AGENT REVIEW'S

GUIDE TO **LIFE INSURANCE**

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LIFE INSURANCE

WHAT IS LIFE INSURANCE?

Life insurance is protection against the loss of income that would result if the insured died. The named beneficiary receives the proceeds and is thereby safeguarded from the financial impact of the death of the insured. The explanation is straightforward, however the reason that more than 40% of eligible individuals do not buy it is not … So lets start with the basic question, “Do I need life insurance?”

DO I NEED LIFE INSURANCE?

There have been numerous surveys conducted by the insurance industry in an effort to determine why so many of those who understand what life insurance does, nevertheless, do not purchase it—or if they do purchase life insurance, why in amounts that are insufficient to protect their families. Here are the usual reasons given for not purchasing coverage:

- Too young
- I don't have a family
- Spouse or significant other has other means of support
- Dependents are provided for with other assets
- Too expensive
- More important priorities

The above reasons make sense from a risk point-of-view—fewer than 2% of insurance policies pay a death benefit during working years; but have you thought about an unexpected death from a consequence point-of-view?

It starts with an assessment of who and what is important to you. The "who" is, hopefully, your family—those you invited into your life and promised to take care of. The "what" is lifestyle, or more simply, the financial commitments you have made to them. There is little doubt that you understand what would happen to your ability to keep these promises if you die during your working years ... However, that's assuming you believe you could.

Like many healthy consumers, you likely believe that risk is ... Zero.

In fact, the above statistic pretty much confirms it. So the thought is, "If I'm not going to die during my working years, how can it effect my family? Why then spend money on insurance?"

No argument—from a statistical point of view you're right. Another way of thinking about it however is that your family is not a statistic—they are an inseparable part of your life and because of that, you have become indispensable to them.

Therefore, you may want to consider an unexpected death not as a risk that is unlikely to happen to you, but rather a life-changing event that has serious emotional, physical and financial consequences to those you love.

With that in mind, lets look at these objections again:

- I am too young: If you have a spouse or partner, children and/or commitments, it shouldn't matter how old you are—the consequences of an unexpected death, regardless of age, are just as severe.
- I don't have a family: Right now perhaps, but do you see yourself taking on the responsibility for another in the future? If the words "spouse" or "children" crossed your mind, insurability becomes a

critical issue.

- My spouse or significant other has other means of support: Are you absolutely certain? Perhaps, at present, their income may be sufficient, but is it possible that you may assume more financial commitments in the future? What if he or she leaves the workplace, voluntarily or involuntarily?
- My dependents are provided for with other assets: That may be the case, however, will these assets be sufficient to generate enough income? Are these assets liquid, and if so, would there be serious tax issues if they were used? And perhaps just as important, what were these assets allocated for in the first place? If they were meant to generate income later in life, using them for day-to-day expenses disrupts that plan
- It's too expensive: Actually, life insurance is one of the least expensive protection products, but only if you see a value in it. If you believe you are not going to die during working years, then the value is negligible. If however, you see an unexpected death as a life-changing event for your family, then the product is worth your attention and investment.
- I have other priorities: No doubt you do; however these priorities likely revolve around your commitment to those you love. Priorities should not end at an unexpected death.

Ok, assuming your objections have been addressed, let's take a look at the different types of life insurance available and how to make it affordable.

WHAT IS TERM INSURANCE?

This is the basic or "entry level" form of coverage. The policy provides a check to your beneficiary when you die. It's called term life insurance for a reason—it only covers you for a term of one or more years, therefore it only pays a death benefit if you die within that term.

Pros:

- It is very affordable because it is lapse supported. That is, generally only 2% of this type of insurance actually pays a claim during working years which means the premiums paid by those who don't die keep the cost of paying claims very reasonable.
- It covers specific expenses that are transactional in nature such as private school and/or college tuition, as well as a mortgage. When they are paid the policy can be lapsed.
- Most policies are convertible, which means they can be exchanged for another policy with coverage that doesn't end until death such as whole life, without taking a medical exam or

answering any health questions.

Consider however:

- Your commitments may change later in life and you'll want them insured ... You may become uninsurable, or premiums may become too expensive.
- Your wealth may increase substantially requiring a sophisticated estate plan with insurance to minimize taxes.
- Term policies do not build cash value, which may be helpful if you start a business and want to become your own bank. Products such as whole life or universal life build cash value allowing you to borrow against it rather than go to a bank.

WHAT IS WHOLE LIFE INSURANCE?

Whole life insurance is also referred to as "straight life," "ordinary life," or "permanent insurance." Unlike term insurance, there is no need to renew it and it lasts for the rest of your life.

Pros:

- It can never be cancelled, unless you don't pay the premiums. This makes it useful for estate planning or unexpected expenses later in life.
- Premiums are fixed.
- The cash value can be borrowed against. This makes it useful for small business owners who can avoid the time and expense required to apply for a loan.
- The death benefit is not taxed.
- Dividends may be used to purchase Paid-Up Additions(PUA's) to increase the death benefit.
- Some companies offer so-called "hybrid" policies that use the dividends on the policy to buy additional term insurance.
- The policy pays an annual, guaranteed dividend based on state law.
- You are able to withdraw, tax-free, much or all of what was put in, although there are strict rules.
- It can be used to fund a plan for a special needs child.
- If you have maxed out your contributions to your 401(k) or other tax-advantaged plans, a whole life insurance policy may make sense.

Consider however:

- You need significant cash flow to afford the policy each year based on the amount of the policy.
- The Wall Street Journal pointed to a 2012 study by the Society of Actuaries ... It found that 20% of whole-life policies are terminated in the first three years and 39% within the first 10 years. That means that you have paid a substantial amount in premiums, the majority of which go to the agent in the first year, in exchange

for little benefits—unless of course you die.

WHAT IS VARIABLE LIFE INSURANCE?

The policy benefits—both death and earnings—vary based on the performance of the assets your premium payments are invested in. You will generally be offered a variety of investment options, including equity, bond, and money market mutual funds. Death benefits and cash values are directly related to the performance of investment options you choose, although there may be a guaranteed minimum death benefit. Agents who sell these types of policies must have an insurance agent license, be registered as a representative of a broker-dealer licensed by the National Association of Securities Dealers (NASD) and be registered with the Securities and Exchange Commission (SEC).

Pros:

- The policy builds both cash value and death benefit.
- You can manage the funds by choosing from investment accounts offered by the carrier, giving you the potential of outperforming a whole life policy
- You get the death benefit, tax-free.
- It can help fund an estate plan.
- It can be used to fund a plan for a special needs child.
- You can borrow against the cash value.

Consider however:

If investments perform poorly, you may have less cash value.

- Poor fund performance also means that the cash and/or death benefit may decline, though never below a defined level.

WHAT IS VARIABLE UNIVERSAL LIFE INSURANCE?

Variable universal life policies (VUL) allow the policy owner to allocate money between the insurance and savings components of the policy, which allows you to make adjustments based on individual circumstances. For example, if the savings portion is earning a low return, it can be used, instead of external funds, to pay the premiums. Unlike whole life insurance, VUL allows the cash value of investments to grow at a variable rate that is adjusted monthly.

Pros:

- The benefits are essentially the same as whole life, with the primary difference being that you control how the premium is used. For example, you can increase or decrease the death benefit. However, an increase in the death benefit usually requires underwriting, while a decrease in the death benefit may cause surrender charges.

Consider however:

- This is not an investment. In fact, it is illegal under the Investment Advisers Act of 1940 to offer VUL as an "investment" to individuals. Therefore, it cannot be marketed or sold as a "security," "variable security," "variable investment" or as a direct investment in a "security."
- These are complex policies, with risk to the policyholder. For example, its flexible premiums include a risk that the policyholder may need to pay a greater-than-expected premium, in order to maintain the policy.
- If a loan is taken on the policy, it may cause the policyholder to pay a greater-than-expected premium. This is because the loan values are no longer within the policy to earn interest and help defray costs.
- If the policyholder skips a payment or makes late payments, it's possible that in later years, the policyholder may need to make up for this with greater-than-expected premiums.

OTHER FORMS OF LIFE INSURANCE

Guaranteed issue insurance
Guaranteed issue life insurance is divided into two basic subsets:

- No underwriting: The carrier does not ask for medical information. However, the benefits are modest, and there is usually a waiting period of between one to four years before the death benefit is paid to the beneficiaries. If the proceeds can only be paid for your funeral and related expenses, they are referred to as "final expense" insurance.
- Modified underwriting: Also referred to as "senior life insurance". Carriers generally do not ask for a medical examination, but may ask a number of health questions. Death benefits are generally between \$10,000 – \$150,000, and there may be a waiting period based on answers to the health questionnaire.

Viatical Settlements

Merriam-Webster defines a "viatical settlement" as, "… an agreement by which the owner of a life insurance policy that covers a person (as the owner), who has a catastrophic or life-threatening illness, receives compensation for less than the expected death benefit, (but more than the current cash value) of the policy in return for turning over (as by sale or bequest) of the death benefit or ownership of the policy, to the other party (as a company specializing in such transfers)."
The third party becomes the new

owner of the policy, pays the monthly premiums, and receives the full benefit of the policy when the insured dies. There are, however, strict conditions—the policyholder must be terminally or chronically ill, which is generally defined as have a life expectancy of less than two years.

Pros:

- Allows the policy to cover extraordinary expenses during his or her life.
- Allows for the policyholder to make bequests while alive.

Consider however:

The policyholder loses the death benefit, which may greatly exceed the amount offered by the company.

Life Settlements

As with a "viatical settlement," the policyholder sells an existing policy to a third party for more than its cash surrender value, but less than its net death benefit. However, there is no requirement that the individual be terminally ill.

Pros:

- The policy owner may no longer need the policy.
- The insured may wish to purchase a different kind of life insurance policy, or premium payments may no longer be affordable.

Consider however:

- The family does not receive the death benefit, which may greatly exceed that which is offered.

Is it better to buy direct or from an agent?

If your budget only allows for term, buying direct may be the right choice. However, if you foresee assuming additional responsibilities in the future, such as starting a business or having more children, purchasing only term insurance is rarely the right choice. A professional agent is more likely to ask you to consider blending it with a form of permanent insurance—one that guarantees its availability in the future.

For more complicated forms of insurance, estate planning or charitable commitments as examples, it makes sense to consult with an agent who is trained to work with other professionals—such as attorneys, accountants and/or CPAs—to take a total approach to your family's needs.

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