Life Insurance

Types of Products

The primary reason for purchasing life insurance is to provide dependents with financial protection in the event of an untimely death; however, numerous other applications exist such as: estate planning, business continuation and succession planning, retirement planning, and other wealth transfer utilizations.

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Life insurance is a contract between a life insurance carrier and a policyowner whereby the carrier agrees to pay beneficiaries a predetermined dollar amount upon the death of the insured person(s) subject to the contract terms. The primary reason for purchasing life insurance is to provide dependents with financial protection in the event of an untimely death; however, numerous other applications exist such as: estate planning, business continuation and succession planning, retirement planning, and other wealth transfer utilizations. Furthermore, certain types of life insurance may provide living benefits, where cash values grow on a tax-deferred basis and may be accessed without incurring income tax liability.[1]

There are two basic forms of life insurance, term and permanent, which may be further sub-divided as detailed below. The appropriate product is based on your needs and objectives determined by your Baird Financial Advisor during the financial planning process.

TERM LIFE INSURANCE

Term insurance provides death benefit coverage only during the term of the contract and does not accumulate cash value. Coverage terminates at the end of the contract term or earlier if premium payments cease. Most term insurance policies may be converted to permanent insurance with the same company for a specified period of time without providing evidence of insurability. Premiums for term insurance are the least expensive of all life insurance policies.

Common Types of Term Life Insurance

Annual Renewable Term (ART)

- Death benefit remains level
- Premiums increase each year on the each policy anniversary date
- Policy renews annually, if premiums are paid, up to a specified age

Level Premium Term

- Death benefit and premiums remain level for the entire term period
- Terms typically range from 10-30 years
- Policies typically move to ART at the end of the policy term period

Return of Premium Term (ROP Term)

- Death benefit and premiums remain level for the entire term period
- Terms typically range from 10-30 years
- Provides a schedule for a return of premiums paid with a full refund at the end of the term

Consider Term Insurance if You:

- Are concerned about affordability (lower premiums allow you to buy higher coverage)
- Have a specific temporary need to cover (mortgage, car payment, college costs, etc.)
- Don't have a need to build cash value
- Have permanent insurance to cover your other needs

PERMANENT LIFE INSURANCE

Permanent life insurance is intended to provide a death benefit for the life of the insured, subject to the terms, design and performance of the contract. A key difference between term insurance and permanent insurance is the tax-deferred cash value element offered by permanent insurance. When properly structured, cash values may be accessed on a tax-advantaged basis through the use of withdrawals and/or loans.[1]

Common Types of Permanent Life Insurance

Whole Life Insurance

- Premiums required for the life of the insured or for a specified period of time (e.g. 10 years or age 65)
- Cash value grows at a rate that will enable it to equal the death benefit at policy maturity
- "Participating" policies return a portion of the premium as a non-guaranteed dividend

Universal Life Insurance

- Premiums may be flexible
- Cash value grows at a fixed interest rate, typically declared annually at anniversary, with a contractually-guaranteed minimum
- Some emphasize guaranteed death benefit protection and de-emphasize cash value

Index Universal Life Insurance

- Premiums may be flexible (life universal life)
- Cash value and, in some cases, death benefit are tied to the performance of a specified index (typically the S&P 500) up to specified caps and participation rates
- Some provide limited or full death benefit guarantees regardless of the index performance

Variable Universal Life Insurance[2]

- Premiums may be flexible (like universal life)
- Cash value and, in most cases, death benefit are based on the performance of mutual fund-like investment options (sub-accounts) chosen by you and/or your advisor
- Some provide limited or full death benefit guarantees regardless of sub-account performance

Survivorship Life Insurance

- One policy covering two lives and based on joint life expectancy
- Lower premiums than separate policies on each insured
- Proceeds are payable upon the death of the second insured
- May come in the form of universal life, variable universal life or whole life

Consider Permanent Insurance if You:

- Need long-term protection against life's uncertainties
- Desire the potential for tax-deferred cash accumulation
- Are funding an estate or business succession plan

LIFE INSURANCE RIDERS

When you buy a life insurance policy, you will probably have the opportunity to select one or more riders to add to the policy. Riders are amendments that expand or restrict a policy's benefits, typically for an additional premium. Some of the more common riders are:

Accidental Death and Dismemberment

- Pays an additional benefit for death resulting from an accident or for a specific injury such as the loss of both legs or both arms, or blindness in both eyes
- Child Rider
- Provides death benefit protection for children of the insured
- Children born or legally adopted after the policy is issued are also covered
- Coverage typically purchased in units (e.g. $1,000 per unit)
- Coverage typically continues until age 21

Chronic Illness Rider

- Accelerates the death benefit to help pay for costs associated with a chronic illness
- Eligibility requires a physician to certify that the illness is likely to last the rest of the insured's life
- May not be marketed or presented as a long-term care rider
- Generally benefits paid from the Chronic Illness rider reduce the death benefit dollar-for-dollar
- Any portion of the death benefit not used will be paid to the beneficiaries as a death benefit
- Typically there is no residual death benefit in excess of the original death benefit amount

Long-Term Care (LTC) Rider

- Accelerates the death benefit to help pay for the costs of long-term care services
- Eligibility requires that the insured be unable to perform at least two of six Activities of Daily Living (ADLs) without substantial help for at least 90 days or diagnosed with a cognitive impairment
- Generally benefits paid from the LTC rider reduce the death benefit dollar-for-dollar
- Any portion of the death benefit not used will be paid to the beneficiaries as a death benefit
- Maximum monthly benefits according to the IRS per diem limits apply
- Typically has a residual death benefit of 10-25% of the original specified amount

Waiver of Premium

- Premium is waived if you become disabled or seriously ill
- Usually requires disability for a specified amount of time, such as six months before benefit takes effect

This material is provided courtesy of Baird and its Financial Advisors. It contains references to concepts that have legal, accounting and tax implications. It is not intended as legal, accounting or tax advice. Consult your own attorney and/or accountant for advice regarding your particular situation. Death benefit proceeds are generally received federal income tax free as provided in Internal Revenue Code Section 101(a). There are some exceptions to this general rule, including certain changes in ownership and payment of any additional interest at death.

[1] Both loans and withdrawals from a permanent life insurance policy may be subject to penalties and fees and, along with any accrued loan interest, will reduce the policy's account value and death benefit. Depending upon the performance of the policy, the account value may be worth more or less than the original amount invested in the policy. Assuming a policy is not a Modified Endowment Contract (MEC), loans are free from current Federal taxation and withdrawals are taxed only to the extent that they exceed the policyowner's basis in the policy. Distributions from MEC's are subject to Federal income tax to the extent of the gain in the policy and taxable distributions are subject to a 10% additional tax, with certain exceptions.

[2] Investors should carefully consider the investment objectives, risks, charges, and expenses of variable universal life product and the underlying investment options before investing. This and other information can be found in the prospectus or summary prospectus for the variable universal life product and the prospectuses or summary prospectuses for the underlying investment options, which can be obtained by contacting a Baird Financial Advisor. Please read them carefully before you invest.