

Life Insurance Buyer's Guide

Illinois

This guide can show you how to save money when you shop for life insurance. It helps you to:

- Decide how much life insurance you should buy,
- Decide what kind of life insurance policy you need, and
- Compare the cost of similar life insurance policies.

This guide has been prepared by the Illinois Department of Insurance, in part using material developed by the National Association of Insurance Commissioners.

The National Association of Insurance Commissioners is an association of state insurance regulatory officials. This association helps the various State Insurance Departments to coordinate insurance laws for the benefit of all consumers. You are urged to use this Guide in making a life insurance purchase.

This guide does not endorse any company or policy.

Buying Life Insurance

When you buy life insurance, you want a policy that fits your needs without costing too much. Your first step is to decide how much you need, how much you can afford to pay and the kind of policy you want. Then, find out what various companies charge for that kind of policy. You can find important differences in the cost of life insurance by using the life insurance cost indexes, which are described in this guide. A good life insurance agent or company will be able and willing to help you with each of these shopping steps.

If you are going to make a good choice when you buy life insurance, you need to understand which kinds are available. If one kind does not seem to fit your needs, ask about the other kinds, which are described in this guide. If you feel that you need more information than is given here, you may want to check with a life insurance agent or company or books on life insurance in your public library.

Life insurance can be bought either on an individual basis or on a group basis. Group insurance may be inexpensive when compared to individual insurance. It is important to remember that insurance purchased on this basis is usually term insurance, and hence will not develop cash values, and is dependent on your continued membership in the group or employment. Also the amount of insurance that is available for purchase is usually limited.

Choosing the Amount

One way to decide how much life insurance you need is to figure how much cash and income your dependants would need if you were to die. Life insurance can provide cash for last expenses and income for your family's future living expenses. Your insurance should come as close as you can afford to making up the difference between (1.) What your dependents would have if you were to die now and (2.) What they would actually need at some time in the future when needs change.

Choosing the Right Kind

All life insurance policies agree to pay an amount of money if you die. But all policies are not the same. There are three basic kinds of life insurance.

- Term Insurance
- Whole Life Insurance
- Endowment Insurance

The kind of life insurance you purchase is dependent on the need you are trying to satisfy. Some needs are temporary, i.e. do not exist throughout your life, while other needs are permanent. As an example, the need to finance your children's education is a temporary need. The need to meet mortgage payments is also a temporary need; since it exists only while the mortgage exists. On the other hand, the financial needs of your family after your death are permanent. Remember, no matter how fancy the policy title or sales presentation might appear, all life insurance policies contain one or more of the three basic kinds of coverage. If you are confused about a policy that sounds complicated, ask the agent or company if it combines more than one kind of insurance. The following is a brief description of the three basic kinds.

Term Insurance is death protection for a "term" of one or more years. Death benefits will be paid only if you die within that term of years. Term Insurance generally provides the largest immediate death protection for your premium dollar. Some term insurance policies are "renewable" for one or more additional terms, even if your health has changed. Each time you renew the policy for a new term, premiums will be higher. You should check the premiums at older ages and the length of time the policy can be continued. Some term insurance policies are also "convertible". This means that before the end of the conversion period, you may trade the term policy for a whole life or endowment insurance policy even if you are not in good health. Premiums for the new policy will be higher than you have been paying for the term Insurance.

Whole Life Insurance gives death protection for as long as you live. The most common type is called "straight life" or "ordinary life" Insurance, for which you pay the same premiums for as long as you live. These premiums can be several times higher than you would pay initially for the same amount of term insurance. But they are smaller than the premiums you would eventually pay if you were to keep renewing a term insurance policy until your later years. Some whole life policies let you pay premiums

for a shorter period, such as 20 years, until age 65. Premiums for these policies are higher than for ordinary life insurance since the premium payments are squeezed into a shorter period. Although you pay higher premiums to begin with for whole life insurance than for term insurance, whole life insurance policies develop “cash values” which you may have if you stop paying premiums. You can generally either take the cash, or use it to buy some continuing insurance protection. Technically speaking, these values are called “non-forfeiture benefits”. This refers to benefits you do not lose (or “forfeit”) when you stop paying premiums. The amount of these benefits depends on the kind of policy you have, its size, and how long you have owned it. A policy with cash value may also be used as collateral for a loan. If you borrow from the life insurance company, the rate of interest is shown in your policy. Any money that you owe on a policy loan would be deducted from the benefits if you were to die or from the cash value if you were to stop paying premiums.

Endowment Insurance pays a sum or income to you – the policyholder – if you live to certain age. If you were to die before then, the death benefit would be paid to your beneficiary. Premiums and cash values for Endowment Insurance are higher than for the same amount of Whole Life insurance. Thus Endowment Insurance gives you the least amount of death protection for your premium dollar.

Finding A Low Cost Policy

After you have decided which kind of life insurance fits your needs, look for a good buy. **Your chances of finding a good buy are better if you use two types of index numbers that have been developed to aid in shopping for life insurance.** One is called the “surrender cost index” and the other is the “net payment cost index.” It will be worth your time to try to understand how these indexes are used, but in any event, use them **only** for comparing the relative costs of similar policies. **Look for policies with low cost index numbers.**

What Is Cost?

“Cost “is the difference between what you pay and what you get back. If you pay a premium for life insurance and get nothing back, your cost for the death protection is the premium. If you pay a premium and get something back later on, such as cash value, your cost is smaller than the premium. The cost of some policies can also be reduced by dividends; these are called “participating” policies. Companies may tell you what their current dividends are, but the size of future dividends are unknown today and cannot be guaranteed. Dividends actually paid are set each year by the company. Some policies do not pay dividends. These are called “guaranteed cost” or “non-participating” policies. Every feature of a guaranteed cost policy is fixed so that you know in advance what your future cost will be. The premiums and cash values of participating policies are guaranteed, but the dividends are not. Premiums for participating policies are typically higher than for guaranteed cost policies, but the cost to you may be higher or lower, depending on the dividends actually paid.

What Are Cost Indexes?

In order to compare the cost of policies, you need to look at:

- Premiums
- Cash Values
- Dividends

Cost indexes use one or more of these factors to give you a convenient way to compare relative costs of similar policies. When you compare costs, an adjustment must be made to take into account that money is paid and received at different times. It is not enough to just add up the premiums you will pay and to subtract the cash values and dividends you expect to get back. These indexes take care of the arithmetic for you. Instead of having to add, subtract, multiply and divide many numbers yourself, you just compare the index numbers that you can get from life insurance agents and companies.

Life Insurance Surrender Cost Index: This index is useful if you consider the level of the cash values to be of primary importance to you. It helps you compare costs if at some future point in time, such as 10 or 20 years, you were to surrender the policy and take its cash value.

Life Insurance Net Payment Cost Index: This index is useful if your main concern is the benefits that are to be paid at your death and if the level of cash values is of secondary importance to you. It helps you compare costs at some future point in time, such as 10 or 20 years, if you continue paying premiums on your policy and do not take its cash value.

There is another number called the **Equivalent Level Annual Dividend**. It shows the part dividends play in determining the cost index of a participating policy. Adding a policy's equivalent level annual dividend to its cost index allows you to compare total cost of similar policies before deducting dividends. However, if you make any cost comparisons of a participating policy with a non-participating policy, remember that the total cost of the participating policy will be reduced by dividends, but the cost of the non-participating policy will not change.

How Do I Use Indexes?

The most important thing to remember when using cost indexes is that a policy with a small index number is generally a better buy than a comparable policy with a larger index number. The following rules are also important:

- Cost comparisons should only be made between similar plans of insurance. Similar plans are those that provide essentially the same basic benefits and require premium payments for

approximately the same period of time. The closer policies are to being identical, the more reliable the cost comparison will be.

- Compare index numbers only for the kind of policy, for your age and for the amount you intend to buy. Since no one company offers the lowest cost for all types of insurance at all ages and for all amounts of insurance, it is important that you get the indexes for the actual policy, age, and amount that you intend to buy. Just because a “Shoppers Guide” tells you that one company’s policy is a good buy for a particular age and amount, you should not assume that all of the company’s policies are equally good buys.
- Small differences in index numbers could be offset by other policy features, or differences in the quality of service you may expect from the company or its agent. Therefore when you find small differences in cost indexes, your choice should be based on something other than cost.
- In any event, you will need information on which to base your purchase decision. **Be sure you can afford the premiums and that you understand its cash values, dividends and death benefits.** You should also make a judgment on how well the life insurance company or agent will provide service in the future, to you as a policyholder.
- These life insurance cost indexes apply to new policies and should not be used to determine whether you should drop a policy you have already owned for awhile, in favor of a new one. If such a replacement is suggested, you should ask for information from the company that issued the old policy before you take action.
- An important fact to note is the difference in premium payments paid during one year’s time based on an annual premium versus the annualized periodic premium. For example, if you choose to pay premiums on a monthly basis, the annualized periodic premium would be 12 times the monthly premium. There may be a significant difference between the annualized periodic premium and the annual premium, and it should be considered when deciding on a payment schedule.

Important Things to Remember-A Summary

The first decision you must make when buying a life insurance policy is choosing a policy whose benefits and premiums most closely meet your needs and ability to pay. Next, find a policy that is also a relatively good buy. If you compare the surrender cost index and the net payment cost index of similar competing policies, your chances of finding a relatively good buy will be better than if you do not shop. **Remember, look for policies with lower cost index numbers.** A good life insurance agent can help you to choose the amount of life insurance and the kind of policy you want and will give you cost indexes so that you can make a cost comparison of similar policies. **Don’t buy life insurance unless you intend to stick with it.** A policy that is a good buy when held for 20 years can be very costly if you cancel during the early years of the policy. If you surrender such a policy during the first few years, you may get little or nothing back and much of your premium may have been used for company expense. Read your new policy carefully and ask the agent or company for an explanation of anything you do not understand. Whatever you decide now, it is important to review your life insurance program every few years to keep up with changes in your income and responsibilities.