Life Insurance as a Financial Planning Tool

Fifth Third Bank

Life insurance is a key financial planning tool that can often be overlooked. However, life insurance can help build an estate for those who die prematurely prior to accumulating sufficient assets on their own and can also be an integral part of your overall financial planning efforts.

Why do you need life insurance?

There are many reasons you could need life insurance, among them:

- **Protecting your family while they're young.** Families with young children should consider life insurance in the event one or both parents die prematurely. The death benefit can help offset lost income and can help fund goals like college for the children.
- **Boosting the overall value of the policy.** Some types of policies offer a combination of death benefit and investment options.
- **Funding a buy-sell arrangement in conjunction with a succession plan for a business.** A buy-sell can facilitate an orderly transition for a company in the event that one of the owners or partners dies unexpectedly. A life insurance policy can fund a buyout of the deceased owner's share of the company via a pre-arranged valuation, providing liquidity for the late owner's family and heirs.
- **Key man coverage for a business.** This is a policy purchased on the life of a key executive or on another essential employee. The thought is that in the event

of this employee's death, the company could suffer from a leadership void, it could jeopardize some client relationships, etc. The death benefit can buy the company time to replace this individual and to implement alternative strategies if needed.

- **Meeting estate planning needs and objectives.** A common use of life insurance, the death benefit can be used to pay any federal or state death taxes that may be due, or simply to provide additional funding for your heirs to augment other assets you might have.

What types of life insurance are there?

There are a number of different types of life insurance policies offering different coverages for various financial planning needs. Here are a few to consider:

Term insurance

Term insurance guarantees the payment of a specified death benefit over a specified period of time. It's often called pure insurance, as there is no cash value or investment component—your premium payments go towards purchasing a death benefit only over the term of the policy. It is also generally the least expensive form of life insurance.

Term insurance can be useful for younger people who want to purchase the largest death benefit they can, perhaps to protect young children and their spouse in the event of their premature death. It can also be useful for those needing a death benefit for a specific period of time

Typical term durations include 10, 20 and 30 years. With term insurance, the policy will lapse unless you continue to pay the premiums. At the end of the term period, you can keep the policy in force if you wish, the premiums will generally increase to a level that makes this impractical. Some term policies offer the ability to convert to a permanent policy with no medical exam, which can be valuable if your health status has changed and you still have a need for the insurance coverage. The premium will typically be based upon your age at that time.

Whole life insurance

Whole life insurance provides a lifetime death benefit for the insured, also known as permanent, or, traditional life insurance. Whole life policies also provide a cash value that can be tapped if needed, via a policy loan. The value of any loans outstanding will reduce the policy's death benefit. Whole life policies also offer dividends in many cases that can be used to add to the policy's cash value or to pay some or all of the ongoing premiums.

Premiums can be paid monthly, quarterly, annually or as a one-time single payment—this will vary by insurance company and policy.

Whole life insurance fills a need for those who need coverage over their lifetime, for estate planning or other needs. Whole life can be used in conjunction with term or other types of policies to tailor your life insurance coverage to your needs over time. Once you are approved for the policy, you can't be denied coverage due to changes in your health situation as long as the premiums are paid.

Variable life insurance

Variable life insurance is another type of permanent life insurance policy that offers an investment component and flexible premiums. The investment component is via sub-accounts, which are similar to mutual funds and offer a variety of investment choices. These sub-accounts allow for potential growth in the policy's cash value via investment returns.

The death benefit can increase over time based upon the performance of the investment account. Policies vary and some offer a choice of death benefits including a level death benefit and a face plus cash value death benefit. The latter costs more, but your beneficiaries will receive the cash value of the policy in addition to the death benefit.

Premiums are generally not fixed on these policies and policyholders can adjust their premium payments to meet their financial needs and situation over time. The accumulated cash value can help offset a lower premium payment, and the cash value is a form of tax-deferred savings.

Universal life insurance (UL)

This is a form of permanent life insurance that offers flexible premiums and savings component that earns interest. Some policies do require either a fixed monthly payment or a one-time single premium payment. Universal life is generally less expensive than a traditional whole life policy.

The cost of insurance is the minimum premium to keep the policy in force. Over time as the cost of insurance increases to the policy holder's age and is based on the several components that comprise the total cost of insurance for the policy.

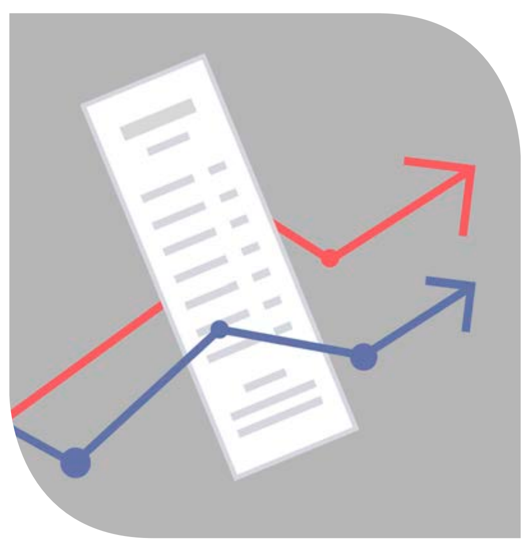
The cash value portion of the policy earns either a market rate of interest or a different rate offered by the insurer. This pool of money can be accessed during the insured's lifetime via a loan. The cash value can also be used to reduce the required premium payments over time while still maintaining the death benefit. You can also use the cash value to increase the death benefit over time if needed as well.

Variable universal life (VUL)

VUL insurance combines the low and flexible premiums offered by universal life policies and the investment features of a variable life policy. The sub-accounts in the investment portion of the policy allow you to significantly grow the policy's cash value but can also cause declines in the cash value of your returns are negative.

VUL policies offer flexible maximum and minimum premium payments and a guaranteed minimum death benefit.

There are other types of insurance policies out there, including variations of the ones already mentioned. It's important to select the type of insurance that best fits into your overall financial planning needs and to keep in mind that you can combine more than one type of policy to meet your needs as appropriate.



Group insurance coverage vs. private policies

You may already have access to group life insurance coverage via your employee benefit plan at work. This might be a good solution in some cases, but there are several factors to consider when deciding on group insurance coverage versus buying life insurance privately. That said, you can certainly use both types of life insurance together. Some factors to be considered include:

- **Cost.** Generally, group coverage will be less expensive than buying a similar coverage privately. Some employers offer free coverage, often up to some percentage of your salary.
- **Limits of coverage.** The amount of death benefit might be limited and not enough to cover the amount you need.
- **Can the group coverage be continued once you leave the company—and at what cost?** Many group policies offer this feature, but be sure to check into this prior to purchasing group coverage and prior to leaving the employer.
- **Ability to pass a medical exam.** This requirement generally does not exist, at least for the basic level of group coverage offered, if not for all levels of coverage. For those with medical conditions that may increase their cost of coverage or prohibit them from obtaining private coverage, a group policy can be an effective way to meet some or all of their life insurance needs.

If your needs are beyond the basic level, group life insurance probably won't meet your needs, at least not entirely. That said, there is no reason not to utilize group coverage to meet a portion of your life insurance needs in combination with your outside life insurance policies.

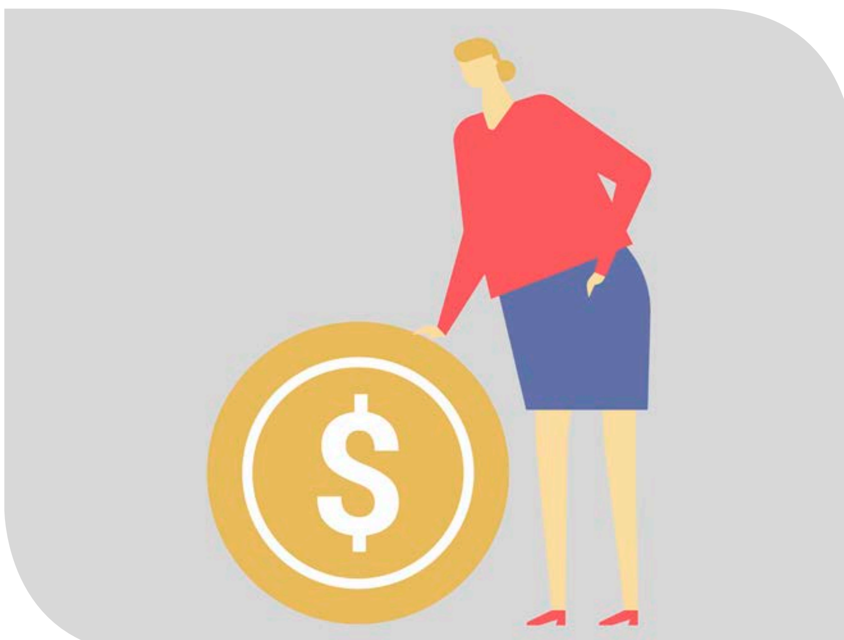
Life insurance as part of your overall financial plan

Life insurance should only be purchased as needed to meet your financial planning objectives. In addition to the death benefit needed, attention should be given to the type of policy that best meets your needs. Some things to consider include:

What role does the death benefit play in your financial plan? This can vary widely—in some cases, the policy will cover the financial void left by the death of the insured, which could be the case if you have young children. The death benefit can also help fund retirement for the surviving spouse or college for the children. At the very least it can provide a bridge to allow the surviving spouse time to get back on his or her feet financially. The death benefit might also be used to fund a variety of estate planning objectives.

How long will you need the insurance for? If the need is temporary, a term policy might suffice—if the need is permanent, then it's best to consider some form of permanent insurance. Often term policies are purchased without giving enough thought to the need for insurance beyond the term period. People are living longer, and life insurance can be used to offset any shortfall in assets for a surviving spouse. Divorce and blended families are becoming more common, which is where the death benefit can be used to solve often complex inheritance issues.

Cash value policies can be another leg in your retirement planning efforts. Especially for those who have maxed out their contributions to traditional retirement savings vehicles like their 401(k) and an IRA, some life insurance policies offer attractive investment options and tax-deferred growth while invested within the policy.



A bridge to retirement. If a married couple is nearing retirement but hasn't saved quite enough, the death of one spouse can be financially devastating for the surviving spouse in a couple of ways. First, the lost income and retirement plan contributions during these key years leading up to retirement. Second is the lost income and retirement plan contributions of the deceased spouse in these key years leading up to retirement. The death benefit can help cover any retirement shortfall or could go towards paying down the mortgage on the couple's home eliminating that ongoing expense for the surviving spouse.

Business liquidity can be an issue funded by a life insurance policy. We mentioned buy-sell arrangements previously and life insurance can certainly fund these pre-arranged transfers in the event one of the business owners dies prematurely.

Beyond this scenario, there are instances where a business owner has done any sort of succession planning and then pass away. In many cases, this can cause their heirs to sell the business at less than full value, or to have to come up with an alternative plan to run the company. This may lead to losses in sales and profitability for the business. A life insurance policy on the owner can provide money for their family and heirs to offset the devastating impact the owner's death might have on the business.

Estate taxes. Life insurance can provide the cash your heirs need to pay estate taxes due on the transfer of personal or business assets. Even with the higher estate tax thresholds currently in place, these taxes can be devastating on larger estates.

Life insurance can be an important financial planning tool for people at all stages of life and in various types of situations. The death benefit can provide a much-needed infusion of cash, and many policies offer other benefits as well.

Your financial planning professional can help you review your situation to determine if your current policy or policies are sufficient for your needs and if more or different coverage is needed. Just like your investment portfolio and your tax planning efforts, don't neglect your life insurance needs when doing financial planning.