Financially Speaking

With Trisha Arndt, CFP®

Oops… Maybe You Don't Have as much Life Insurance as you Thought

Over the years I have found that there are many common mistakes that people make as it relates to their finances. Some are conscious decisions – such as electing not to contribute enough to a 401k to receive the full employer match – but many are completely unintended mistakes resulting from a lack of knowledge or a misunderstanding.

One of the most common such mistakes relates to life insurance. While almost everyone struggles with determining how much coverage they should have, a large number of people that come to see me for the first time have some coverage in force – or at least they think they do.

There are a number of ways that people can obtain life insurance. The most common method is through an employer (your own or a spouse's). Most people that have such coverage know that they have something but aren't necessarily sure of what they have or how it will work over time.

I typically see that people either have whatever amount of coverage that the employer provides free of charge or, possibly, they have added voluntary coverage up to the amount that can be issued without an exam. Many people don't realize that the coverage is tied to that employment and if that job ends the coverage often does too. There is often an option to convert the coverage to a privately owned policy upon leaving but the conversion option is generally limited to a form of coverage that can be substantially more expensive than it had been while working. Still, if someone has health conditions that would preclude them from buying coverage on their own it is an option to seriously consider.

Outside of something tied to employment the most common type of coverage I see are individual policies bought with the assistance of an insurance agent. While people are often confused by the type of coverage they have – term, universal life, variable universal life, whole life, etc. – they generally have an idea of the coverage amount and they have a resourrce to go to with questions.

Regardless of how the life insurance is obtained, it is not uncommon for people to not fully understand what they have. But at least they can be fairly confident that if the unforeseen happens and they die with the coverage in force that their beneficiary will receive the benefits.

Or can they be sure of that?

Sadly, one of the most common misunderstandings that I see people have is to think that they have life insurance that will pay under any circumstance when what they really have is a form of accidental death insurance.

Accidental death insurance is sometimes offered through an employer but more commonly it is bought as part of an offer received in the mail or read on-line. It is attractive because it generally is issued without underwriting (i.e. health questions) and it seems inexpensive for the amount of coverage you receive.

There is a reason for that.

While accidental death insurance is life insurance it will not necessarily pay benefits if the covered individual dies. Why? Because it pays benefits only if an individual dies as the direct result of an accident – i.e. is "hit by a bus". If death is attributed to any sort of natural cause – think cancer or a heart attack – an accidental death policy may pay absolutely nothing. In some cases accidental death policies may not even pay if a person lives too long after suffering an accident or may only pay if someone dies in one of a list of specifically covered types of accidents. In short, you can't depend on it to take care of your loved ones if something happens to you.

Because accidental death policies are relatively inexpensive some people will elect to have them as a potential supplement to their other coverage. There is no reason not to do so – they can serve a valid place in a well thought out plan. But, if you think you have all of the life insurance you need and you pull out your policy and see the word "accidental" in the policy name you better think again. It's time to visit with a qualified insurance agent and financial planner to get a good handle on what you really have.

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