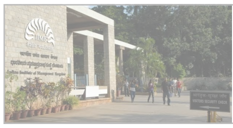

Intro To Insurance: Life Insurance Considerations

By Cathy Pareto

By Cathy Pareto

There are other important considerations that you should know about life insurance before you buy it. (For more insight, read *Life Insurance Clauses Determine Your Coverage*.)

Tax Treatment

The death benefit proceeds of life insurance policies are not taxable to the beneficiaries. They are, however, included as a part of the estate in some cases, depending on how the life insurance policy is owned. This, however, is beyond the scope of this tutorial. Distributions from cash values of whole life policies (loans or withdrawals) may be tax-free or taxable depending on whether they exceed the cost basis (or premiums paid) of the policy. Meanwhile, the earnings or growth of the cash value is tax deferred until a distribution is made. (For related reading, see *Life Insurance Distributions And Benefits*.)

Standard Provisions

A life insurance policy and your application for the coverage constitute a binding contract between the applicant and the insurer. It is understood that the information provided by the applicant is warranted to be true and that no misrepresentations have been made to attain coverage. The incontestable clause protects the insurance company if at a later date, as benefits are paid, it is revealed that the insured lied about his or her health or risk exposures. Once a policy is in force for at least two years, the validity of that contract cannot be questioned under the incontestable clause, unless in the case of fraud. If the insured commits suicide within one or two years of the policy being in force, then no death benefits will be paid, only a refund of premiums.

Beneficiaries

In the assignment of beneficiary designations, there are always two categories: primary and contingent beneficiaries. The primary beneficiary is the person (or entity) who is first entitled to the death proceeds. Of course, more than one primary beneficiary can be named. The contingent beneficiary is the person (or entity) who would be entitled to the death benefits if the primary beneficiary or beneficiaries are dead or unable to receive benefits. One easy way to deal with beneficiary assignments of multiple family generations is to use either the "per capita" or "per stirpes" description. It's easy to accidentally disinherit family members without proper wording. If your intent is to leave your benefits, for example, to your surviving children, a "per capita" designation might be appropriate, whereby your surviving children would share the proceeds each receive an equal share of the benefits intended for that family line. It is critical that both primary and contingent beneficiaries be named to ensure the proper planning.

Beneficiary designations can be deemed revocable or irrevocable, depending on the contract's flexibility. If revocable, the policy owner can change the beneficiary designation at any time without the beneficiary's consent or notification. With an irrevocable designation, the policy owner cannot change the beneficiary designation without the beneficiary's consent, such as in a business or key man policy. (For more insight, see *Life Insurance Distribution And Benefits*.)

Distribution Options

Life insurance benefits can be distributed in a number of ways. The most obvious is the lump sum distribution, which is essentially a one-time payment in cash. With an "interest option", the death benefits are left with the insurance company but paid out at a later time, in which case a minimum guaranteed rate of interest is paid to beneficiaries. Beneficiaries can also opt for an "installment option", whether a fixed installment period or fixed installment amount. The latter option is sometimes used by policy owners to ensure that the beneficiary does not spend all the money at once. Finally, the "life income" option, which is much like an annuity, also pays the life insurance proceeds over time, but based on the beneficiary's life expectancy. The life income option has several payout possibilities:

Straight Life Income: Proceeds are paid to the beneficiary on the basis of life expectancy.

Life Income with Period Certain: The beneficiary is paid for as long as he or she is alive, but with a minimum number of guaranteed payments.

Life Income with Refund: The beneficiary is paid as long as he or she lives, and if original principal remains after the beneficiary dies, then it is paid to a contingent beneficiary.

Joint and Survivor Income: Income is paid to two beneficiaries, with payments continuing to the survivor after the first payee dies.

Next: Intro To Insurance: Other Insurance Policies

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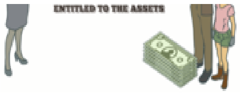

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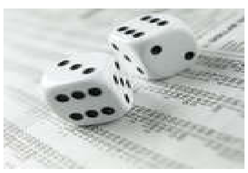

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