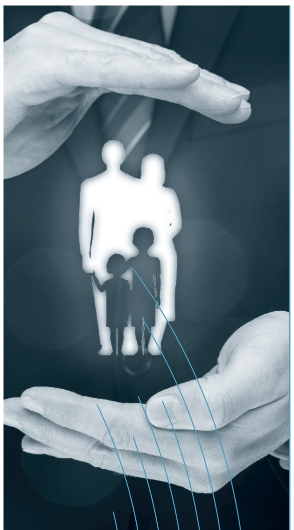
HBKS® Wealth Advisors

Life Insurance 101: The Basics



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MANY FINANCIAL EXPERTS consider life insurance to be the cornerstone of sound financial planning. We at HBKS consider it a part of risk management, one of the pillars of financial planning. The COVID-19 crisis has reminded us that our clients should be reviewing their financial plans with their financial advisors to ensure that life insurance is not only part of their plan, but that there is enough coverage to meet their families' needs.

USES FOR LIFE INSURANCE

Life insurance serves as a useful tool in many situations:

1. Replace income for dependents.
The most fundamental reason to have life insurance is to replace income should the earner die. It is particularly critical for parents with young children to own life insurance. Insurance to replace income can be especially useful when government- or employer-sponsored benefits of the surviving spouse or partner are reduced following the death of their companion.

2. Pay final expenses.
Life insurance can pay funeral and burial costs, probate and other estate administration costs, debts, and medical expenses not covered by health insurance.

3. Create an inheritance for heirs.
Even people with no other assets to pass on can create an inheritance by buying a life insurance policy and naming their heirs as beneficiaries.

4. Pay federal "death" taxes and state "death" taxes.
Life insurance benefits can be used to pay estate taxes so heirs will not have to liquidate other assets or use part of their inheritance. Changes in the federal "death tax" rules between now and January 1, 2021, will likely lessen the impact of this tax on some people, but some states are offsetting those federal decreases with increases in their state estate taxes.

5. Make significant charitable contributions.
By making a charity the beneficiary of a life insurance policy, a donor can make a much larger contribution than the cash equivalent of the policy's premiums.

6. Create a source of savings.
Some types of life insurance create a cash value that, if not paid out as a death benefit, can be borrowed or withdrawn on the owner's request. Since most people make paying their life insurance policy premiums a high priority, buying a cash-value type policy can create a kind of "forced" savings plan. Furthermore, the interest credited is tax deferred — and tax exempt if the money is paid as a death claim.

TYPES OF LIFE INSURANCE

There are two major types of life insurance: term and permanent.

1. Term insurance is the simplest form of life insurance.
The insurance company pays the benefit only if death occurs during the term of the policy, which is usually from one to 30 years. Most term policies have no other benefit provisions.

There are two basic types of term life insurance policies: level term and decreasing term. In a level term policy the death benefit stays the same throughout the duration of the policy. The benefit in a decreasing term policy is systematically reduced, usually year by year, over the course of the policy's term.

2. Permanent life insurance pays a death benefit whenever the policyholder dies.
There are three major types of permanent life insurance: traditional whole life, universal life and variable universal life, and there are variations within each type.

- With traditional whole life, both the death benefit and the premium are designed to stay the same throughout the life of the policy. The "cost" to an insurance company per $1,000 of benefit increases as the insured person ages, and it obviously gets very high when the insured lives to 80 and beyond. The insurance company keeps the premium level by charging a premium that, in the early years, is higher than what is needed to pay their insureds' claims, investing that money, and then using it to supplement the level premium to help pay the cost of life insurance for older people.

  By law, when these "over payments" reach a certain amount, they must be available to the policyholder as a cash value if he or she decides not to continue with the original plan. The cash value is an alternative, not an additional, benefit under the policy. This is also the least flexible permanent life insurance in terms of premium payments.

- Universal life, also known as adjustable life, is more flexible than traditional whole life policies. The savings vehicle, called a "cash value account," generally earns a money-market rate of interest. Once the account has accumulated money, the policyholder has the option of using that money to reduce premiums—providing there is enough money in the account to cover the costs.

- Variable life policies combine death protection with a savings account that can be invested in stocks, bonds and money-market mutual funds. The value of the policy can grow more quickly than other types of policies, but variable life involves more risk. If investments do not perform well, the cash value and death benefit may decrease. Some policies, however, guarantee that the death benefit will not fall below a minimum level. Generally, the premiums are higher for this type of life insurance due to the increased risk of the cash value being invested in stock, bond or money market mutual fund investments.

- Universal variable life combines features of variable and universal life policies. It has the investment risks and rewards characteristic of variable life insurance, as well as the option to adjust premiums and death benefits that is characteristic of universal life insurance.

Life and life's circumstances change, so it is a good policy to review your life insurance on a regular basis. Your HBKS advisor can review your coverage and help you determine the kind and amount of life insurance that best serves your needs now and in the future.

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