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THE WHITE PAPER

Your Retirement Planning Newsletter

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Life Insurance: What Kind Should You Get, and How Much Do You Need?

Do you need life insurance? If there are individuals who depend on you for support -- financial or otherwise -- you probably do. But, what kind, and how much? Included here are some definitions that can help you familiarize yourself with insurance products.

Types of Insurance

There are many different types of insurance coverage. Here are five of the most prevalent.

- **Term** insurance is the most basic, and generally least expensive, form of life insurance for people under age 50. A term policy is written for a specific period of time, typically 1 to 10 years, and may be renewable at the end of each term. Be warned: The premiums increase at the end of each term and can become prohibitively expensive for older individuals. A level term policy locks in the annual premium for periods of up to 30 years.
- **Whole Life** combines permanent protection with a savings component. As long as you continue to pay the premiums, you are able to lock in coverage at a level premium rate. Part of that premium accrues as cash value. As the policy gains value, you may be able to borrow up to 90% of your policy's cash value tax free, although loans reduce the policy's death benefit and cash value, and may trigger a taxable event if the policy lapses.
- **Universal Life** is similar to whole life with the added benefit of potentially higher earnings on the savings component. Universal life policies are also highly flexible in regard to premiums and face value. Premiums can be increased, decreased, or deferred, and cash values can be withdrawn. You may also have the option to change face values. Universal life policies typically offer a guaranteed return on cash value. You'll receive an annual statement that details cash value, total protection, earnings, and fees.
- **Variable Life** generally offers fixed premiums and control over your policy's cash value. Your cash value is invested in your choice of stock, bond, or money market funding options.[1] Cash values and death benefits can rise and fall based on the performance of your investment choices. Although death benefits usually have a floor, there is no guarantee on cash values. Fees for these policies may be higher than for universal life, and investment options can be volatile. On the plus side, capital gains and other investment earnings accrue tax-deferred as long as the funds remain invested in the insurance contract.
- **Universal Variable Life** insurance is the most aggressive type of policy. Like variable life, you can choose from a variety of investment options. However, there are no guarantees on universal variable policies beyond the original face value death benefit. These policies are probably best suited to affluent buyers who can afford the risks involved.

How Much Do You Need?

A popular approach to buying insurance is based on income replacement. In this approach, a formula of between five and ten times your annual salary is often used to calculate how much coverage you need. Another approach is to purchase insurance based on your individual needs and preferences. To do so, start off by determining your net earnings after taxes. Then add up all your personal expenses such as housing, health care, food, clothing, transportation expenses, etc. This represents the amount that your insurance will need to replace. You'll want a death benefit amount that, when invested, will provide income annually to cover this amount. Then, you should add to that the amounts needed to fund one-time expenses such as college tuition for your children or paying down mortgage or debt.

Income replacement for nonworking spouses is an important and often overlooked insurance need. Coverage should provide for your costs for day care, housekeeping, or nursing care. Add to this any net earnings from part-time employment. Finally, estimate your own "final expenses" such as estate taxes, uninsured medical costs, and funeral costs.

For more information, contact an insurance professional.

[1]*Investing in stocks involves risks, including loss of principal. Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and are subject to availability and change in price. Investing in a money market fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the fund.*

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