

Comparing state insurances and private income protection

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Contractors who can't find work or are too ill to work will find that state insurances do not provide any kind of a safety net for the resulting loss of contracting income.

"The main state benefits for contractors not able to find work or too ill to work are [Jobseeker's Allowance](#) (JSA) and [Statutory Sick Pay](#) (SSP)," notes [Contractor Financial's](#) life and income protection insurance expert [Mark McBurney](#).

"However most limited company contractors will not be eligible for benefits or in the case of SSP effectively have to fund it themselves anyway, so the only realistic alternative is for contractors to make their own provision with income protection and critical illness policies."

Umbrella company contractors working for a compliant service provider should both qualify for and be paid sick pay if they cannot work due to illness, but face the same challenges as limited company contractors when between contracts.

What state insurances are available for contractors out of work?

In theory, anyone who cannot find work can claim JSA of up to £73.10 per week if they satisfy the eligibility criteria. Low earners and those who can't work for other reasons, perhaps because they are full time carers, can also claim [Income Support](#).

But as McBurney explains, not only are the payments a fraction of what a contractor normally earns, but few would pass the eligibility criteria: "A senior IT contractor earns in an hour what JSA pays out in a week, so state insurances are no replacement for contracting income.

"Furthermore, limited company contractors continue to be employed by the limited company between contracts, so are technically in employment. Resigning from their limited company to qualify for JSA could actually make them ineligible for unemployment benefits, so in practical terms there is no state support for contractors on the bench."

Do contractors qualify for Statutory Sick Pay?

Although limited company contractors will qualify for SSP after being off sick for four days, this benefit is usually funded out of a business's National Insurance Contributions (NICs), ie regular employers deduct SSP paid to employees from the NICs they would normally pay HMRC.

"But limited company contractors don't pay any NICs, so there is nothing to deduct the SSP from," highlights McBurney. "Furthermore, SSP is only £88.45 a week, which is a fraction of the average contractor's weekly earnings."

Umbrella company contractors are employed by their service provider so should enjoy the same benefits as any other employees. This means they will qualify for SSP, although they face the same shortfall in earnings as a limited company contractor.

Contractors should have 3-6 months of cash savings

"Most contractors are not able to cut their living and household costs overnight if they suddenly fall ill or are out of contract," continues McBurney. "That's why at as a minimum we recommend that contractors have cash savings that will pay for at least three and preferably six months or more of living expenses.

"There is another reason to have a generous cash pile, and that is because the premiums for private income protection and critical illness insurances are reduced if there is a deferred period.

The deferred period acts much like an excess does on familiar insurances such motor and buildings insurance. The longer the period, the greater savings a contractor will make on premiums but in turn this means having greater savings.

"Contractors should review the level of savings against their outgoings on a regular basis, because what might last for six months last year might only last for three months in a year's time," adds McBurney.

Private income and critical illness protection provides a safety net

McBurney says that income protection is effectively a replacement short-term sick pay: "The cover can be tailored and include a deferred period that will reduce the premiums. Income protection can protect up to 70% of a contractor's income. It can be index linked so it rises with the cost of living.

"For more serious long-term illness such as cancer or a heart attack, or a disabling accident, then contractors should take out critical illness cover so that it

works together with income protection. Critical illness can pay out up to a contractor's retirement, when their pension should paying them an income."

McBurney urges contractors to check the details: "Make sure the insurance has a clause for total and/or permanent disablement. Plus it should also pay out of a contractor cannot return to their own occupation. This means they would not be forced to return to work in a more menial role."

There are no other insurances to replace state support. Some contractors will be familiar with older products such as Payment Protection Insurance (PPI), but products such as these no longer exist.



Mark McBurney

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Mark McBurney is an experienced financial adviser, with ten years' history in the mortgage market, now specialising in protection for contractors.

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He concludes: "To avoid the pitfalls, contractors should work with a financial adviser who will also be able to help tailor the package according to their needs. Then it is important to review the cover at least once a year to ensure that it is still appropriate to a contractor's circumstances."

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