GUIDE TO UNDERSTANDING LIFE INSURANCE

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LIGHTBULB PRESS®

Insuring the Future

A complete financial plan includes insuring your life.

When you think of financial planning, you probably think about saving for goals like retirement, buying a house, paying for education, and otherwise achieving the future you want for your loved ones. There is another possibility to consider in your financial plan, however: What happens if you're no longer around to provide the income necessary to meet these goals?

If your family depends on your financial contributions for their security, without you there to support them, their goals might be at risk. For example, if you have young children, you may be saving for their college educations. Without you, they might have a hard time meeting that goal. Your spouse may depend on your income to help pay the mortgage and meet everyday living expenses. You may have other family members or loved ones, such as elderly parents or an unmarried partner, who would be forced into a lower standard of living without you.

Life insurance is a way you can provide for the people you care about so that they can still have the lives you want them to have, even if you can't be there.

WHAT LIFE INSURANCE DOES

Life insurance can cover final expenses, or costs associated with your death—for example, funeral and burial arrangements, any potential legal expenses involved in settling your estate, and your debts. But life insurance can do much more. You can use life insurance to replace the income you would have provided if you'd lived as long as expected. That would mean the people who depend on you are protected from the financial hardship that could come from losing you. They can use that income replacement to pay for their living expenses, maintain their standard of living, and save for their goals.

Life insurance can also help you while you're alive. For example, some policies have an **account value**, which you may borrow against—though you'll probably be charged interest, and the death benefit will be reduced by the loan amount plus the interest. If you own your own business, life insurance can secure your company's finances, and you can offer it as a benefit to attract employees.

As part of an estate plan, life insurance can also play a big role. Some people use life insurance benefits to equalize an inheritance—for example, leaving a valuable asset to one child and a life insurance benefit of equal value to another. Your heirs can use life insurance to pay estate taxes that might be due when you die rather than having to sell off assets.

Not everyone needs to address all of these risks with life insurance, though. The amount of life insurance you actually need depends on your particular goals, life situation, and finances. For example, you'll need more life insurance if you're supporting young children than you would if your children were already old enough to support themselves. So as you get older and your situation changes, you'll want to review your life insurance periodically, to make sure your financial plans keep step with your life.

NOT THE BREADWINNER?

Don't make the mistake of thinking that simply because you're not the family breadwinner you don't need to worry about life insurance. You may do valuable work for your family that would be difficult and costly to replace if you weren't there. For instance, you might be responsible for the housekeeping, the childcare, the maintenance of the house, or other necessary jobs.

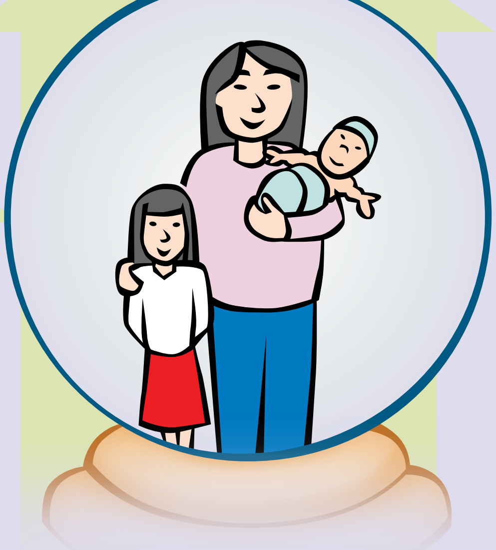
Hiring professionals to do the same work is likely to be expensive. The value of what you do varies, but it could cost a family $70,000 or more a year to replace the services that a homemaker provides. So it might make sense for you and your family to consider insuring your life if you're a stay-at-home mom or dad, since the contribution you make has more than sentimental value for your family.

YOUR LIFE, YOUR INSURANCE

As your life goes through different stages, your life insurance needs will change. Everyone's experience is different, but here are some of the key concerns you might face.

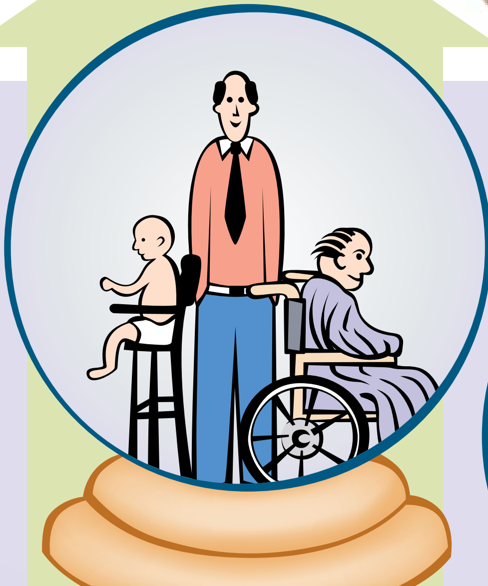
Young couple, new homeowners

Buying a home together is exciting. But it's also a major financial commitment that may depend on two incomes. If one of you were to die unexpectedly, you want to be sure that the surviving spouse is able to keep the home you love. If both of you have life insurance, you're protecting each other and your investment.



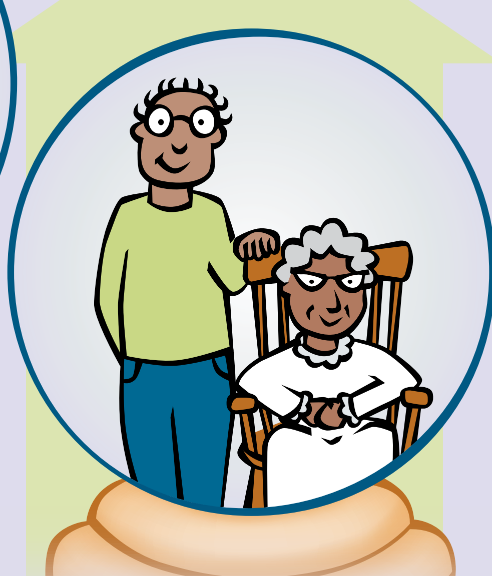
Young working parent

Since your kids depend on you to support them, if you were to die, their financial security might be at risk. Even if your spouse or relatives will be there to raise your children, they may not have the financial resources to provide the things for your children that you wanted them to have. Life insurance can help you make sure that whoever raises your children after you're gone can maintain the standard of living you want for them.



Supporting kids and parents

These days, more and more people find themselves raising children while at the same time supporting their parents in their old age. There's even a name for it: the sandwich generation. It's because you find yourself squeezed between two equally pressing obligations. The more people you have dependent on you, the more life insurance you probably need.



When the kids are grown

Without kids to support, your life insurance needs will probably be considerably smaller than they were before. You might still have older parents to think of, or you may need life insurance to support a surviving spouse or as an estate planning tool. And if you've got a policy with a cash value attached, you might be able to use that to help reach your retirement goals.

LIFE INSURANCE

Qualifying for Insurance

What kind of life insurance risk are you?

Buying life insurance isn't simply a question of pointing to the policy you want and writing a check. First the company has to decide whether it makes business sense to insure you, and what the price will be. Specifically, the company wants to know your **mortality risk**—or the odds that it will have to pay the death benefit on your policy sooner than it would normally expect. The process of assessing this risk can be complicated, but it boils down to this: Good health and low-risk employment and hobbies mean you qualify for higher amounts of coverage and lower premiums.

THE NUMBER CRUNCHERS

The point of life insurance is to protect loved ones from financial hardship when you die. Of course, everyone dies. The question that matters to insurers is, when? Being able to afford to provide coverage is based on a company's ability to calculate the answer—not for you individually, since that can't be done, but for groups of people of the same age and gender with similar medical histories and lifestyles. This process of classifying the risk you pose is called **underwriting**.

The statistical experts who crunch these numbers are called **actuaries**. They gather information on large numbers of people and divide them into groups with similar risks. Then, they calculate how many from each group can be expected to die from one year to the next. This information is charted in **mortality tables**, which insurers use to calculate how much money they'll need to pay **claims** each year.

Your premium rates are based on where you fit in the mortality tables. A long life expectancy translates to lower rates.

OTHER PATHS TO COVERAGE

There are alternatives for purchasing insurance even if you have health problems. In some cases, the insurer charges more. For example, with a **table rating** you pay a percentage increase above the company's standard rate for a comparable policy. For example, a table 1 offer might increase your premium by 25%.

You should also check whether you can get group insurance through an employer or other association to which you belong. Group policies often cover all eligible participants up to a certain limit before requiring underwriting. And if your spouse or partner is eligible for group insurance, you may be able to get coverage through that policy.

Or, if you have an existing policy, you may be able to increase coverage without underwriting. But always be honest. Lying on your life insurance application is called misrepresentation, and if the company finds out, it can refuse to pay the death benefit.

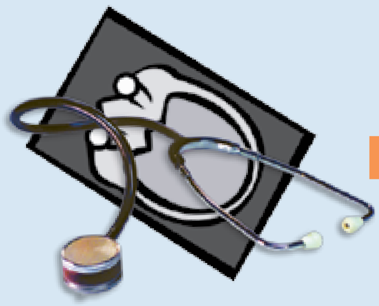
RISK CATEGORIES

Life insurance companies use four basic risk categories, although many companies divide these further into subcategories for more accurate pricing:

- + **Preferred risk** applicants have the longest life expectancy and pay the lowest rates.
- **Standard risk** applicants have an average life expectancy and pay standard rates.
- – **Substandard risk** applicants have a lower life expectancy and pay the highest rates.
- **Declined** or **uninsurable** applicants pose more risk than the company is willing to insure.

HIGH-RISK WARNINGS

Every company sets its own underwriting standards, but most of them pay close attention to:



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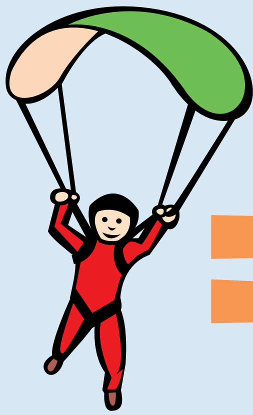

= MORTALITY RISK

Your current health: You may have to undergo a physical exam to confirm basic details about your health. Certain health conditions—such as heart disease, cancer, diabetes, and AIDS—may trigger higher rates, or mean your application is turned down. Smokers or others tobacco users pay more than people in otherwise similar health who don't smoke or use tobacco.

Your health history: The insurer can request past health records. You may be in a high-risk category if there is a history of certain diseases in your family, such as Huntington's disease, heart disease, stroke, or sickle cell anemia.

Occupation and hobbies: Some jobs are considered high risk and may make it more difficult to buy insurance. Certain hobbies, such as flying your own plane, car racing, and skydiving, are considered high risk and may increase your premiums or make it difficult to find coverage.

IF YOU LIVE TO BE 100

Companies used to price premiums for permanent policies so that, if you lived to be 100, your cash value would equal your death benefit. At that point, the company would write you a check for the cash value and your coverage would end. These days, living to 100 isn't the rarity it used to be, so many policies let policyholders keep their insurance in force as long as they live.

IN THE GENES

Medical research regularly uncovers more information about the impact of your genetic make-up on your vulnerability to certain diseases. This can be an enormous advantage, both for prevention and early treatment. But many people worry that details of their DNA could be used to deny them insurance.

Here's the good news. Most states prohibit or restrict insurance companies from denying coverage because of genetic risks—though in some states insurers can use the information to assess your application. In addition, some insurance companies, as a matter of policy, refuse to use this information.* If you're concerned about this issue, check your home state's laws and the genetic testing policies of any insurer you're considering.

* State Farm does not use genetic testing.