

STAYING ON TRACK FOR THE PRICE OF AN ANNUAL PREMIUM

"It takes tremendous self-confidence to spend money so sensibly," wrote the Philadelphia Inquirer's Architecture Critic Inga Saffron, when reviewing Philadelphia's art palace - the Perelman Building. Rather than using funds to simply 'out-glamour' other museums, two-thirds of the Perelman is devoted to study rooms, conservation labs, workshops, climate-controlled storage, offices, and a library. It contains just five public galleries. "Modesty and restraint" were used to describe its unique character.

It is serendipitous that some of the language chosen to characterize this building - originally built for a life insurance company - can be borrowed to help illuminate the 'whys?' and 'what fors?' of consumers' decision-making in the realm of *purchasing* life insurance to protect loved ones. Let's start in the building's library and determine what types of life insurance one is likely to encounter.

The two broad categories of life insurance are *term and permanent*. Fortunately the names are descriptive. Unfortunately, the infinite naming mutations created by marketers to sell product can be less straightforward. Generally speaking, one can purchase *term* insurance for fewer premium dollars annually. It lasts for a specific period of time and does not build up cash value. Permanent insurance, on the other hand is designed to last for your lifetime and usually builds cash value (slowly over decades.) This 'cash' may be withdrawn - now lowering your promised face amount of death benefit, or loaned to yourself from time to time.

Let's head from the library to a study room and tackle 'why' a consumer might purchase life insurance. Life insurance was created to offer protection from financial catastrophe due to the premature death of a wage earner. Consumers might need to protect their children, their husband, wife, or significant other, or today - a dependent elderly parent. Surviving loved ones could need to replace income, to pay off the mortgage, to continue saving for retirement, or to fund kids' college expenses or the needs of elderly parents. The old idea, "Gee, we have \$100,000 of life insurance; that should be enough," probably doesn't take into account 21st-century costs. More sophisticated legacy planning concerns - such as wealth preservation or the funding of estate taxes - may also be resolved through the purchase of life insurance.

The workshop is our next stop as we consider how much life insurance may be enough. Readers, as you do your family's calculations, I encourage you to consider investing a potential lump sum insurance benefit - to seek to produce annual income. For most, a conservative investment vehicle is appropriate because immediate distributions are likely to be required. Consider drawing off earnings of no more than 4 - 5%. In plain English, \$4,000 - \$5,000 of income might be used annually from every \$100,000 of benefit invested. That amount of money doesn't go far today, and some will be forfeited to taxes. A million dollars of benefit may be appropriate in 2007. Our 4 - 5% factor translates into potentially \$40,000 - \$50,000 of earnings to supplement the family spending plan.

Adopting the Perelman Building's characteristics of "modesty and restraint" as you choose your life insurance product could save your family money. If your employer

offers group term, determine the maximum face amount for which you are eligible. It may be your least expensive option. However, check to see whether it is transferable (in case you change jobs) and be certain of the age limits on benefits eligibility. When choosing an individual term policy, beware the proclamation 'lasts to age 100.' Keeping coverage in force beyond the initial designated term would probably result in skyrocketing annual premiums. Check the illustration before you buy!

Despite the titling mutations, there are three basic "flavors" of permanent insurance - whole life, universal life, and variable life. The premium cost is higher than term products, but as long as you pay on time, the benefits last a lifetime. Well-written term policies usually contain a conversion privilege - permitting the purchase of permanent insurance later on if one's financial situation is served by it.

Generally speaking, the most familiar flavor of permanent insurance is whole life. Whole life policies have level premiums, and company guaranteed interest rates within the contract. Universal life policies, on the other hand, permit an owner some flexibility with respect to premium payments and death benefits. This flexibility is dependent on the earnings achieved by the insurance company in their underlying holdings. Care should be taken by the owner, for a contract must retain sufficient cash to remain in force.

In a variable life policy, the owner - not the company - takes responsibility for the investment risk of the underlying holdings. In a straight up bull market, this could sound dandy, for the thought of substantially lowered premiums might make the contract seem affordable. Remember, our financial markets go down, not just up. A consumer could be left holding a policy requiring *higher* premium payments, or, steep surrender charges if a decision is made to drop the contract altogether.

I suggest you sidestep the glamour and marketing hype of certain life insurance companies, and seek instead to thoughtfully fulfill your protection needs. Your financial professional may provide guidance. Protecting your family from the chance of catastrophic financial loss offers a perfect opportunity to reflect critic Saffron's beautifully stated thought, "It takes tremendous self-confidence to spend money so sensibly."

E-mail me with your life insurance questions: joslyn@entrustfinancial.com

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