

Contractor income protection and the myth of unemployment cover exposed

"Buyer beware!" is the message for contractors when it comes to unemployment insurance says Tony Harris of Independent Financial Advisers [Contractor Financials](#). He is angry that there are many insurance products marketed to contractors that claim to be suitable for those working on fixed term contracts.

The product providers and brokers who sell these policies invariably ignore fundamental flaws in the policy wordings which mean that, according to Harris, "By the very nature of how they work, most contractors are excluded in the event of a claim".

"Even when they are not in a contract, contractors are still nominally employed by their [limited company](#) or [contractor umbrella company](#)," continues Harris. "So technically, just because they don't have a contract, it is difficult to prove unemployment."

Caveats and exceptions for contractors

Most permanent employees receive sick pay from their employer when they can't work through illness. Their families are also entitled to death-in-service payments of up to four times the employee's salary. And many employees opt to pay for various types of income protection cover, such as 'redundancy insurance' and 'unemployment cover'.

However, according to Harris, although contractors can take out policies to cover ill health and death, insurances that advertise they cover contractors for periods of unemployment are full of caveats and exceptions, making it highly unlikely that the contractor is ever going to be able to make a successful claim.

"The devil is in the detail with unemployment protection insurance, and policies covering periods out of work generally exclude most contractors," explains Harris. "This can be because the insurance terms stipulate that contracts must last 12 months, which of course most contractors don't like because of [IR35](#), or the terms state that the contract must have a minimum of one renewal, which again many contractors will be reluctant to accept because lengthy periods at one client will increase the likelihood of the contractor falling foul of [HMRC](#)."

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Tony Harris, Contractor Financials

"Even in the unlikely event that a client has a 12 month contract that has been renewed, they can still fall foul of the clause found in most policies that states you must have 6 months left to run when you are terminated early," argues Harris, "it is almost bound to happen that with the 6 months rule you are terminated with 5 months and 3 weeks left to run!"

Money better saved than spent on insurance

"Rather than spend £50-£60 a month on an insurance policy upon which there may never be a successful claim," continues Harris, "we recommend that contractors 'self-insure' by stashing away a rainy day fund in a high interest deposit account."

"It's amazing how quickly £60 a month mounts up and after a couple of years a contractor has enough cash to pay the bills for several months if they can't find a suitable contract. It takes discipline, but most contractors should have enough net income that they can afford to put away a good amount to tide them over during periods with no work."

So, what protection policies are worth the paper they are written on?

If family security is an issue, there are many completely watertight insurances that provide a lump sum for the family if a contractor dies prematurely or is diagnosed with a critical illness. These policies are not specific to profession or employment status and so are completely appropriate for a contractor.

Similarly, contractor friendly policies can be arranged that pay an income if the contractor is ill or injured and is unable to work at the client's site. Indeed, it could be argued that, if between contracts, a freelancer could always accept a lower rate to maintain some income. However, if the contractor is ill or injured their earnings could stop completely in the short term and may be irreplaceable in the event of a more serious long term condition.

Peace of mind need not be expensive, with the average accident and sickness policy, also known as permanent health insurance, costing no more than £40-£50 per month for contractors with no medical complications.

Permanent health insurance - how does it work?

"Contractors should carefully check the details of any [permanent health insurance](#) to ensure there are no unwelcome clauses," says Harris, "although if the contractor is working with a good, contractor experienced IFA [Independent Financial Adviser], their adviser will ask these questions of a policy before recommending it."

For example, some policies won't pay out if the contractor can work in a more menial role, even if they have a condition that precludes

them from working as a contractor. If a condition allows them to work in, say, a post room, or as a security guard an 'any occupation' policy will not pay out. So the policy should be on an 'own occupation' basis to ensure that a claim will be successful.

Those contractors who pay themselves low salaries and the balance in dividends should also check that their policy factors this in; otherwise they may find their benefit payments are well below expectations.

Contractors can also reduce their monthly payments by opting to extend the period before the insurance starts paying out by up to 12 months, which is another option for contractors with a good pot of savings.

And contractors should beware that most policies will only pay 65% of their normal income as an incentive to get the contractor back to work although it should also be noted that benefits are tax-free.

Flexible policies for flexible lifestyles

"As contractors' personal circumstances are constantly changing, so should a good policy change to meet the needs of those changes," concludes Harris. "As their needs change, so can their policies. So, if a contractor is earning more and has higher expectations, they can increase the amount they would be paid if they had to claim."

State benefits are becoming increasingly tough to qualify for and, says Harris, particularly in these difficult times for borrowers, the long-term impact on a credit rating if a contractor misses mortgage or credit card payments through lack of funds can be hugely damaging. In this way income protection could very well be a policy that you cannot afford to be without.

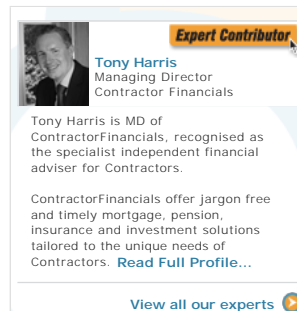
Despite the lack of protection for contractors when unemployed, they should take heart that financial security can be bought for themselves and their families and that there are policies that will deliver when the Contractor is at his or her most vulnerable.

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ContractorFinancials offer jargon free and timely mortgage, pension, insurance and investment solutions tailored to the unique needs of Contractors. [Read Full Profile...](#)

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