



**lifeinsurance.org**

# A Guide to Understanding Life Insurance Basics

Have questions? Call 1-877-627-4048

## How much do you know about life insurance?

This guide will provide you with an overview, key terms and next steps you need to help make life insurance decisions for your specific needs.



Not sure how much coverage you need?

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life insurance agent

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## What is life insurance?

Life insurance is a contract between you and an insurance company. The agreement is that the insurance company will pay a financial benefit to your designated beneficiaries in the event of your death. The amount depends on your policy. Life insurance policies have specific conditions and limitations that vary by plan. For example, if you don't continue to pay your premiums on time or in full, the insurance company could raise your premiums or cancel the policy.

Understanding your policy is important. With the right policy, you can offer financial protection to your family even after you're gone.

## Types of life insurance

There are two main types of life insurance:



**Term**



**Permanent**

### Term Life Insurance

Term life insurance offers coverage for a predetermined period of time, usually at **lower premiums** than permanent life insurance policies. If you die during that time period and you haven't violated the terms of the contract, the insurance company pays the benefit amount to your beneficiaries. If you outlive the term, you may be able to renew the policy (possibly at higher premiums). You may be able to convert the policy to a permanent one, and some plans may offer a refund of premiums.<sup>1</sup>

<sup>1</sup> These benefits may incur additional costs.

Always make sure you are familiar with the terms and conditions of your life insurance policy before you buy.

Term life insurance is generally **a good option for individuals, young families or anyone looking for some financial peace of mind during key life stages but may not need coverage for their entire life.** These could include people paying off a mortgage or paying for their children's education.


## **Permanent Life Insurance**

**Permanent life insurance covers you for the rest of your life,** as long as you continue to pay your premiums on time and in full. When you die, your beneficiaries receive a payout from the insurance company, as long as the policy is in good standing.

**These plans can also build cash value over time.** There are different ways you can access this cash value while you are living, which could make this an attractive feature for some people.

Permanent life insurance may be a good fit for you if you want life insurance coverage that doesn't expire, or if you want to use your policy for estate planning purposes. Keep in mind that permanent life insurance policies are generally more expensive than term life insurance policies.

The chart on the following page explains the factors included in different types of life insurance.

	Life Insurance	Policy Length	Cash Value	Premium Structure	Additional Considerations
	Term	1-30 years	NO	Stay level or increase over time, depending on policy	Doesn't accumulate cash value
	Term w/ return of premiums	1-30 years	NO	Stay level or increase over time, depending on policy	Premiums are returned if policy expires <sup>2</sup>
	Whole	The rest of your life <sup>3</sup>	YES	Level	Low risk, but less lucrative than other investment options
	Universal	The rest of your life <sup>3</sup>	YES	Can vary based on taxes and what customer wants to pay	Premiums, death benefits, and frequency of payments can be changed.
	Variable Whole	The rest of your life <sup>3</sup>	YES	Level	Cash value may be at risk of losses due to underlying investments fluctuating, but also allows for greater earning potential
	Variable Universal	The rest of your life <sup>3</sup>	YES	Can vary based on taxes and what customer wants to pay	Similar to variable whole, above, but allows you to increase and decrease the death benefit

<sup>2</sup> This rider comes at an additional cost.

<sup>3</sup> As long as your premiums are paid on time.

\* Note: A permanent policy's cash value can be used to pay premiums, or may be accessed via loans or withdrawals. Policy loans and withdrawals will reduce cash values and death benefits, and may cause the policy to lapse. Additional premium payments may be required to keep the policy in force. Withdrawals may be subject to a surrender charge. Withdrawals and any unpaid loans are subject to ordinary income tax and, if taken prior to 59 1/2, a 10% federal additional tax.

## Underwriting

Traditional term or permanent life insurance policies involve a process called underwriting. The insurance company will scrutinize your application to assess your risk as policyholder. Age is the one of the biggest factors that affects the cost of your policy (or if you are accepted at all). Health is another major factor.

The underwriting process typically involves a health questionnaire and a medical exam. The medical exam is like a shorter version of a medical exam you would receive at a doctor's office. A medical examiner will typically assess your height and weight, take your blood pressure and pulse, and may also take blood and urine samples. The medical exam could include other components as well.

Other factors that may be considered in underwriting include your gender, your occupation, your driving record and your hobbies.

If traditional permanent or term life insurance isn't the right fit for you, there are some other options.

## Simplified Issue Life Insurance

Simplified issue life insurance is type of life insurance policy that **doesn't require a medical exam**. A simplified issue policy may be term or permanent.

You usually just have to answer a series of health questions. Because these plans are not fully underwritten, the **approval process is faster**. Simplified issue plans generally have **lower benefit amounts** and are generally more expensive per dollar of coverage.

These plans are usually a better fit **for those who don't want to undergo a medical exam or want to secure life insurance coverage quickly**. Your health is still a factor, and issuance of the policy may depend on answers to the health questions set forth in the application.

## The Cost of Dying

Depending on where you live, the average cost of a funeral in the United States can range anywhere from \$7,000 to \$10,000. Cremation can be a more affordable option, but even the least expensive cremation with a memorial service can still cost your family several thousand dollars.

Below is a list of the average funeral costs per service in the United States as of September 2017, according to Parting.com:

- Funeral director's service: \$1,500
- Casket: \$2,300
- Embalming: \$500
- Using a Funeral Home for Service: \$500
- Gravesite: \$1,000
- Grave digging: \$600
- Burial vault: \$1,000
- Headstone: \$1,500

**Total cost: \$8,900**

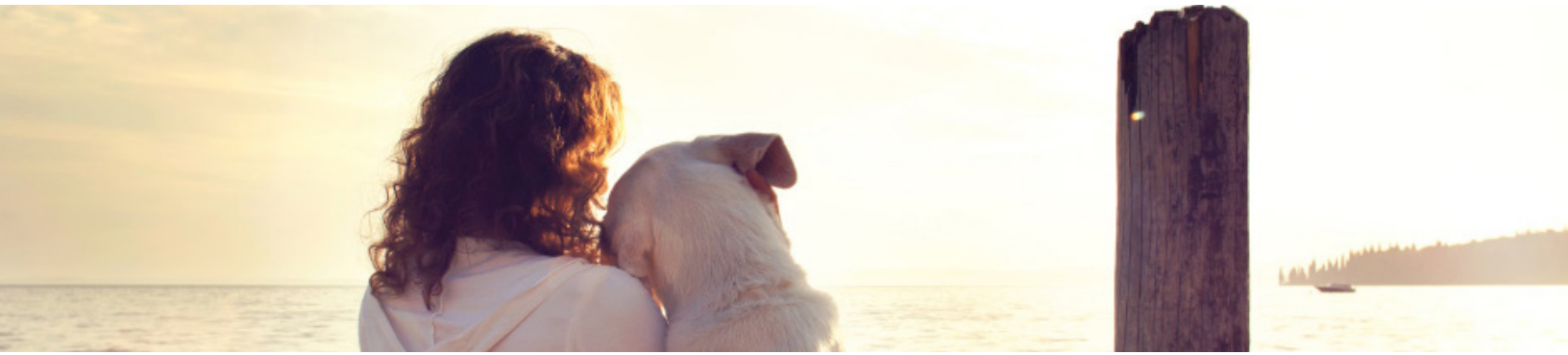
Keep in mind that these numbers are an estimate, and prices could be significantly more or less depending on your location and the providers you choose.

## Guaranteed Issue Life Insurance

Guaranteed issue life insurance is a type of permanent life insurance. These plans generally offer the **lowest benefit amounts**, but they also **don't require a medical exam or health questionnaire**. These plans are usually restricted to adults with a certain age range (ages 50 to 85 is a common range), but the age ranges may differ by carrier and by policy. Guaranteed issue plans may have a graded death benefit, meaning your family won't be able to receive the full death benefit until after the specified time period (usually two years) has passed. If you don't live beyond the graded death benefit time period, some plans will repay your premiums to your family and some may pay interest on the premiums.

Because of the limitations of these plans, guaranteed issue life insurance is usually the best fit **for those who don't qualify for other types of life insurance** based on age or health.





## How much does it cost?

Life insurance is probably less expensive than you think.

A study from Life Happens and LIMRA discovered that some people overestimate the cost of term life insurance by more than five times the actual rate.<sup>2</sup>

Premiums will vary from person to person. Generally, the factors that affect your premiums include:

- Age
- Gender
- Health
- Tobacco use
- Personal and family medical history
- Career, hobbies and lifestyle
- Driving record

### 5 ways to save on life insurance

- ① Get healthy
- ② Buy the right amount
- ③ Consider adding riders
- ④ Buy young
- ⑤ Explore your payment options

The type of life insurance and benefits you choose will also affect your cost. Premiums and policy details will also vary between insurance companies.

<sup>2</sup>"2017 Insurance Barometer Study," Life Happens and LIMRA, accessed March 6, 2018.





## How do I know how much coverage I need?

This is the tricky part. Coverage needs are different for everyone. The amount of coverage you need out of a life insurance policy depends on a few factors, including:

- Marriage and family status
- Household income
- Mortgage and other debt
- Future family plans
- Final wishes
- Current savings and investments

The best way to determine your needs is to talk to a licensed life insurance agent or use a free life insurance coverage calculator.

### Calculate your coverage needs

As a general rule, you can calculate how much life insurance you need by adding your income (times the amount of years you want to be protected) + your current debts + your future financial commitments (like college costs for your kids and your final expenses) minus your liquid assets (like your savings and current life insurance coverage).

Let's look at an example of how this could work:

John currently makes \$50,000 a year and wants coverage for at least the next 18 years, when his youngest child should be done with college. He currently owns a home and he has \$130,000 left on his mortgage. He wants to leave at least \$10,000 for his own funeral and at least \$20,000 to help pay for his children's college. He also has \$15,000 in savings and \$100,000 in life insurance from his current employer.

To play it safe (many financial professionals will recommend getting slightly more life insurance than you think you need), John could round up and look for a 20-year, \$1,000,000 policy.

So the math would be:

\$900,000 (income × 18)

+\$130,000 (debt)

+\$30,000 (future commitments)

-\$15,000 (savings)

-\$100,000 (current life insurance)

Total = \$945,000

*Hypothetical illustration for informational purposes. Your needs and situation will vary.*



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*Applications for life insurance may be subject to acceptance by insurer. Issuance of the policy may depend upon answers to health questions. Rates and coverage amounts depend upon the carrier selected. Your policy may be subject to underwriting approval. You will receive only the benefit amount in the policy issued.*

*Applications for simplified issue life insurance may be subject to acceptance by insurer. Issuance of the policy may depend upon answers to health questions set forth in the application. Rates and coverage amounts will depend upon the carrier selected.*

*Guaranteed issue life insurance policies are available to individuals within a certain age range. You will receive only the benefit amount in the policy issued. Plans may have a graded death benefit for the first two years. In order for the policy to remain in effect, premiums must be paid as they become due.*

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