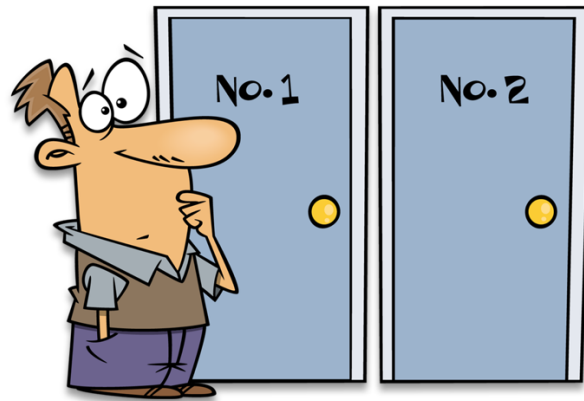


What Type of Life Insurance Should I Buy?

By: Exchange Capital Management

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The purpose of life insurance is to secure the financial well-being of your loved ones in the case of your unexpected passing. Although life insurance may not be necessary for everyone, certain groups could benefit from having a policy in place. If you've decided you need coverage, your next step is selecting a policy that suits your needs.

Types of Life Insurance

Term Life Insurance

Term life insurance provides financial protection for a specified period, typically ranging from 5 to 30 years. This policy has fixed premiums and no guaranteed payout date, making it more affordable than other types of life insurance. Since the premium is influenced by the applicant's health status, it's wise to purchase when you're young and healthy. If you pass away during the policy's term, your beneficiaries will receive a death benefit.

Term life insurance ensures your family can maintain their lifestyle upon your death by covering significant expenses like mortgage payments, your child's education, and even replacing the day-to-day support you provided. For example, if you were the primary caregiver – the death benefit can help your spouse afford daycare. In other words, it provides financial resources to support them after your passing, offering some relief during challenging times. Once the term ends, the contract expires, and you are no longer insured.

Permanent Life Insurance

Permanent life insurance provides coverage for your entire life and offers both a death benefit and a savings component. When you pay your premium, a portion goes towards the cost of the policy, and some is also put into a cash value account that earns interest and grows tax deferred. If you need to access the cash value in the account, you can make a withdrawal or take a loan against the policy. Be wary of making withdrawals as it may reduce your death benefit or increase your premiums.

While many tout the benefits of the cash value in permanent life insurance, this money will likely not be included in the death benefit and will be forfeited to the insurance company upon your death.

These policies offer you coverage for your entire life, ensuring your loved ones will receive a payout from the insurance company when you pass away. Because of the guaranteed payout date and the cash value component that requires administrative and investment management, these policies tend to be more expensive than others.

We rarely recommend these contracts, but there is an exception: if you have a dependent with a disability. In these cases, the policy guarantees your loved one has the necessary financial resources for their continued care when you are no longer around to support them.

If you need permanent life insurance, there are three primary types to choose from:

Whole Life Insurance: Most policies have a fixed premium and death benefit. The cash value component in the account will offer a guaranteed rate of return, usually around 1 – 3.5%.

Universal Life Insurance: The cash value in this account earns interest at a rate set by the insurer. The main difference in universal life insurance is its flexibility, allowing the policyholder to adjust the death benefit and premium as needed. If you need less coverage over time, then the insurance can be tailored accordingly.

Variable Life Insurance: The rate of return is tied to underlying investments in the form of mutual funds. It gives you the potential for higher returns but also carries the risk of investment losses. The premiums stay consistent, and the death benefit is guaranteed regardless of market performance. These policies are often more expensive due to fees associated with the investments.

In almost all cases, we don't recommend these policies. It's best not to mix insurance and investments in one policy because they serve different purposes. While insurance is meant to provide coverage and financial protection, investments aim to generate returns. When you combine investing with an insurance policy, the investment options are often limited and costly – potentially reducing your overall investment return.

The Bottom Line

At its core, life insurance is meant to cover the loss of your income and support for your loved ones in the event of your death. While there are numerous policy options available, most of them won't be the right fit for your situation. For many individuals, a simple term life insurance policy will do the trick.