THREE REASONS TO OWN LIFE INSURANCE

Life insurance is like a Swiss army knife — it is remarkably useful, versatile and essential. One of the little-known facts about today's life insurance policies is that they can offer much more value than simply a death benefit. While helping secure the financial future for loved ones is the primary goal, life insurance can play an integral part in your overall financial plan.

Overview

Basically, life insurance is there in case you ever are not. In exchange for a one-time or ongoing premium, a beneficiary(s) receives proceeds upon the death of the policy owner. This money can be used in any way the recipient sees fit. For the policy owner, life insurance can provide a sense of confidence that his or her loved ones will be financially provided for should something happen to him or her. Although life insurance can be used to address a wide variety of financial issues, family financial well-being is generally its most important feature.

When determining whether you should purchase life insurance to replace income, ask yourself this question: "Does anyone rely on me financially?" If the answer is yes, then you should own life insurance. If the answer is no, then you don't necessarily need life insurance for this purpose.

When you purchase life insurance, you are essentially making a deal with an insurance company to trade payment — known as a premium — for the guarantee that it will pay your beneficiaries a set amount upon your passing. This is known as the death benefit, and all guarantees are based on the claims-paying ability of the insurer.

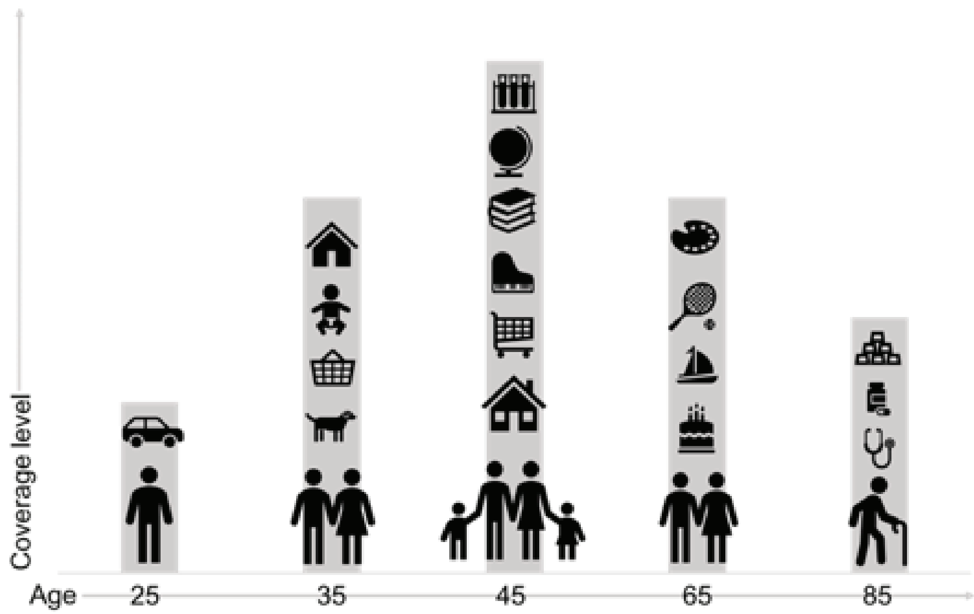
One of the primary questions a buyer should address is how much life insurance to purchase. The best way to determine this is to work with a qualified insurance professional. If your goal is long-term financial well-being for your loved ones, be sure to consider leaving enough money for them to:

- Maintain their current lifestyle
- Pay off debt, such as the mortgage
- Attend college
- Have a retirement nest egg

Every situation is different. Working with a licensed insurance professional is the best way we know of to balance the coverage you need at a cost that you can afford.[1]

"We love our spouses, we love our children, we love our grandchildren, so obviously we should care about what happens to them if we die." [2]

How Life Insurance Needs Can Change Over Time[3]



Here Are Three Reasons to Own Life Insurance:

No. 1: Replace Lost Income in the Future

As much as we'd like to believe life is invaluable, it is possible — and prudent — to attach an economic value to our lives — both breadwinners and caregivers. The term "economic lifetime value" (ELV) refers to the lifetime sum of earned income you would receive if you do not pass away before retirement. Replacing lost future income is probably the No. 1 reason someone would consider buying life insurance.

For example, if you make $60,000 a year and plan to work for another 30 years, your base ELV is $60,000 x 30 years, which equals $1.8 million. While that level of earned income is a base ELV, you may have more expenses to consider. To get an accurate idea of the amount of life insurance coverage you may need, consider additional variables such as long-term inflation, future raises and other available assets you may have.

No. 2: Pay Off Expenses

The next reason to consider purchasing life insurance is to pay off liabilities after you pass away. Initially, you should have enough coverage to pay for final expenses. Funeral arrangements can easily run to $11,000 or more, so life insurance can leave your heirs with a hefty sum to handle those expenses and more.[4]

Besides final expenses, you may wish for your beneficiary to pay off the mortgage or fund the purchase of a home. Maybe you'd like to pay for college tuition for your children or grandchildren. Perhaps you had always planned to pay for your daughter's wedding — or your four daughters' weddings. Calculate the sum of all of these extra costs to determine the face value of your life insurance policy.

Another common scenario is for business owners to use life insurance to pay off business debts in the event of their passing. Business partners will often create what's called a buy-sell agreement. This agreement simply asserts that if one partner were to pass away, the other one would buy the deceased's portion so that the business can remain viable.

By using a life insurance policy to facilitate that transaction, not only can the surviving partner continue to earn a living, but proceeds from the sale go to the deceased's loved ones to help secure their financial future. It also avoids the situation of the partner trying to co-manage the business with the deceased's family.

No. 3: Asset Management Tool

A third reason to purchase life insurance is one of the most overlooked and lesser-known uses. Life insurance can be used as an asset management tool as part of your savings or investment portfolio.

When most people think of accumulating wealth, they think of stocks, bonds, mutual funds, ETFs, etc., but life insurance can be used to enhance wealth as well. Here is a hypothetical example in which a 65-year old woman uses a life insurance policy to augment her financial portfolio.

Let's say she has accumulated roughly $1 million in her investment portfolio. She decides to withdraw $15,000 a year to pay annual premiums toward a $1 million life insurance policy.

Imagine this woman lives for another 20 years and therefore pays a total of $300,000 in premiums ($15,000 x 20). Bear in mind that when she passes away after 20 years, her beneficiaries will receive $1 million from this policy alone.

If it seems questionable to withdraw that much money over 20 years, consider what she might have otherwise done with the money. In fact, had she contributed the $15,000 every year into a traditional investment, she would have needed about an 11 percent annualized rate of return to reach $1 million after 20 years.[5] To reach that sum after taxes and fees, she would need to earn an even higher rate of return.

First of all, while possible, that's not an entirely realistic rate of return. Historically speaking, rolling 20-year returns of the S&P Index from January 1979 to December 2016 ranged from 6.4 percent to 18 percent a year.[6]

Second, her investment performance is by no means guaranteed. Not only are life insurance proceeds not subject to income taxes (although they may be included as part of the policy owner's estate for estate tax purposes) but they also are guaranteed by the insurance company.

So as you can see, life insurance can be leveraged to expand the return on an investment portfolio. This strategy is best utilized by people with excess wealth who would like to increase the value of their estate or increase the amount of money they can pass on to heirs.

Concerns and Caveats

When it comes to purchasing life insurance, there are caveats. The older you are, the more expensive the premiums. Life insurance also requires medical underwriting, so people who suffer from certain health conditions may be denied coverage. Premium rates are determined by the applicant's age, lifestyle and current health status. For permanent life insurance policies, there could be penalties should you need to withdraw or access the funds prior to beneficiaries receiving the death benefit. Withdrawals or surrenders made during a surrender charge period may be subject to surrender charges and may reduce the ultimate death benefit and cash value.

Many employers offer life insurance coverage, generally at competitive group rates. However, the coverage is typically limited to one to three times the employee’s annual salary. Therefore, it is recommended that most households purchase an additional policy separate from work. This also is a good idea because employer coverage almost always terminates when you leave your job.

Final Thoughts

If you do not currently own life insurance, consider the many reasons why it may be a good idea for your situation. If you do have a policy, recognize that this is a complex financial tool that should be monitored and potentially adjusted periodically to reflect your changing life circumstances and objectives.

Consult with an experienced life insurance professional for advice and recommendations. It is critical not only to identify any gaps in your coverage, but also to discover ways different forms of life insurance could potentially help increase your family’s financial well-being — both now and in the future.

THE Wealth REPORT

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[2] Ibid.
[3] Prudential. "Types of Life Insurance." https://www.prudential.com/personal/life-insurance/life-insurance-101/types-life-insurance. Accessed June 27, 2018.
[4] Jim T. Miller. HuffPost. Oct. 17, 2016. "This Is How Much An Average Funeral Costs." https://www.huffingtonpost.com/entry/how-much-does-a-funeral-cost_us_5804c784e4b0f42ad3d264de Accessed June 13, 2018.
[5] Bankrate.com. "Investment Calculator." https://www.bankrate.com/calculators/retirement/investment-goal-calculator.aspx. Accessed June 13, 2018.
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