Investment Solutions, Inc.

The Long Run
Newsletter

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Term vs. Permanent Life Insurance

According to industry experts, most people don't have enough life insurance. The American Council of Life Insurers recently reported that average coverage equals $197,000, which is equivalent to almost 3.5 years in terms of income replacement (with the median income being $59,540 in 2024, according to the Bureau of Labor Statistics). That's only half the recommended 7-year threshold.[1,2]

Furthermore, 38 percent of consumers said that their households would be in financial trouble within six months if a wage earner died today.[3]

When considering life insurance, one of the most important factors to understand is the difference between term and permanent insurance. Here's an inside look at both.

Term and Perm

Term life insurance is temporary; it provides a death benefit for a specific term, such as 10, 20, or 30 years. Unlike other types of life insurance, it does not accumulate a cash value. If the policyholder dies during that term, their beneficiaries receive the benefit from the policy. When the contract ends, so does the coverage.

This limited term leads to term life insurance's main advantage: price. Generally, term life insurance costs less than permanent life insurance, especially if the purchaser is younger. This has the potential to free up funds for other household expenses.

Permanent insurance remains in place as long as the policyholder makes payments. In addition, permanent policies are designed to build up "cash value," a cash reserve that accumulates with the policy. Typically, this cash reserve pays a modest rate of return. However, the policyholder has limited access to the funds.

Which Should You Choose?

Term life insurance can be designed to provide protection against upcoming expenses, such as putting children through college. Permanent life insurance, on the other hand, can be more useful for covering long-term financial needs, such as estate planning.

Many people find that they have a combination of short- and long-term needs. In such circumstances, it may be prudent to have both types: a basic level of permanent life insurance supplemented by a term policy. A review of your situation may help determine what type of life insurance is appropriate.

Several factors will affect the cost and availability of life insurance, including age, health, and the type and amount of insurance purchased. Life insurance policies have expenses, including mortality and other charges. If a policy is surrendered prematurely, the policyholder may also pay surrender charges and have income tax implications. You should consider determining whether you are insurable before implementing a strategy involving life insurance. Any guarantees associated with a policy are dependent on the ability of the issuing insurance company to continue making claim payments.

Term or Perm?

In 2022 people purchased more permanent life insurance policies than term life insurance policies. However, term policies account for approximately 71% of the face amount of the policies issued.[1]

Source: ACLI.gov, 2023

Citations:

1. ACLI.com, 2023
2. BLS.gov, 2024
3. LIMRA.com, 2023

What Is a 1035 Exchange?

According to the most recent information available, Americans have individual life insurance with a total face value of $14 trillion.[1]

Due to a variety of factors, these individuals may find themselves in circumstances where the specific life insurance policy or annuity contract they own does not suit their needs. They may want to exchange products without incurring a taxable event.[2]

That's where Section 1035 of the Internal Revenue Code comes in. A 1035 exchange provides a means for exchanging an annuity contract or life insurance policy without being treated as if it had been surrendered or sold. Keep in mind that a 1035 exchange can be used only when it involves the same contract or policyholder and the same type of product.[3]

Trading In an Older Policy

A 1035 exchange, provided certain requirements are met, gives policy or contract holders the flexibility to "trade-in" an older contract or policy for a newer contract or policy. A newer policy or contract may have lower costs, a higher death benefit, or more investment choices.

1035 exchanges involve a complex set of tax rules and regulations. Before moving forward with a 1035 exchange, consider working with a tax professional who is familiar with the rules and regulations.

Partial Exchanges

Also, individuals can do a partial 1035 exchange for a portion of the total contract. A tax professional should be consulted for a partial exchange because any gain may be subject to ordinary income tax when withdrawn.

Key Considerations

Several factors will affect the cost and availability of life insurance, including age, health, and the type and amount of insurance purchased. Life insurance policies have expenses, including mortality and other charges. If a policy is surrendered prematurely, the policyholder may also pay surrender charges and have income tax implications. You should consider determining whether you are insurable before implementing a strategy involving life insurance. Any guarantees associated with a policy are dependent on the ability of the issuing insurance company to continue making claim payments.

Annuities have contract limitations, fees, and charges, including account and administrative fees, underlying investment management fees, mortality and expense fees, and charges for optional benefits. Most annuities have surrender fees that are usually highest if you take out the money in the initial years of the annuity contract. Withdrawals and income payments are taxed as ordinary income. If a withdrawal is made prior to age 59½, a 10% federal income tax penalty may apply (unless an exception applies). The guarantees of an annuity contract depend on the issuing company's claims-paying ability. Annuities are not guaranteed by the FDIC or any other government agency. The earnings component of an annuity withdrawal is taxed as ordinary income and, if taken before age 59½, may be subject to a 10% federal income tax penalty. Annuities have fees and charges associated with the contract, and a surrender charge may also apply if the contract owner elects to give up the annuity before certain time-period conditions are satisfied.

Variable annuities are sold by prospectus, which contains detailed information about investment objectives and risks, as well as charges and expenses. You are encouraged to read the prospectus carefully before you invest or send money to buy a variable annuity contract. The prospectus is available from the insurance company or from your financial professional. Variable annuity sub-accounts will fluctuate in value based on market conditions and may be worth more or less than the original amount invested if the annuity is surrendered.

Citations:

1. ACLI.com, 2024
2. Endowment contracts and qualified long-term care contracts also may be eligible for a 1035 exchange. A tax professional should be consulted before considering an exchange.
3. Investopedia.com, November 14, 2023

For Your Information

- We are open from 9:00 a.m. – 5:00 p.m. Monday through Thursday, and 9:00 a.m. – noon on Fridays.
- We are open during the lunch hour.
- We have a mail drop on the far north door of the building. If you have any information you would like to deliver after normal business hours please drop it off there.

When one flower blooms,
spring awakens everywhere.

"Spring is nature's way of saying, 'Let's party!'"

— Robin Williams

Long & Associates, P.C.

Assisting you with accounting, tax preparation, and tax planning

Investment Solutions, Inc.

Advising you and creating strategies for investment and retirement planning

Benefit Resource Group, Inc.

Handling employee benefits and other business services

Whether you need one of these services, or all three, you'll work with the same professional, knowledgeable staff with our Comprehensive Solutions Program

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