PAGE and ASSOCIATES

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Client Information Summary

Types of Life Insurance

The potential loss of income due to death is a key consideration in the creation and preservation of wealth. Until an individual has created sufficient wealth to provide adequate income for their family in the event of their death, it is vital to ***manage*** this potential risk. In most situations, the risk can be managed by ***transferring*** the potential loss to an insurance company through the acquisition of life insurance.

Factors to consider

There are five basic financial factors one should consider when purchasing life insurance:

1. **Last Expenses:** When an income earner dies, his or her last expenses generally become the family's first expense. These expenses may take the form of medical bills, funeral costs, outstanding loans or unpaid taxes. Insurance coverage can provide for any such expenses, so that they do not become a financial burden upon your family.

2. **Spouse's income:** Will the surviving spouse have any means of generating employment income for support? If not, you will likely want sufficient coverage to ensure their comfort and continued standard of living.

3. **Dependency period income:** If you have children, you will likely want to leave them provided for, particularly during the dependency period, which runs from the time the income earner dies until the children are grown and can support themselves.

4. **Education Fund:** Most parents also want to make certain that future tuition and living expenses will be covered, to ensure that their children obtain a good education.

5. **Mortgage Fund:** Insurance may also be used to pay off a mortgage upon the income earner's death, thereby reducing the demands on the family's remaining financial resources.

Once you have assessed the particulars of your circumstances, a determination can be made as to which of the following types of life insurance would best suit your needs and your current financial means.

Term Insurance
(5, 10, 20 Year & to Age 65)

Term insurance is the most competitive and easily compared type of insurance, and relatively simple to understand. It is purchased at a specific cost (or premium) for a specified period of time (for instance, a term of 5, 10, or 20 years).

Term insurance is insurance in its purest form, with no savings component, and should be acquired when available cash flow is limited and a certain amount of coverage is needed for a particular length of time. Probably the most competitive and most available version is Term 10. With Term 10, the premium stays level for 10 years, and then rises for each successive renewal period of 10 years until the maximum renewal age is reached (typically age 80).

Policy Provisions

Generally, a term policy would expire after the specified term of insurance, unless otherwise provided for in the policy provisions, which are the terms and conditions of the policy as contained in the insurance contract. Some of the provisions contained in insurance contracts are required by law; however, other provisions are offered by insurance companies in a bid to stay competitive with other insurance providers. The following two provisions, in particular, can provide you with future options, which may be desirable:

Renewability Provision

"Renewable" means the policy can be renewed at the end of the term, for another term usually of the same length as the first, without further proof of insurability being required. For instance, if you were to purchase a five year renewable term policy, you would be required to pass a medical exam to prove eligibility for insurance. Five years later, when the contract expired, you could elect to renew the contract under the same terms (but with a pre-determined increase in the premiums), without having to undergo a further medical exam. For a Term 10 policy, as a rough rule of thumb, each renewal rate will be about 3 to 4 times the previous rate. We generally recommend that clients go back to the market and reapply for new insurance at each renewal point, and, depending on the their health, they might get a renewal rate that is only about 2 times the previous rate.

Conversion Provisions.

Convertible term policies allow the holder to convert the policy to a Whole life policy (a type of permanent insurance), without providing further evidence of insurability. For example, if your term insurance contract automatically renewed every 5 years, you might decide, at age 50, to convert it to a Whole life policy rather than let it terminate when you turn 65. Exercising this option would provide you with a more permanent type of insurance, without you having to provide new evidence of insurability, regardless of any health concerns or issues which may have arisen since the purchase of the policy.

Term To 100

Term to 100 is a form of "permanent insurance" that matures when the insured either reaches the age of 100 or dies, whichever comes first. Such insurance usually does not have a savings component. Premiums are fixed on a monthly or annual basis and will not increase for the life of the policy.

Term to 100 insurance should be acquired when there is a long-term need for a specific amount of insurance, which extends beyond retirement, and limited cash flow is available. Term to 100 rates will be much higher than Term 5, 10 or 20 rates because the insurance stays level for the life of the insured.

Living past the age of 100

In the event that the insured individual lives beyond the age of 100 (as some of us will!), the policy will usually either *endow*, meaning that it will pay out the face amount of the policy at that time, or be considered *paid up*, meaning that no future premiums would be required to keep the policy in force, for the remainder of the insured person's life.

Universal Life

Another type of *permanent insurance,* Universal life is a combination of a term life insurance policy and a tax-deferred savings or investment program. Originally developed as a form of "de-bundled" whole life (see below), Universal Life breaks up the life insurance and savings components into their separate pieces in such a way that the underlying assumptions and costs can be seen.

Universal life policies provide a high degree of flexibility by separating the three main parts in the life insurance contract: the cost of insurance, the administration expenses, and the cash value build up.

An insured person's deposits are credited to the policy as they are paid. Normally, an insurance company will then subtract the cost of the insurance, as well as certain administration expenses. The balance would be available for investment within a tax- sheltered environment.

Flexible Premiums

A particularly attractive feature of Universal life is the fact that the policy owner can vary his or her annual premium, based upon their financial situation at any given time. Thus, if you had a Universal life policy that covered your life for $100,000, but your current circumstances required you to buy a new car and replace the roof on your home, you could elect to only pay half of your annual Universal life deposit. The balance of the deposit would be taken out of the cash value built up in the policy. This would allow you to maintain the policy, and meet the cash flow required for home repairs and the purchase of a new vehicle. This flexibility goes the other way too, with the policy holder having the option to overfund the policy, which would increase the savings component. There are limits to the overfunding defined by the MTAR limit (Maximum Tax Actuarial Reserve), which are complex rules from the federal government. If these limits are exceeded, the policy becomes non-exempt (the insurance companies do not allow this to happen).

Flexible Investments

Universal life also offers policy owners the option of choosing where their money will be invested within the tax deferred savings or investment component of the policy. The investment possibilities include savings accounts, guaranteed term deposits, mutual funds and indices that track the performance of market indexes like the S&P 500 or S&P/TSE60. This means that you could, for instance, change the investments in your Universal life plan from term deposits to a more aggressive investment option, such as a stock-index linked account, in order to make up for reduced deposits.

Whole Life

Whole Life is also a type of *permanent insurance*, although it is normally less flexible than Universal life. There are many variations of Whole life, but our comments here are confined to what is referred to as "participating whole life," which means that the policy holders participate in the upside of an insurance company's ability to manage its reserves, by way of the payment of dividends.

The long-term performance provided by this type of insurance reflects the actual results the insurance company achieves, relative to their death claims and operating expenses. However, the greatest factor governing performance of the policy is the investment return the company achieves on the surplus premiums collected.

Any excess premiums collected by the insurance company are refunded to the policyholder in the form of a "dividend," which can be either received in cash or re-invested to increase the death benefits and/or cash value of the policy.

Premiums for this type of insurance are always greater in the early years than the actual cost of the insurance. The degree to which the premium exceeds the actual cost of insurance will determine the long-term cash accumulation that takes place within the policy. Usually, the higher the premium, the higher the cash value accumulation will be.

Another benefit is the fact that the funds accumulating within the Whole life policy are not subject to taxation, provided the contract falls within the limits of what the Canada Customs and Revenue Agency categorizes as an exempt policy (see the discussion above under Universal Life).

Whole life should be utilized when there is a permanent, long-term need for coverage that extends beyond retirement, and personal cash flow is sufficient to fund the premiums.

Joint Life Insurance Policies

A joint life insurance policy is a policy in which the need for insurance is based upon two lives. The cost of the insurance policy is also based upon the ages and the health of both persons insured.

There are basically two types of Joint life policies:

Joint 1st to Die

This type of Joint life pays out the death benefit after the first person dies. Because the there are 2 people at risk, the costs will be greater than for a single life policy. For example:

Mark and Jennifer are married and both are employed. If either of them were to die, the survivor would need $200,000 of capital to provide the income to maintain their standard of living, so they purchased a joint 1st to die life policy for $200,000.

Joint last to Die

A joint last to die policy, on the other hand, covers a minimum of 2 lives and pays the death benefit upon the death of the last insured individual. Because both have to die before the policy pays out, the costs are less than for a single life policy. For example:

Mark and Jennifer are married and own a small business corporation. Capital gains tax will be payable on the appreciation of the corporate shares when the last of them dies. To preserve their estate for the children, they purchased a Joint last to die insurance policy for $400,000, to cover their capital gains tax upon death.

Term, Universal Life and Whole Life policies can all be established as Joint life policies. We can also combine policies using riders. For example, a Term 100 policy can have a Term 10 rider, which saves on policy costs (roughly $125 per year).

Summary

Choosing the right type of life insurance can be a complicated decision. However, the decision becomes easier when you know how much coverage you need, how long you need it for, and the current and future cash flow you can allocate to premiums, without any detrimental effect to your personal financial strategy.

Your Page financial advisor would be pleased to assist you in assessing your insurance needs, within the context of your overall financial strategy, to make sure that the coverage you choose best suits your specific circumstances and the needs of your family.

Page Client Information Summary

Edited by: Jonathan Flawn CA, CFP, CLU

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Head Office:
405-95 Mural Street Richmond Hill, Ontario L4B 3G2
Phone: (905) 884-5563
Fax: (905) 884-3365
www.askpage.com