

# §7-1

Life Insurance: Who Needs it?

## Goals:

- ▶ Understand what life insurance is
- ▶ Decide who needs it
- ▶ Determine how much a family should buy
- ▶ Examine the kinds of life insurance that are available
- ▶ Calculate the cost of various amounts of life insurance

# Where to you get it??



# LIFE INSURANCE

- ▶ A contract to pay a specified amount of money to a beneficiary upon the death of the policy owner.
- ▶ Basically used to replace the lost income of the policy owner.
- ▶ Beneficiary- is a person or people named in the policy as the recipient of the money upon the death of the owner.
  - ▶ EX. (Spouse, child, nephew, charity, pet, etc.)

# HOW DOES IT WORK?

- ▶ Policy owners pay premiums into a pool of money with many other people.
- ▶ When a policy owner dies, money is taken from the pool of money to pay out the “death benefit” or “survivors benefit”.
- ▶ Premium-the amount of money paid on a regular basis for an insurance policy
- ▶ Premiums are based on many factors, such as age, physical fitness, lifestyle choices, marital status, dependents, etc.

# Who needs life insurance?

- ▶ Any member of a family that provides a significant portion of the income.
- ▶ Life insurance is purchased to protect the dependents of the policy owner.
- ▶ Life insurance does not usually need to be purchased for a high school or college age student who does not have children or provide for their family.

## How Much is Needed?

- ▶ Goal is to be able to maintain the current standard of living.
- ▶ A minimum of 60% of the deceased's gross income for the remaining years that they would have worked.
- ▶ 75% is usually manageable.
- ▶ 100% would be ideal, but is sometimes carries unaffordable premiums.

# Types of Life Insurance

- ▶ Term insurance
- ▶ Cash-Value insurance (permanent)
  - ▶ Within both of these main types of life insurance there are different types of policies

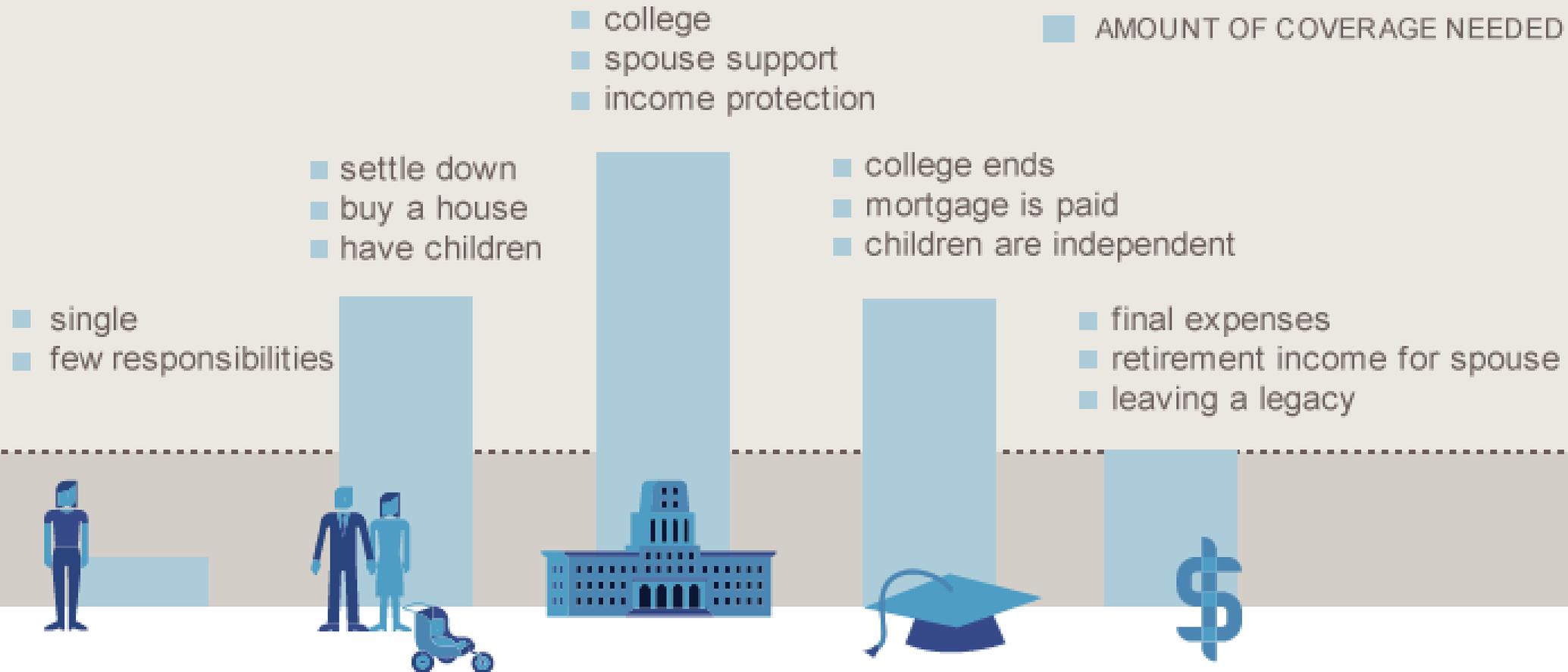
# Term Life

- ▶ Provides temporary coverage, they will be paid the benefit during a fixed period of time or “term”
- ▶ The term is usually 5 or 10 years
- ▶ If the insured person does not die during the term, the policy can be renewed or it will expire.
- ▶ If the insured person dies during the term, the beneficiary receives the face value of the policy.
- ▶ This is the most flexible and least expensive option.

# Types of term insurance

- ▶ **Group life insurance**-is purchased thru an employer and provides term insurance for a large number of people under a single policy without the need for a medical exam.
- ▶ **Renewable convertible term insurance**-can be renewed without a medial exam and can be changed into a different form of insurance
- ▶ **Decreasing term insurance**-the benefit decreased over time as the dependents grow up and the mortgage payment decreases, which reduced the survivors' expense and thus need for a higher death benefit.

# How life insurance needs can change over time...



# Cash Value Insurance

- ▶ Not only are you purchasing protection , but you are also saving money at the same time.
- ▶ As premiums are paid, the policy will build cash value much like a savings account

# Types of cash-value insurance

- ▶ **Whole life** - (aka, straight life or ordinary life) -you pay premiums your entire life. Part is invested, building up the cash value of the policy. You can cash in the policy. You can borrow part of the cash value.
- ▶ **Limited Payment life-** has a fixed number of premium payments, usually 20 years. Has higher premiums but the policy is paid up to its cash value in fewer years than whole life
- ▶ **Endowment Policy-** emphasis on cash build up, but has extremely high premiums
- ▶ **Universal life-** similar to whole life, two types that differ in the death benefit. Type A-benefit remains constant. Type B-benefit varies with the cash value.

# Replacement Life Insurance Formula

- ▶  $R = mS$
- ▶ R = required replacement insurance
- ▶ m = multiple from table
- ▶ S = original salary or wage

## Skill 1

- ▶ Cartman's father, Jack, was earning \$65,000 per year when he was 45 years old. How much life insurance should he have bought to replace 60% of his regular gross income?



# Multiple of Salary Chart

Current Gross Earnings	Current Age							
	25 Years		35 Years		45 Years		55 Years	
	75%	60%	75%	60%	75%	60%	75%	60%
\$ 7,500	4.0	3.0	5.5	4.0	7.5	5.5	6.5	4.5
9,000	4.0	3.0	5.5	4.0	7.5	5.5	6.5	4.5
15,000	4.5	3.0	6.5	4.5	8.0	6.0	7.0	5.5
23,500	6.5	4.5	8.0	5.5	8.5	6.5	7.5	5.5
30,000	7.5	5.0	8.0	6.0	8.5	6.5	7.0	5.5
40,000	7.5	5.0	8.0	6.0	8.0	6.0	7.0	5.5
65,000	7.5	5.5	7.5	6.0	7.5	6.0	6.5	5.0

## Solution

- ▶  $R = mS$
- ▶  $R = 6.0 * 65,000$
- ▶  $R = \$390,000$
- ▶ Cartman's father, Jack Tenorman, should buy \$390,000 worth of life insurance to replace 60% of his gross income when he dies.

## Skill 2

- ▶ Kenny's mother, Carol, is 35 years old and is comparing the premiums for different types of life insurance.
- ▶ How much would a \$500,000 policy cost for each main type offered by this company?

**COMPARISON TABLE FOR TERM AND WHOLE LIFE PREMIUMS**

Policy Face Value is \$100,000

Age	Five-Year Renewable Term	Whole Life	First-Year Difference
20	\$205	\$ 775	\$ 570
25	207	918	711
30	218	1112	894
35	254	1374	1120
40	363	1729	1366
45	562	2127	1565
50	878	2689	1811



# Solution

- ▶ Since the table is for \$100,000 worth of life insurance annually, multiple the premiums by 5
- ▶ 5-Yr Term---\$254 x 5 =
- ▶ Whole Life---\$1374 x 5 =
- ▶ The annual premium for a 5-yr \$500,000 Term insurance policy at age 35 is \$1270
- ▶ The annual premium for \$500,000 whole life insurance policy at age 35 is \$6870

# Homework

- ▶ Ask Yourself P.324 #1-6
- ▶ Try Your Skills P. 327 #1-9

