



Significance of Life Insurance



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About this book

Most of us spend plenty of our time planning for Goals and give relatively little thought to the issue of life insurance. Very often, people buy life insurance right after they get married or have their first child and don't give it another thought until their policies are set to expire.

Life Insurance gives peace of mind while we plan for our family's future. How much life insurance cover we need really depends on our circumstances and the type of protection we're looking for.

You need to ensure that the insurance covers all your dependents and that it also covers the majority of health problems.

To educate yourself about life insurance basics you can use our resources and Insurance needs calculator from www.ifea.in.

Happy Reading!

Rs.40/-

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Significance of Life Insurance



Preparing for family's future, is more than investing appropriately for goals and time horizon. It also involves purchasing the right amount of life insurance to protect family's lifestyle. Life insurance can help in reducing the financial impact in the event of death. Life insurance policy provides the opportunity to help replace lost income, eliminate debt, pay for college, keep a business going, protect family wealth, or other financial needs while family adjusts to a new life.

Principles of Life Insurance

Life insurance is based on a number of principles that are tailored to meet market conditions and ensure insurance companies make profits, while offering security to insured individuals.

There are broadly four major insurance principles applied in India, these being:

Insurable Interest

This principle pertains to the level of interest an individual is expected to have in a particular policy. The interest could be a family bond, a personal relationship and so on. Based on the interest level, an insurance company can choose to accept or reject an application in order to protect the misuse of a policy.



Law of large numbers

This is a theory that ensures long-term stability and minimizes losses in the long run when experiments are done with large numbers.

Good faith

Purchasing insurance is entering into a contract between company and individual. This should be done in good faith by providing all relevant details with honesty. Covering any information from the insurance company may result in serious consequences for the individual in the future. This being said, the insurer must explain all aspects of a policy and ensure that there are no unexplained or hidden clauses and that the applicant is made aware of all terms and conditions.



Risk & Minimal loss



Risk is spread out among all policyholders that the insurer deals with. All customers of the insurance company contribute money to the general account. This money is invested, and then claims are paid out when an individual from the group dies.

The principle of minimal risk states that the insured individual is expected to take necessary action to limit him/ her from any hazards.

How Life Insurance Works

There are three major components of a life insurance policy.

Death benefit

1. (Sum Assured on Death) is the amount of money the insurance company guarantees to the beneficiaries identified in the policy upon the death of the insured. The insured can choose the desired Sum assured based on estimated future needs of surviving heirs. The insurance company will determine whether there is an insurable interest and if the insured qualifies for the coverage based on the company's underwriting requirements.



Premium

2. Payments are set using actuarially based statistics. The insurer will determine the cost of insurance (COI), or the amount required to cover mortality costs, administrative fees, and other policy maintenance fees. Other factors that influence the premium are the insured's



age, medical history, occupational hazards, and personal risk propensity. The insurer will remain obligated to pay the death benefit if premiums are submitted as required. With term policies, the premium amount includes the cost of insurance (COI). For other policies, the premium amount consists of the COI and a cash value amount.

Cash value

3. Cash value of endowment / whole-life insurance **(Maturity Benefit / Survival Benefit)** is a component that serves two purposes. It is a savings account, which can be used by the policyholder, during the life of the insured, with cash accumulated on a tax-deferred basis. Some policies may have restrictions on withdrawals depending on the use of the money withdrawn. The second purpose of the cash value is to offset the rising cost or to provide insurance as the insured ages.





**Make sure these smiles
never fade from your
loved one's faces**

A Term Insurance Plan is the best economical product, which can safeguard your loved ones against odd financial crunch in your absence.

The amount of Life Insurance coverage you need will depend on many factors such as:

- How many dependants you have
- What kind of lifestyle you want to provide for your family
- How much you need for your children's education

As a thumb rule, Sum Assured is determined based on $\text{Annual Income} \times 10 \text{ times} + \text{Loans/Liabilities}$



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Reasons Why Life Insurance Is Important

Most people are unaware of the importance of life insurance. Here are some reasons why you must consider taking life insurance –

1. Pay off Debts:

In case of a crisis, you would not want your family to deal with financial problems. If you buy the right life insurance policy, then any outstanding debts like a car loan, home loan, and other personal loans will be taken care of.



2. Your family will be taken care of:

Nobody wants their family to depend on somebody else if something were to happen to them. Whether it is paying for the education of child or making sure spouse is financially secure, life insurance can secure family's financial future.



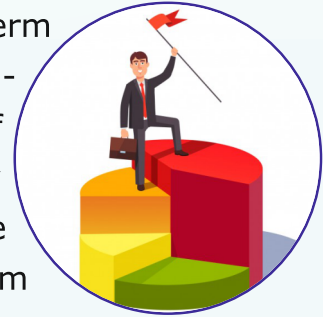
3. Supplement Retirement Goals:

We all want our retirement savings to last, don't we? And they will if you invest in a good insurance plan. With the right life insurance plan, you can get a regular stream of money every month after your retirement.



4. Achieve Long Term Goals:

Taking a life insurance policy is a long-term investment, which can help you achieve long-term goals. You create a second source of income or leave a legacy. Before buying any policy, consider your options. Select the one you think would help you meet your long term goals.



5. It can save your business:

Life insurance can not only protect your family, but also your business. There are some policies that can take care of business owners. In case of unfortunate event, business share can be purchased by surviving partner and sum assured would be given to nominee.



6. Tax Benefits:

Irrespective of what plan you buy, you could save tax with insurance policies. As per Section 80C of the Income Tax Act, 1961, the premium paid for life insurance policies qualify for deduction, up to a maximum of Rs. 1.5 lakhs a year. Also, the maturity/death benefit is tax-free as per Section 10 (10D) of the Income Tax Act on meeting the premium to sum assured criteria.



7. Might not be qualified for it later:

Life insurance policies always run on uncertainties. You may be healthy now and paying for life insurance may seem like an added financial burden. But if something happens to you all of sudden and on getting better, you'd realize that you should take a life insurance policy; however, at that time, you may not be allowed to buy a policy. This is why it is best to buy one policy as early as you can because it will still remain in force even if you start having health problems.



8. A tool for forced savings:

If you choose a traditional or unit-linked policy, the premium you will pay every month will be higher than the cost that is required to insure you. This extra money that you pay gets invested. You can choose to surrender or borrow the cash against the policy in case of an emergency.



Life Insurance Riders

Many insurance companies offer policyholders the option to customize their policies to accommodate their personal needs. Riders are the most common way a policyholder may modify their plan. There are many riders, but availability depends on the provider.



- The accidental death benefit rider provides additional life insurance coverage in the event the insured's death is accidental.
- The waiver of premium rider ensures the waiving of premiums if the policyholder becomes disabled and unable to work.
- The disability income rider pays a monthly income in the event the policyholder becomes disabled.
- Upon diagnosis of terminal illness, the critical illness rider allows the insured to collect a portion of Sum Assured.

Each policy is unique to the insured and insurer. Reviewing the policy document is necessary to understand the coverage in force and if additional coverage is needed.

Ways in Choosing Life Insurance

Once you understand the importance of taking out a life insurance policy, you need to make the right choice. To do this, you need to ask yourself about your needs and purchase a product that works for your family and your budget. A financial security advisor can help you with this.

You need to ask yourself three main questions to figure out what type of life insurance would work best in your situation.

Family and work situation

First of all, your insurance needs will be influenced by the following: your family situation, your age, your health situation and whether you are an owner or self-employed.



Life insurance is important, whether you are single or in a relationship. In the event of your death, your loved ones will have to pay your funeral expenses and pay off any financial liabilities you have, such as your debts. If you have insurance coverage, your debts will not be a burden for your family members. In addition, your loved ones may also have to bear some of your shared responsibilities, such as your credit card fees, your lease, your car payment, your mortgage payment, your student debt, or other. If you have children, life

insurance will let you replace the lost income from one of the parents to provide for the children's needs.

Life insurance is also an effective financial tool for protecting your business. It lets you ensure you and your loved ones' financial security should something bad happen. If you start your own business with a partner who passes away prematurely, will you have the funds needed to buy out his/her shares and continue moving forward with your dream? An unfortunate event like this could have a major impact on your company. So you need to start thinking about it now. If you don't have coverage, getting a policy will let you cover your needs as a self-employed person and will avoid future concerns for your family.

Life goals

Your personal, family and professional goals will also determine your choice of life insurance. For example, do you plan on having children? What are your career and income goals? At what age would you like to retire?



This will help you evaluate how much life insurance you should take out to protect your loved ones in the event of death.

Coverage type

You have thought about your situation and life goals. Now all you need to do is figure out what type of coverage is best for you.

For example, you might ask yourself if you need short-term or long-term coverage. Do you want coverage that generates liquidity and surrender value that you can use to reach your goals, etc.? Once you answer these questions, you will be well equipped to choose the life insurance that works best for you.



What are the advantages of Life Insurance?

There are various benefits of having a life insurance cover.

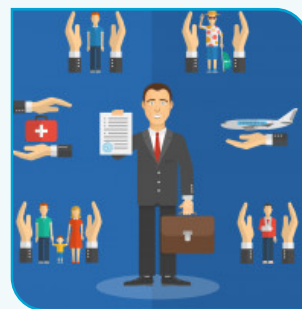
😊 **Peace of Mind/ Financial Security**

Having life insurance provides the ultimate peace of mind, knowing that family and loved ones will have a financial safety net. All of us have some financial liabilities at some point, but an adequate life insurance cover ensures that debts are taken care of, in case of some mishap.



😊 **Wealth Creation**

Some life insurance plans also offer you the opportunity to create wealth. Apart from life cover, these policies invest your premium in different investment classes to deliver risk-adjusted returns and grow your corpus.



😊 **Tax Savings**

Life insurance plans offer dual tax benefits. The premiums paid offer tax deduction under section 80C of the Income Tax Act. This means up to



₹ 1.50 lakh premium paid annually is deducted from your gross income, thus lowering your tax outgo. Separately, the maturity insurance plans may be entirely tax-free. This tax benefit is under Section 10(10D) of the Income Tax Act.

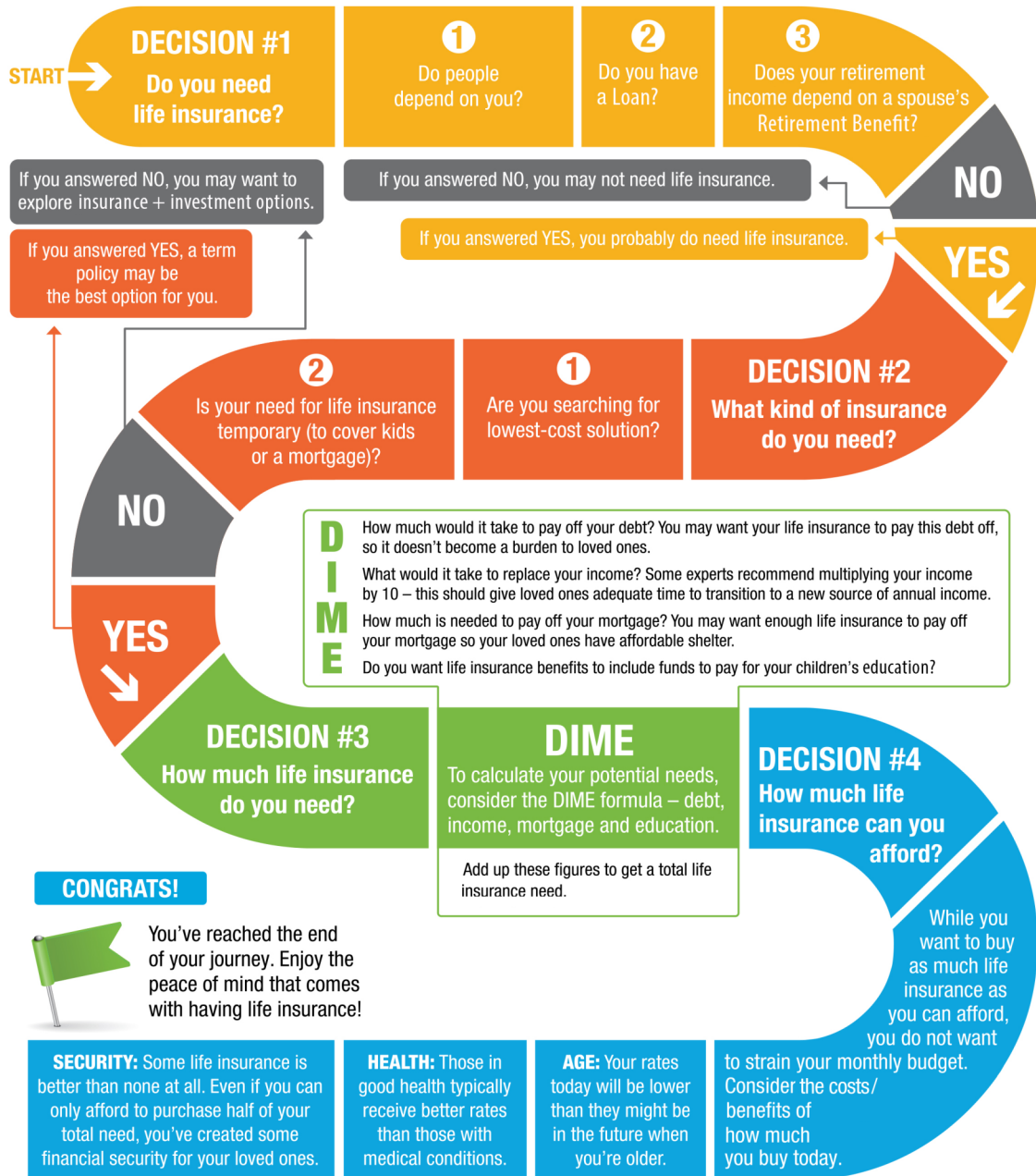
Buy Young, Save More

Life insurance plans give you the ability to lock in low premium rates while you're young. If you buy the same policy when you are older, you will be paying a much higher premium compared to if you bought the same plan when you were younger.



The important thing is to choose the right solution for your budget and your needs. Over the years, your needs, your family situation and your life goals will evolve. When that happens, it will be time for you to re-evaluate the right type of insurance for you to ensure you are covered properly. Remember that you are never too young to buy life insurance, since the younger you are, the lower the cost of your premium.

Your Life Insurance Decision Journey



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Factors involved in Life Insurance

Life insurance is a great way to protect our loved ones financially. Over a period of years, even a slightly lower premium can yield major savings. The following are some of the biggest factors that insurers consider when pricing out their policies. Some of these criteria are outside their control, while others are things you can remedy with simple lifestyle choices.

Age

The number one factor behind life insurance premiums is the age of the policyholder. If the policyholder is young, the premium is lower. Hence, it would be better off taking out a policy before it's too late



Life style

Higher premiums are directly related to any lifestyle factors that come with increased medical costs, or a raised chance of disability or death. On the other hand, if they are in great shape with a healthy lifestyle may be eligible for discounts, reduced premiums and other bonuses from insurers. Some lifestyle factors can be determined through medical tests, blood tests, BMI calculators and other methods.



Occupation

What one does for a living can affect their life insurance rate as well. If their work requires performing dangerous duties that put them at a higher risk of accidental death, they will pay higher insurance rates. In turn, if they are exposed to toxic chemicals or their job is known to have other long-term health effects, they will likely pay more for their coverage.



Family Medical History

As we previously discussed, their medical history has an effect on their life insurance coverage. Their family's medical history will also play a role in determining their rates. If they do not have relatives with serious health issues, especially those that are hereditary, their cost for coverage will be higher.



The Policy type

The type and length of their policy and the amount of their benefit all contribute to the rate they will be paying for their life insurance coverage. Basically, the longer the term and the larger the amount, the more they will be paying. In addition, whole or endowment life insurance policies are generally more expensive than term life insurance policies.



Purpose of Insurance

There are a few different reasons for which the policy holder might be purchasing a life insurance policy and each plays its own role in determining their rate. Whether they are purchasing a policy as part of their estate planning or for their family's or business's protection, their insurance rates will change accordingly depending on the type of policy chosen.



The degree to which each of these factors affect the life insurance rate will depend on the severity of each and the insurance provider you choose.

Select the best life insurance plan/policy in 3 easy steps:

Once the policy holder has identified the need to take life insurance, they should know about getting some basic steps right to select the best life insurance policy.

- **Engage an insurance advisor:**

While this may seem trivial, engaging a reliable and competent insurance advisor at the initial stage in your quest for life insurance is critical. Most individuals might delay the decision

and it is better to seek the expertise of an insurance advisor.



- **Calculate the life cover:**

The insurance advisor will help to calculate the amount of life cover – or the sum assured. He will assess sources of income, number of dependents, debts and liabilities and expenses based on lifestyle and arrive at a life cover. He will also decide the best plan be it – a term plan, endowment plan, unit-link plan or a combination of plans, to provide with an optimum life cover.

Likewise, if you have other needs like planning for their child's education or marriage, pension for retirement, trust the advisor to do the math and come up with an ideal solution.

- **Compare insurance plans:**

Since there are many insurance companies in the market offering a variety of plans, you need to be sure to select the most suitable one. The insurance advisor will do the homework by comparing life insurance plans from various insurers across relevant parameters recommending the most apt plan based on your needs.



How much Life Insurance do you need?



It is very much essential for an individual how much life insurance they would require apart from the one given by their employer to safe guard family in a comfortable and worry-free way. Having group life insurance, or life insurance through their employer, certainly has its benefits. It's easily accessible and often cheap or free. However, sometimes amount of coverage provided by group insurance isn't enough for them.

Is the insurance held up with the employer enough?




The answer is No. The life and health insurance coverage provided by the employer has its own benefits and limitations as well. First, employer-based policies often don't provide enough coverage to replace your income for very long. Second, employer-based policies typically end soon after you leave the job. This means if you quit your job or get laid off or fired, your family could find themselves without coverage when they need it.

When would an individual require more life insurance?



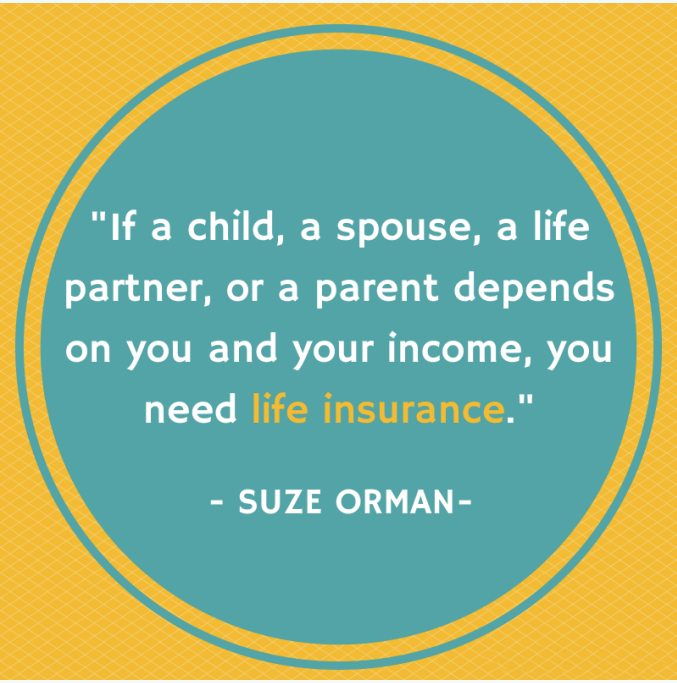
It's up to the individual to check whether their employer-sponsored coverage meets their needs. Remember the primary functions of life insurance: cover final expenses, pay off their mortgage, replace lost income and pay for their children's education. If a single parent or the only working spouse, don't skimp on the life insurance.



If employer's coverage isn't enough for their family's needs, they have two options. First, they can opt for buying additional coverage from their employer's insurance company. Or buy supplemental life insurance in the open market.

Before they go with option one, considering how long they are likely to stay in their job is essential. If layoffs are looming or if they are looking around for other opportunities, adding to their employee policy probably won't be the best idea.

Even if they are planning on staying at their job for many years, sticking with the same insurance company might not be the best bet.



"If a child, a spouse, a life partner, or a parent depends on you and your income, you need **life insurance**."

- SUZE ORMAN -

[illegible]

Life Insurance

who should get it?

The sooner you buy life insurance, the less it may cost over time.
Having life insurance makes sense for these individuals:



Married



Married With Kids



Single Parent



Stay-at-Home Parent



Parent of
Grown Children



Retired



Family
Caregiver



Small-Business
Owner

Life insurance may never be cheaper or easier to come by than now, while you are young and healthy. Help protect your loved ones today.



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About IFE Academy

IFE Academy was established in 2011 as a Not-for-Profit entity to promote Financial Education. IFE Academy conducts Investor Awareness Programs across the country with the support of other market participants. www.ifea.in is a comprehensive website on Financial Education. It has various sections such as Videos, Puzzles & Games, Financial Calculators and Library. It gives a holistic view on financial education combining various aspects such as Savings, Investments, Credit, Insurance and Pension at a single place. IFE Academy periodically publishes Investor Educational materials and distributes it to general public.



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