



Life insurance is financial protection. It provides the resources your family may need to pay immediate and continuing expenses after you die.

WHAT YOU SHOULD KNOW

About Buying Life Insurance

There are different types of life insurance and choosing a policy is an important decision. You should begin by evaluating the ongoing and future financial needs of those who depend on you. Then become familiar with the various policies available and how they work. You'll be in a better position to make a selection best suited to your financial needs and those of your family.

The American Council of Life Insurers (ACLI) has prepared this guide to help you understand the types of life insurance available and what questions to ask when you're buying a policy.

GETTING STARTED

As you prepare to buy a life insurance policy, evaluate your ongoing and future financial needs. To begin, ask yourself some basic questions:

Why do I need to buy life insurance?

If someone depends on you financially, the likelihood is that you need life insurance. Life insurance provides cash to your family after you die. The money your beneficiary receives (the death benefit) can be an important financial resource. It can help cover daily living expenses, pay the mortgage and other outstanding loans, fund tuition, and ensure that your family is not burdened with debt. Having a life insurance policy could mean your spouse or children won't have to sell assets to pay bills or taxes (Note: Beneficiaries do not have to pay federal income taxes on the money they receive from a life insurance policy).

Stay-at-home parents also might consider life insurance to help cover the costs of services they routinely provide, such as caring for children and the home. Retirees living on limited income also may find peace of mind knowing that a surviving spouse will not be faced with a financial burden after their death.

How much life insurance do I need?

Everyone's needs are different. A life insurance agent or financial advisor can help you determine what level of protection is right for you and your family based on your financial responsibilities, sources of income, and savings. There are online calculators that also can help you; however, sitting down with an insurance professional to review your financial information can give you a more personalized view of your needs.

In general, deciding how much life insurance you need means calculating the total income that would need to be replaced upon your death to help pay for your family's financial needs. Consider ongoing expenses (day care, tuition, rent, or mortgage), immediate expenses (medical bills, burial costs, and estate taxes), and long-term financial goals (savings for college education and retirement). Your family also may need money to pay for a move or to cover daily expenses during a job search.

While there is no substitute for evaluating needs based on your own financial information, some experts suggest that if you own a life insurance policy it should pay a benefit equal to seven to 10 times your annual income. Your needs could be higher or lower depending on your unique situation.

Beneficiaries do not have to pay federal income taxes on the money they receive from a life insurance policy.

TYPES OF LIFE INSURANCE

What are the different types of insurance?

There are two basic types of life insurance: *permanent* and *term*. Permanent insurance pays your beneficiary whenever you may die; term insurance pays your beneficiary if you die during a specific period of time.

What is permanent insurance?

Permanent (cash value) insurance provides lifelong protection as long as premiums are paid. It may build up cash value over time, which grows tax deferred. With all permanent policies, the cash value is different from the face amount. The face amount is the money that will be paid to your beneficiary if you die. Cash value takes time to grow. But after you've held the policy for several years, its cash value can offer you several options:

- You can borrow from the insurer using your cash value as collateral. You can get the loan even if you don't have a good credit history. If you don't repay the loan (including interest), it will reduce the amount paid to your beneficiaries after your death.
- You can use the cash value to pay your premiums or to buy more coverage.
- You can exchange the policy by using the cash value for an annuity that will provide a steady stream of retirement income for life or a specified period.
- You can cancel (surrender) the policy and receive the cash value in a lump sum. You will pay taxes on the value that exceeds what you've paid in premiums.

Basic types of cash value insurance

- **Whole life** offers premiums that generally stay fixed over the life of the policy, a fixed death benefit, and cash value that grows at a fixed rate of return.
- **Variable life** allows you to choose among a variety of investments offering different risks and rewards—stocks, bonds, combination accounts, or options that guarantee principal and interest. Death benefits and cash value will vary depending on the performance of the investments you select. By law, you'll be given a prospectus for variable life insurance. This prospectus will include financial statements and outline investment objectives, operating expenses, and risks. The cash value of a variable life policy is not guaranteed. If the market doesn't perform well, the cash value and death benefit may decrease, although some policies guarantee that the death benefit won't fall below a certain level.
- **Universal life** gives you flexibility in setting premium payments and the death benefit. Changes must be made within certain guidelines set by the policy; to increase a death benefit, the insurer usually requires evidence of continued good health. A universal life policy can have a variable component.

The money your beneficiary receives can help cover expenses and ensure that your family is not burdened with debt.

What is term insurance?

Term insurance provides protection for a defined period of time—from one year to 10, 20, or even 30 years—and pays benefits only if you die during that period. Term insurance is often used to cover financial obligations that will disappear over time, such as tuition or mortgage payments. Premiums for term insurance either can be fixed for the length of the term or can increase at a point specified in the policy. They also can be less expensive than for a cash value policy.

Term policies can include a return of premium benefit that will generally return all of the premiums paid at the end of a specified term if no death benefit was paid. Term policies with this feature are more expensive than those without.

Some term policies can be renewed at the end of a term. However, premium rates will usually increase upon renewal. To qualify for renewal at the lowest rates, many policies require evidence of insurability (continued good health). At the end of a term, you also may be able to convert the policy to a permanent policy. Term policies don't usually build up a cash value.

WHAT ARE THE ADVANTAGES AND DISADVANTAGES OF EACH TYPE OF INSURANCE?

Cash Value Insurance

Advantages

- Lifelong protection as long as the premiums are paid.
- Premium costs that can be fixed or flexible to meet individual financial needs.
- Cash value, which can be: used to pay premiums or buy more coverage; borrowed against; converted to an annuity; or surrendered for cash.

Disadvantages

- Cash value insurance is designed to be kept for the long term; therefore, cancelling a cash value policy after only a few years can be expensive.

Term Insurance

Advantages

- A policy can cover financial obligations that will disappear over time, such as a mortgage or college expenses.
- Premiums are generally lower than those for cash value insurance at younger ages.

Disadvantages

- Provides protection for a specific period of time, not for life.
- Renewing coverage at the end of the term generally means premiums will increase.
- Policies don't usually build up a cash value.

HOW TO PURCHASE: CHOOSING A COMPANY OR AGENT

You can buy life insurance at an insurance agency, brokerage firm, bank, or directly from a life insurance company on the Internet, over the phone, or by mail. Most companies have websites describing their products and services and some sites will direct you to a local agent.

How do I choose a company?

Contact your state insurance department for a list of companies licensed in your state, then:

- Ask friends and relatives for recommendations based on their own experiences.
- Talk to an insurance agent or broker.
- Conduct an Internet search.
- Research companies at a public library.

Generally speaking, life insurers are in excellent financial health. They're required by law to maintain reserves to guarantee that they can meet obligations to their policyholders. However, you should still verify a company's financial strength.

You can check any company's financial condition by looking at its rating. Rating agencies, including A.M. Best Company, Fitch Ratings, Moody's Investor Services, Standard and Poor's Insurance Ratings Service, and Weiss Ratings evaluate the financial strength of companies. Rating information is available online or in publications usually found online or in the business section of your public library.

How do I choose an agent?

Collect the names of several agents through recommendations from friends, family, and other sources. Find out if an agent is licensed in your state to sell insurance by checking with your state's insurance department. Agents who sell variable products also must be registered with the Financial Industry Regulatory Authority (FINRA), and have an additional state license to sell variable contracts.

The agent should be able and willing to explain the different kinds of policies and other insurance-related matters.

Agents often belong to professional associations that offer continuing education and grant professional credentials. The National Association of Insurance and Financial Advisors offers local educational seminars for agents. The Society of Financial Service Professionals and the Financial Planning Association offer similar training for financial professionals. Agents may earn such professional designations as Chartered Life Underwriter (CLU) and Life Underwriter Training Council Fellow (LUTCF). Agents who also are financial planners may carry such credentials as Chartered Financial Consultant (ChFC), Certified Financial Planner (CFP), or Personal Financial Specialist (CPA-PFS).

WORKING WITH AN AGENT

What should an agent do for me?

The agent should be able and willing to explain the different types of policies and other insurance-related matters. You should feel satisfied that the agent is listening to you and looking for ways to find the right type of insurance at an affordable price. If you're not comfortable with the agent, or you aren't convinced he or she is providing the service you want, interview another agent.

What should I expect during my meeting with an agent?

An agent will begin by discussing your financial needs. You should have basic personal financial information available—along with a general idea of your goals—before you meet or talk with an agent. He or she will ask questions about your family income, other financial resources you might have, and any debts. The agent will be better able to assess your needs with the information you provide.

What types of questions will I be asked?

In addition to questions about finances, be prepared to answer questions about your age, medical condition, family medical history, personal habits, occupation, and recreational activities.

Always answer questions truthfully; a company will use this information to evaluate your risk and set a premium for your coverage. For instance, you'll pay a lower premium if you don't smoke; on the other hand, if you have a chronic illness, you can expect a higher premium. When it's time to submit a claim, the accurate and truthful answers you provided the agent will enable your beneficiary to receive prompt and full payment.

When you apply for life insurance, you may be asked to take a medical exam. In many instances, a licensed health care professional hired and paid for by the life insurance company will make a personal visit to your home to conduct the exam.

EXAMINING A POLICY

How do I know if a life insurance policy is right for me?

Read the policy carefully to make sure it meets your personal goals. Because your policy is a legal document, it's important that you understand exactly what it provides. Ask for a point-by-point explanation for anything that is unclear and make sure the agent explains items you don't understand.

If your agent recommends a cash value policy, ask:

- Are the premiums within my budget?
- Can I commit to these premiums over the long term?

Cash value insurance provides protection for your entire life. Cancelling a cash value policy after only a few years can be a costly way to get short-term insurance protection. If you don't plan to keep the policy for the long term, consider another type of coverage such as term insurance.

If you're considering a term policy, ask:

- How long can I keep this policy? If I want to renew it for a specific number of years, or until a certain age, what are the renewal terms?
- Will my premiums increase? If so, will increases start annually or after five or 10 years?
- Can I convert to a cash value policy? Will I need a medical exam if and when I convert?
- If it has a return of premium benefit, ask: What would the policy cost without this benefit? Will all of the premiums be refunded?

Is a policy illustration a legal document, like a contract?

A policy illustration is not part of the life insurance policy and is not a legal document. Legal obligations are spelled out in the policy contract. A policy illustration, however, can help you understand how a policy works.

What is in a policy illustration?

A policy illustration is meant to provide an example, based on certain assumptions, of how a policy's costs and benefits may develop over time—including, but not limited to, premium amounts owed, cash values, and death benefits. For a term policy, the illustration extends to the end of the term. With a cash value policy, the illustration extends past your 100th birthday.

Your actual costs and benefits could be higher or lower than those in the illustration because they depend on the future financial results of the insurance company. However, when figures are guaranteed, the insurance company will honor them regardless of its financial success. Ask your agent which figures are guaranteed and which are not.

A policy illustration can be complicated. Your agent or financial advisor can explain information you don't understand.

What should I look for in a policy illustration?

Study the policy illustration to answer the following:

- Is my classification (i.e., smoker/nonsmoker, male/female) correct?
- When are premiums due—monthly, annually, or according to some other schedule?
- Which amounts are guaranteed and which are not?
- Does the policy have a guaranteed death benefit or could the death benefit change depending on interest rates or other factors?
- Does the policy offer dividends or interest credits that could increase my cash value and death benefit or reduce my premium?
- Will my premiums always be the same? Could premiums increase if future interest rates or investment returns are lower than the illustration assumes?
- If the illustration shows that I won't have to make premium payments after a certain period of time, is there any chance I would have to start making payments again at any time in the future?

AFTER PURCHASE

After purchasing your life insurance policy, keep it with other financial records or legal papers, or anywhere your survivors are likely to look for it if they need to file a claim. As a precaution, you shouldn't store a life insurance policy in a safe deposit box. In most states, boxes are sealed temporarily upon one's death, which could delay the claims process.

Keep your agent's name and contact information easily accessible. The agent can help your beneficiaries fill out the necessary forms and act as an intermediary with the insurance company.

Review your life insurance policy from time to time to be certain it continues to meet your needs as your circumstances change, such as the birth of a child, a job promotion, divorce, remarriage, or retirement. Also, review it to ensure your beneficiaries are correctly named.

FREQUENTLY ASKED QUESTIONS

What happens if I miss a payment?

If you miss a premium payment, you usually have a 30- or 31-day grace period in which to make your payment without consequences. If you die within the grace period, your beneficiary will receive the death benefit minus the overdue premium. However, the policy will lapse (terminate) if you don't make your payment by the end of the grace period. If you own a cash value policy, your company—with your authorization—can draw from your policy's cash value to pay the premium. This method of keeping your policy active can work only as long as your cash value lasts.

Do I have any recourse if my policy lapses?

Some life insurance contracts let you reinstate a lapsed policy within a certain time frame. However, you must prove insurability, pay all overdue premiums (plus interest), and pay off any outstanding policy loans.

An accelerated benefits rider lets you, under some conditions, receive the death benefits of your life insurance policy before you die.

In addition to the death benefit, are there other features I should be aware of when considering a life insurance policy?

Many policies offer purchase options or riders. Some riders let you buy more insurance without taking a medical exam; others waive premiums if you become disabled. Some policies offer an accidental death benefit that pays an additional amount if death occurs as a result of an accident. Some companies offer accelerated benefits, also known as living benefits. An accelerated benefits rider lets you, under some conditions, receive the death benefits of your life insurance policy before you die. Such conditions may include terminal or catastrophic illness, confinement to a nursing home, or need of other long-term care services. You also can purchase a long-term care rider that allows you to use the policy's cash value to pay for long-term care expenses.

When will my policy take effect?

If you decide to buy a policy, find out when the insurance becomes effective. That date may be different from the date the policy is issued.

How is life insurance taxed?

Your beneficiaries will not pay income taxes on death benefits. If you own a cash value policy, you won't pay income taxes on the cash value unless you cancel the policy and withdraw the money. Then you'll pay taxes on the amount that exceeds what you've paid in premiums.

Make sure that you fully understand any policy you're considering and that you're comfortable with the company, agent, and product. Most states require insurers to provide a buyer's guide to explain life insurance terms, benefits, and costs. Ask your agent for a copy of the life insurance company's guide and follow the tips below:

BEFORE PURCHASE

- Check with your state insurance department to make sure the company and agent are licensed in your state.
- Look for a company that is reputable and financially strong. A number of insurance rating services rate the financial strength of companies. You can get such information from your agent, on the Internet, or at public or business libraries. Rating agencies include A.M. Best Company, Fitch Ratings, Moody's Investor Services Inc., Standard & Poor's Insurance Ratings Services, and Weiss Ratings.
- Ask for outlines of coverage so you can compare the features of several policies.
- Always answer questions on your life insurance application truthfully.
- Be sure your application has been filled out accurately. Promptly notify your agent or company of errors or missing information.
- When you buy a policy, make your check payable to the insurance company, not the agent. Be sure to get a receipt.
- Beware of offers for "free" life insurance. Investors may approach some seniors to offer them money to buy life insurance and then sell the policy to the investors. The investors expect to profit by receiving the death benefit when the senior dies. Often called stranger-originated life insurance, legislators and regulators are concerned about these transactions because they violate public policies against wagering on human life. Also, there may be hidden pitfalls, such as unexpected taxes, fees, and loss of privacy.
- Contact the company or agent if you don't get your policy within 60 days.
- Always check the date the insurance becomes effective.

AFTER PURCHASE

- After you've bought an insurance policy, you may have a "free-look" period—usually 10 days after you receive the policy—when you can change your mind. During that period, read your policy carefully. If you decide not to keep it, the company will cancel the policy and give you an appropriate refund. Information about the free-look period is in your contract.
- Keep your life insurance policy with your other financial records or legal papers, or anywhere your survivors are likely to look for it. However, don't keep your policy in your safe deposit box. In most states, boxes are sealed temporarily upon the death of the owner, delaying a settlement when funds may be needed most.
- Contact your original company, agent, or financial advisor before cancelling your current policy to buy a new one. If your health has declined, you may no longer be insurable at affordable rates. If you replace one cash value policy with another, the cash value of the new policy may be relatively small for several years.
- If you have a complaint about your insurance agent or company, contact the customer service division of your insurance company. If you're still dissatisfied, contact your state insurance department. A state insurance department directory is available on www.acli.com.
- Review your policy from time to time or when a major event occurs in your life—such as a birth, job promotion, divorce, remarriage, or retirement—to be sure your coverage is adequate and your beneficiaries are correctly named.
- Visit www.acli.com for more consumer resources and information about life insurance.

The American Council of Life Insurers (ACLI) is a Washington, D.C.-based trade association with approximately 300 member companies operating in the United States and abroad. ACLI advocates in federal, state, and international forums for public policy that supports the industry marketplace and the 75 million American families that rely on life insurers' products for financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing more than 90 percent of industry assets and premiums. **www.acli.com**.

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