RW CONSULTING GROUP

TYPES OF LIFE INSURANCE

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There are many different types of life insurance on the market today to meet all sorts of consumer needs. The first feature of every life insurance policy is its death benefit, which is paid to a beneficiary upon the insured person's death, generally tax-free.

In general, with life insurance, the younger and healthier the insured person is, the lower the cost. Insurance companies use mortality tables as well as physical health examinations to decide whether or not they will insure someone and how much their insurance premiums will be. Because medical underwriting is required, not every person can purchase a life insurance policy.

In addition to a death benefit, with permanent life insurance policies there is a cash value portion of the policy which can grow through time. The cash value in a life insurance policy can be used while you are alive—borrowed to fund college costs, start a new business, pay for retirement expenses and more, sometimes with significant tax advantages as long as the policy remains in force. Some policies even offer coverage for long-term care should you develop the need for it, but provide a death benefit for your heirs if you don't.

Here are some of the basic types of life insurance, along with a brief overview of some of their features. Be sure to check with your financial advisor about specific policies which may be newly introduced to the market, or potentially be more suitable for your situation.

Term Insurance

Term life insurance guarantees a certain death benefit payout if the insured dies during a specified period, such as 1, 2, 10, 15, or 30 years, and then the policy ends. Often premiums for term insurance are level for a certain number of years but may go up as the insured gets older.

Pros

- It is relatively inexpensive.
- It can protect a young family from economic devastation and the loss of the family's income due to unexpected death of their provider/s.

Cons

- It is temporary, and if life insurance is desired in the future, the applicant will have to pass a new medical exam.

Permanent Insurance

The major types of permanent insurance policies are whole life, universal life and variable life in many different forms.

Permanent insurance provides lifetime coverage as long as a policy stays in force, and permanent policies are typically comprised of two parts: a savings, cash or investment portion and an insurance portion. This makes the cost of premiums for permanent insurance higher than for term policies.

Policyholders can borrow against the cash value of a permanent policy, usually tax-free in most cases, although interest will be charged. For this reason, permanent life insurance is also known as cash-value insurance. If you cancel your permanent life policy, you will receive the policy's cash value, minus any borrowed funds, fees or surrender charges.

Pros

- You can borrow against the cash value portion of a permanent policy once it has built up; your cash value can be used as collateral to secure tax-free (in most cases) loans as long as the policy stays in force.
- Some policies continue to credit interest to the total cash-value portion of your account even if you have borrowed money from it.
- The cash value is added to the death benefit if you do not borrow it.
- As long as you continue to pay all premiums, your policy cannot be canceled if your health status changes in the future. (A person who tries to buys life insurance when in ill health can be uninsurable.)
- Some policies have provisions for chronic, critical, terminal illness, or long-term care benefits that can be used in lieu of, or in addition to, the death benefit.

Cons

- If you borrow part of your cash value, you will be charged a fixed or fluctuating interest rate on the outstanding balance of any loan depending on your policy's terms.
- These policies cost more than term policies because they are permanent and have a cash value component.
- Fees and/or surrender charges may be levied at the time of terminating a policy or when withdrawing/borrowing money from your account. Check all policy terms carefully.

• Whole Life

Whole life insurance policies are permanent policies with fairly simple terms. They have fixed premiums and guaranteed cash value accumulation.

Pros

- Whole life has fixed premiums that don't go up.
- Whole life has a guaranteed cash value accumulation amount.
- There is the potential for increased accumulation when a mutual carrier declares a dividend.
- You can borrow against cash value.
- There is limited flexibility, you can use cash in the policy to pay premiums or utilize a future planned non-guaranteed dividend to pay the premium.

Cons

- Whole life can cost more than term or universal policies because of the guarantee.

• Universal Life

Universal life insurance gives consumers flexibility in the premium payments, death benefit amounts, and the savings or cash-value elements of their policies, which is why it's sometimes called adjustable life insurance.

For instance, as a person gets older, their intended beneficiaries may not need the financial protection they once did; with universal life, the death benefit can be lowered so that either the premiums can go down, or more of the premium amounts paid can go toward the cash value portion of the policy. (You can also increase the death benefit if desired, but you may have to undergo another medical exam to do so.)

In some cases, premiums can even be paid by the cash value if there is enough accumulated. Make sure to discuss the status of your cash-value fund with your advisor before stopping premium payments because your policy may lapse if you cease to pay premiums and have insufficient cash value to cover the policy expenses.

Pros

- Premium payments, death benefit amounts and cash-value amounts are flexible depending on the consumer's circumstances and desires.
- If the policy performs well, higher upside potential growth in the cash value is possible in the form of credits to the policy's cash value.
- Universal life is typically less expensive than whole life.

Cons

- The premium amounts due to keep the policy in force are not guaranteed and may go up due to rising costs or separate account underperformance.
- There are complex crediting methods for cash building; the interest credited is determined by the insurance carrier, and is often dependent on market conditions and insurance company reserves. However, some policies do offer guarantees.

Types of Universal Life Policies

Indexed Universal Life (IUL)

Indexed universal life insurance has many of the same characteristics of standard universal life insurance policies, except that the cash value's growth in the form of policy credits is tied to the performance of an index or indices, such as the S&P 500. Each insurer has its own selection of indices available and, depending on the policy, you may be able to choose more than one index.

While an IUL policy's cash value growth is tied to the performance of the selected index or indexes, the money is not actually invested in the market, it is a contract with the insurance company which determines how crediting works based on the index/indices' performance. Therefore, you are protected from stock market risk.

Depending on the individual policy's contract terms, you may have a minimum "floor" of 0% or higher, so that you cannot lose value even if the market dips, and you may or may not have a "cap" on the amount that can be credited during a bull market. Additionally, some IUL policies have a participation rate which is lower than 100%—for example, if the index is up by $500 and your participation rate is 80%, you are credited with $400—while some offer par rates over 100%. Your financial advisor should be able to find policies for your consideration which have the most favorable terms.

Guaranteed Universal Life Insurance

Guaranteed universal life insurance is a universal life insurance policy that won't lapse even if the cash value is zero. Since it's designed with no cash value component, or the cash value is very little, and premiums are usually level for the length of the policy. It essentially behaves as a term life insurance policy with the term ending at whatever age the policy matures, whether that's when you turn 90, 100 or 121. In fact, sometimes these policies are loosely referred to as "term for life".

Joint Survivorship Universal Life

Not as common as individual life insurance, joint policies are designed to enable two people, typically spouses, to share in one life insurance plan. Joint life insurance comes in two types: first-to-die, which pays out to the surviving spouse after the first dies; and second-to-die, or survivorship, which pays a death benefit to the heirs after both spouses are gone.

• Variable Life

Variable life comes in two forms—variable and variable universal life. Both variable life insurance and variable universal life (VUL) insurance are types of permanent coverage that allocate cash value to investment subaccounts, but with variable life, there is a fixed death benefit, while with VUL, there is a flexible death benefit and adjustable premium payment amounts.

Variable universal life (VUL) insurance is similar to indexed universal life (IUL). The primary difference is that the cash-value portion of a VUL policy is actually invested in the market; therefore, with VUL, there is the potential for loss. You can choose between various subaccount investment accounts available with your variable life or VUL policy. You will actually receive prospectuses to review so that you can determine whether or not a subaccount fits with your overall risk strategy.

Like IUL, with VUL there is no fixed, required premium that must be paid on a variable universal life policy. Instead, you must simply pay in enough money to cover the insurance company's expenses and the cost of the insurance, known as the mortality cost. If you pay in more than is needed to keep the policy in force, the excess goes toward the cash value part of the policy and is invested based on your instructions.

Variable policies often have higher fees due to the investment management required. When purchasing a variable life policy, you'll receive a list of potential investments, along with their performance history and fees, and can choose how much of the cash value is invested in each. Because these subaccounts are securities based, the value of your policy may grow more quickly with variable life, but you also have more risk, and if your investments do not perform well, your cash value and death benefit may decrease. Some policies, however, guarantee that your death benefit will not fall below a minimum level.

Pros

- You can choose between various subaccount investment accounts available with your variable policy.
- Variable and VUL policies may allow greater gains within the cash value portion of the policy if the stock market does well.
- Some policies guarantee that your death benefit will not fall below a minimum level.

Cons

- The biggest downside with variable life is the potential for your policy to lose money if the stock market goes down. If your investments do not perform well, both your cash value and death benefit may decrease.
- If the cash value in your policy exceeds a certain amount, your death benefit may also increase, but if the cash value reaches zero, your policy may terminate.
- Variable policies often have higher fees due to the investment management required on the subaccounts.

Learn More About Life Insurance

Life insurance is an important part of a complete financial plan. Allowing insurance companies to carry the risk of a potential adverse life event—such as death, disability, critical illness, need for long-term care, or loss of a spouse—protects the people around you from devastating financial loss and leaves a tax-advantaged legacy that in most cases bypasses probate.

Each life policy from each different insurance carrier has different features, benefits, and pros and cons, and the many product choices can be confusing for a consumer to navigate. Additionally, new types of policies are being introduced to the market all the time. It is very important to work with a qualified advisor to find the policy that might be best suited for you to meet your family's needs.

Contact Us For More Information

This document is for general information purposes only and is not to be relied upon for financial advice. In every case, you should seek the advice of qualified tax, financial and legal professionals to ensure that a life policy is advisable based on your unique circumstances.

Guarantees are provided by insurance companies and are reliant upon the financial strength and claims-paying ability of each individual insurance carrier issuing a life insurance contract.

Life insurance requires medical underwriting; therefore, not everyone will be able to purchase a life insurance policy. Life insurance policies can be complex, and it is recommended that you work with a professional to examine policy terms.

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