year commission driven, meaning you haven't been in the business long enough to establish a solid base of renewal income, if your production is reduced by 50% you will generally have enough income flow to pay your overhead.

Since Residual benefits are calculated by subtracting covered (fixed) expenses from gross revenues, if your practice looks like any of the examples above, it's unlikely your gross revenues would drop below fixed expenses, if you were working part-time. In this scenario, the Residual rider would NOT pay benefits.

If your practice looks like the examples described above, then buying the Residual benefit does NOT seem necessary. However**, buying an OE policy that pays benefits for total disability makes a great deal of sense.**

Taxation of OE premiums and benefits

Premiums for OE insurance are **deductible as a business expense**, whether you file your income taxes as a sole proprietor, partnership, Sub Chapter S Corporation, or C Corporation.

Benefits from OE insurance are taxable as income. However, if the benefits are used to pay deductible business expenses, income tax is NOT payable on the benefits.

The OE program includes:

1. The definition of total disability is "Your-Own Occupation" for the benefit period. If you are deemed totally disabled from your occupation, it is your choice, not the insurance company's, to work in another occupation.
2. Elimination (waiting) periods of 60 or 90 days
3. Benefit Period of 12, 18 or 24 months
4. Premiums and benefits are guaranteed not to change until age 65 (even if you leave the association)

For a personalized premium quote and a complete summary of the program offering (including the actual policy definitions, and underwriting rules) return to the home page and click on the **Request a Quote** button or call Disability Specialists, Inc. (DSI) at (888) 279-8348 (7:00 am – 4:00 pm Mountain Time).