# A guide to life insurance

This booklet is designed to help you understand life insurance and to become an informed consumer. Additional information–and help–is available from your life insurance agent and company as well as from the Consumer Assistance Centre.

Canadian Life and Health Insurance Association Inc.

Association canadienne des compagnies d'assurances de personnes inc.

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## You Told Us What You Want To Know about Life Insurance

*This booklet on life insurance brings together the answers to many typical questions Canadians ask when they call the Consumer Assistance Centre of the Canadian Life and Health Insurance OmbudService (see page 29).*

*Every weekday on national toll-free phone lines **(1-800-268-8099 English, 1-800-361-8070 French)**, we listen and talk to people whose financial goals and problems may differ in many ways. Yet, some of the basics never change: their desire to provide financial protection after their deaths for those closest to them and to ensure that their survivors or dependents can avoid financial hardship.*

*This booklet will help you to:*

- *estimate how much life insurance you need;*
- *understand the different types of policies and options;*
- *understand what happens when you apply, and when there's a claim; and*
- *develop information and questions to discuss with your agent.*

*This booklet is not intended to be a substitute for seeking out a qualified agent. Rather, it is designed as a handy reference you will want to keep with your insurance policies. We suggest you start with the Table of Contents and look for the topics in which you're most interested.*

*Along with many other consumer booklets on related topics (see page 29), this booklet is produced by the Canadian Life and Health Insurance Association. We do not promote any one life insurance company or any particular type of life insurance policy or plan. We leave that choice to you, the consumer.*

*Our objective is to provide the background and insights that will help you to make successfully one of your most important financial planning decisions: purchasing life insurance.*

**Caution:** *This booklet is intended to present a wide variety of general information on life insurance as simply and as accurately as possible. But it is not a legal document; over time, court rulings and legislation may change some of the rules and conditions stated here. If you have specific questions, check your policy and contact your insurance agent or company.*

## Life Insurance: What Is It?

The concept of insurance goes back to the days of the Romans, but it wasn't formalized until the 18th century. Essentially, it's a means of spreading financial risk among a large number of people who pay into a fund or pool. In this way, the cost is minimized for those who suffer an unexpected misfortune.

Life insurance is a way to protect your survivors and dependents against financial hardship. A life insurance contract or *policy* is a legal agreement between you and an insurance company that guarantees payment of the *face value* of the policy, upon death.

A valuable feature of life insurance is that the benefit paid to your beneficiary is almost always tax free.

## How Much Is Enough?

How do you figure out how much life insurance you need? A ballpark measure sometimes used is between five and seven times current net income. But to work out the specifics of your own situation, you'll want a *financial needs analysis.* It gives you a picture of the capital your survivors need when you die. It looks at assets that would be available to them, liabilities they would have to deal with, and continuing family needs for income. *(See the worksheet on page 31 to work out an estimate of your needs.)*

**A qualified life insurance agent can help you work out a more comprehensive financial needs analysis.**

**Tip**

***It's important to review your insurance needs regularly. As your family or business situation changes, so may your insurance needs. Beware, too, of future inflation and the way it could erode your insurance.***

## Do You Need Life Insurance? Thoughts To Mull over...

- If you are in a personal partnership (usually marriage), how much do you contribute to the family budget? If you were to die prematurely, how would your survivor(s) get by, especially dependent children?
- Does anyone else depend on you financially, such as a parent, grandparent, brother or sister?
- If you are a single parent, what level of support payments are you making or getting? How would these be kept up in the event of the contributor's death?
- If you have a mortgage on your home, do you want it paid off in the event of your death?
- If you have children, do you want to put aside money to complete their education in the event of your death?
- Are there any other family members or organizations to

whom you would like to leave money?

- Could life insurance play a role in business or farm succession plans?
- Could life insurance play a role in paying the taxes incurred when capital property is transferred from one generation to the next?

# 2 LIFE INSURANCE POLICIES

## What Different Policies Will Do for You

Though it seems there is a bewildering array of policy types and names, they all boil down to two basic forms of life insurance: permanent and term.

As a rule, permanent needs should be covered with permanent insurance, temporary needs with term insurance. Often, a combination of policy types does the best job for you.

So, what is a temporary need? A mortgage; high needs for continuing income when your children are young; some business obligations; and so on.

Permanent needs? Funeral expenses; supplementing a survivor's income; covering capital gains taxes at death, especially if family property is to be passed on to the next generation; and children who remain dependent for their lifetimes, often due to a disability.

## PERMANENT LIFE INSURANCE

Permanent life insurance has several variations: whole life, universal life, variable life. All are designed to provide insurance protection for your entire lifetime, as long as you keep the policy in force.

### Basic features of permanent policies

- ***Level premiums:*** Most permanent policies have premiums that remain level over the lifetime of the policy, even though the risk of death increases with age. To achieve this, the premiums charged in the initial years are higher than the risk you represent then and are invested to form policy reserves that subsidize the premiums paid in later years when you are older and the risk is higher.
- ***Cash values:*** These reserves accumulate as a

*cash value*, or *cash surrender value*. The cash value is available to you if you want to borrow against your policy or to cancel (surrender) it. (Usually, the cash value is not added to the face amount of the policy, which is paid out on your death.)

**Tip** ***Before withdrawing any or all of the available cash value, ask if there are any tax implications. A portion of the cash value may represent earnings that become taxable on withdrawal.***

- ***Non-forfeiture options:*** These are choices available to a polic holder if he or she discontinues premium payments on a policy. They allow the policyholder to keep the policy in force or to take a cash settlement. *(For more, see pages 12 and 13.)*

- ***Participating policies and policy "dividends":*** A *participating policy* shares in the financial experience of the insurance company, and policy "dividends" are declared annually and paid to policyholders.

Premiums are based on conservative estimates of future expenses, death claims and interest or other investment earnings. When experience is more favourable than these estimates, a surplus is created, which allows the company to credit participating policyholders with dividends. Because dividends are based on future experience, such as costs and earnings, they are *not* guaranteed.

Dividends can be paid in cash, left in the policy to accumulate, used to pay part of the premiums, or used to purchase additional insurance. *(See page 14.)*

- ***Non-participating policies:*** A non-participating policy does not share in the insurer's earnings and does not receive any dividends.

### Variations of permanent insurance

Although every permanent insurance policy is designed to provide you with coverage for your entire life, the guarantees vary in different policies. This, in turn, affects the premium you pay.

- ***Whole life:*** This is the traditional policy that fully guarantees the level of premiums you pay, the death benefit and the growing cash values within the policy.

- ***Interest-rate sensitive policies:*** Unlike whole life policies, which use very long term interest rate assumptions, these policies use current interest rates, which can be adjusted periodically if interest rate levels change. This offers the policyholder the potential of getting more coverage for less premium, but it involves sharing some of the risk with the insurer. Premiums could be increased if interest rates decrease. On the other hand, premiums could be decreased if the reverse holds true.

The most popular and flexible of the interest-rate sensitive policies is **universal life.** It consists of two parts: life insurance and an investment account. You decide what to do with each part of the policy, and you can increase or decrease your premiums and your death benefit, within certain limitations. Earnings on the investment account may or may not be guaranteed, depending on the type of investment chosen.

"New money" or "adjustable" policies usually guarantee the premiums and death benefit for a specified stretch of time (e.g., five years) and re-adjust the premiums and/or death benefit at the end of the period, according to investment conditions at that time.

- ***Variable life:*** Here, the premiums usually are guaranteed, but the cash values vary according to the performance of an investment fund or other index. The death benefits may be guaranteed or may vary with the fund's performance, subject to a minimum guarantee.

## TERM LIFE INSURANCE

Term policies provide insurance coverage for a specified period (e.g., a fixed number of years, or to a set age) and then expire. A death benefit is paid only if you die during the term of the policy.

**Renewable and convertible term insurance**

***Renewable** means that you can renew your policy at the end of its term, for a higher premium, without submitting medical or other evidence of insurability. (Once you've reached the age of 70 or so, the policy may not be renewable.) **Convertible** means that you have the option of exchanging your policy for a permanent insurance policy, without submitting evidence of insurability.*

**Tip**

***If your immediate obligations are large and the funds available to spend on insurance are small, go for whatever insurance policy will meet your needs now. If your choice is term insurance to start with, make sure it's renewable and convertible into a permanent policy. This will give you the flexibility to make changes later on.***

Term policies are commonly available for terms of one, five, 10 or 20 years, or to age 60 or age 65. The premiums usually remain level during the specified term but increase if that term is renewed (e.g., premiums would increase every five years on a five-year renewable term policy).

Most term policies are non-participating and do not include cash values or other non-forfeiture values. Hence, premium costs are lower than for permanent policies — at least when you're younger.

## TERM TO 100

Often categorized as a permanent plan, term to 100 policies provide life insurance coverage through to age 100. Usually they don't pay dividends or include cash values, though some may provide other non-forfeiture values. Accordingly, premiums are lower than for traditional whole life policies.

***To compare the features of different types of policies, see the following chart.***

# Types of Life Insurance

| | Permanent | | Term to 100 | Term |
|---|---|---|---|---|
| **Policy Type** | **Whole Life** | **Universal Life** | | |
| **Period of Coverage** | Life | Life | To age 100 | Depends on term in contract. Often renewable for additional terms but usually not past age 70 or 75. |
| **Premiums** | Guaranteed. Usually remain level. | Flexible. Can be increased or decreased by policyholder within certain limits. | Guaranteed. Usually remain level. | Guaranteed and remain level for term of policy (e.g., 1 year, 5 years, 10 years, etc.). Increase with each new term. |
| **Death Benefits** | Guaranteed in contract. Remain level. Dividends may be used to enhance death benefits in participating policies. | Flexible. May increase or decrease according to fluctuations in cash value fund. | Guaranteed in contract. Remain level. | Guaranteed in contract. |
| **Cash Values** | Guaranteed in contract. | Flexible. May increase or decrease according to investment returns and level of policyholder deposits. | Usually none. (Some policies have a small cash value or other non-forfeiture value after a long period, say, 20 years.) | Usually none. (Some long term policies have a small cash value or other non-forfeiture value.) |
| **Other Non-forfeiture Options** | Guaranteed in contract. | Guaranteed in contract. | See above. | See above. |
| **Dividends** | Payable on "participating" policies. Not guaranteed. | Most policies are"non-participating" and do not pay dividends. | Most policies are "non-participating" and do not pay dividends. | Most policies are "non-participating" and do not pay dividends. |

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| | Permanent | Term to 100 | Term |
|---|---|---|---|
| **Advantages** | ✔ Provides protection for your entire lifetime – if kept in force.<br>✔ Premium cost usually stays level, regardless of age or health problems.<br>✔ Has *cash values* that can be borrowed, used to continue protection if premiums are missed, or withdrawn if the policy is no longer required.<br>✔ Other *non-forfeiture options* allow the policyholder various possibilities of continuing coverage if premiums are missed or discontinued.<br>✔ If the policy is *participating*, it receives dividends that can be taken in cash, left to accumulate at interest, or used to purchase additional insurance. | ✔ Provides protection to age 100 — if kept in force.<br>✔ Premium cost usually stays level, regardless of age or health problems.<br>✔ Premium cost is lower relative to traditional permanent policies. | ✔ Suitable for short term insurance needs, or specific liabilities like a mortgage.<br>✔ Provides more immediate protection because, initially, it is less expensive than permanent insurance.<br>✔ Can be converted to permanent insurance without medical evidence (if it has a convertibility option), often up to ages 65 or 70. |
| **Disadvantages** | ● Initial cost may be too high for a sufficient amount of protection for your current needs.<br>● May not be an efficient means of covering short term needs.<br>● Cash values tend to be small in the early years. You have to hold the policy for a long time, say over 10 years, before the cash values become sizable. | ● Usually no cash values and no or limited non-forfeiture values. | ● If renewed, premiums increase with age and at some point higher premium costs may make it difficult or impossible to continue coverage.<br>● Renewability of coverage will terminate at some point, commonly age 65 or age 75.<br>● If premium is not paid, the policy terminates after 30 days and may not be reinstated if health is poor.<br>● Usually no cash values and no non-forfeiture options. |

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### WHAT ABOUT GROUP LIFE INSURANCE?

If you are employed, you probably have this form of life insurance through your employer or union. Usually, it's term insurance (and available to age 65) issued to a group of people under a master contract. You receive a certificate as evidence of your coverage. For large groups, it is often issued without a medical or other evidence of insurability.

Your group insurance is a vital element in your total insurance coverage. But the coverage usually terminates if you cease to be a member of the group. Check to see if the plan allows you to convert to an individual life policy if you leave the group or if the coverage terminates for other reasons.

## Pricing and Costs

Setting premium rates for life insurance is unlike the pricing of other products where the cost of materials and production is known. It is even unlike car or household insurance, as life policies may stay in force for 50 years or more.

Insurance companies have no way of knowing exactly what their future costs, investment earnings or claims experience will be. Accordingly, they make long term projections based on statistical or actuarial experience, using *mortality tables* that show death rates at various ages of the population over time and making assumptions about future expenses, interest rates and mortality rates. These calculations are made by *actuaries* who are professionally trained in the mathematics of insurance.

### FAIR VALUE

Before your application is approved, the insurance company has to assess the degree of risk involved. Obviously, the older you are, or the poorer your health, the higher the risk you represent. Fair value is achieved by pooling similar risks together. Data and statistics are gathered and used to "classify" people by risk groupings. Insurance prices — the premiums — reflect the value of the risk assessed. The lower the risk of the group, the lower the premium. In evaluating risk, an insurance company looks at many factors, such as age, sex, medical history, physical condition, and so on. For example, women ordinarily pay lower premiums than men. This is based on overwhelming statistical evidence that women live longer. Lower premiums also apply to non-smokers. *(See page 20.)*

## Beneficiaries: Who Is the Life Insurance for?

The *beneficiary* is whoever is named (designated) under the policy to receive the insurance money on your death.

Do you want to name a beneficiary (e.g., spouse), or leave the money to your estate or to a trust? If the money is left to your estate, it will be subject to probate fees when the estate is settled. If you choose a trust, be sure to seek tax advice.

**Tip**

***If you name a beneficiary, the money does not go through your estate but goes directly to the person or organization you name. No probate fees apply.***

### CREDITOR PROTECTION

The beneficiary designation affects whether or not insurance proceeds are protected from your creditors. Provincial insurance laws provide that where a spouse, child, grandchild or parent is named as the beneficiary, the insurance money is exempt from seizure by any creditors you may have.

In Quebec, the beneficiary must be related to the policyholder. In other provinces, such a beneficiary must be related to the person whose life is insured.

This special protection includes adopted children in most provinces, but it does not apply to an ex-spouse unless he or she has been named an irrevocable beneficiary.

### IRREVOCABLE BENEFICIARY

You may name an *irrevocable beneficiary* or an *irrevocable trust*. This means that you, as the policyholder, can't change or revoke that beneficiary without the latter's consent. The money is protected from your creditors and doesn't become part of your estate. (In Quebec, a spouse is considered an irrevocable beneficiary, and divorce automatically cancels that preferred status.)

### WILLS

Note that a designation in a will does not override an earlier beneficiary designation under an insurance policy, unless the will specifically identifies the insurance policy in question. (However, even a specific will would not override an irrevocable beneficiary designation.) In one court case, a man, in his will, had named his present wife as sole beneficiary to his estate. But he hadn't changed the appointment of his former wife as beneficiary in his life insurance policy or identified the policy in his will. The court ruled that the former wife should get the money.

**Contingent beneficiary**

***This is someone who receives the proceeds from your policy if your primary beneficiary, such as your spouse, is no longer living.***

### DIVORCE

At the time of a divorce settlement, if you are the person who is to receive support money, make sure your payments are insured.

There are two ways of doing this using either existing or new policies:

(a) Make it part of the formal agreement that your ex-spouse take out life and disability insurance on his or her life naming you as beneficiary. If you want to ensure that the beneficiary can't be changed without your consent, require your ex-spouse to name you as irrevocable beneficiary.

(b) Take out a life insurance policy on your ex-spouse's life. Name yourself as beneficiary and pay the premiums. Then nobody can cancel the policy and you have control.

## WHAT HAPPENS IF MY BENEFICIARY DIES FIRST OR AT THE SAME TIME?

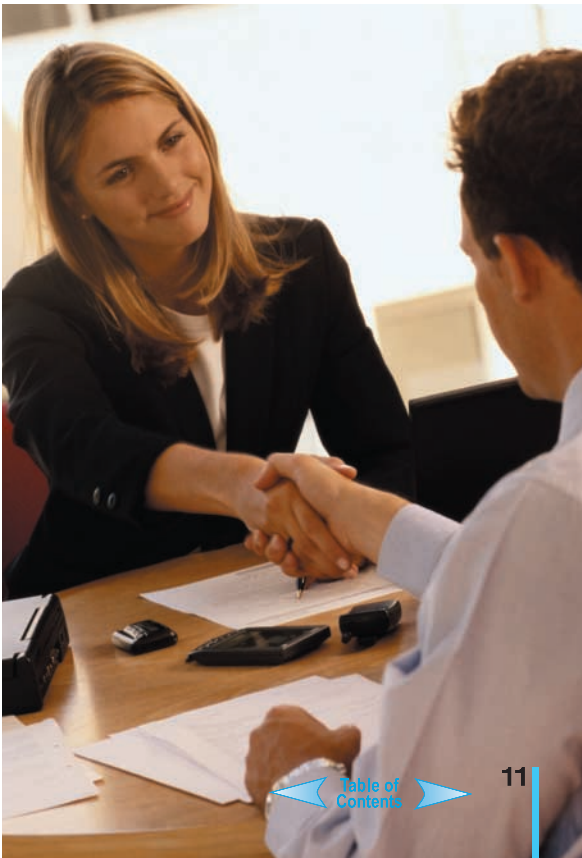
If your beneficiary predeceases you, the insurance money goes to your estate unless you have named a *contingent beneficiary*. In the case of death at the same time (e.g., in an accident), insurance law provides that the beneficiary is deemed to have died first. Again, the insurance money goes to your estate unless you have named a contingent beneficiary.

## WHAT HAPPENS IF MY BENEFICIARY IS A MINOR?

If the beneficiary is under the age of 18, the insurance company can pay the insurance money to a trustee (designated by the insured) who can receive funds on behalf of the minor. Alternatively, in most provinces, the insurance money can be paid into court until the beneficiary can give a valid discharge on receipt of the money.

## LEAVING MONEY TO CHARITY

You can use a life insurance policy to make charitable donations. On your death, the proceeds go to the organization you have named as beneficiary. If the charity is registered with Revenue Canada, the premiums can be tax deductible.



## Premiums: When and How To Pay Them

Typically, Canadians choose to pay their life insurance premiums on a monthly basis, usually through automatic bank withdrawals. There are other options available: annual, semi-annual and quarterly payments.

You can limit the number of years you pay premiums and telescope them into a shorter time-frame. Your premiums will be somewhat higher over those years, but afterward, your policy is free and clear. For example, you may wish to have a permanent life policy fully paid-up at age 65 so no premiums would be payable after retirement. (This differs from the premium offset concept, *discussed on page 14,* which is not guaranteed.)

### WHAT IF I HAVE TO STOP PAYING PREMIUMS?

There is a 30-day *grace period* after the due date to pay a premium. If the premium is not paid by the end of this grace period, the policy *lapses* (terminates). If death occurs during this period, the death benefit is paid, but any outstanding premium is deducted from that payment. Cash values in a policy can provide protection against lapsing *(see "Special Built-in Safeguards" in next column)*.

*Reinstatement* of a lapsed policy can usually take place within two years on payment of overdue premiums, plus interest, and submission of satisfactory medical evidence.

## Riders: Added Protection

A number of options, called *riders,* can be added to your policy to tailor it to your personal needs. For example:

- ***Accidental death and dismemberment:*** Guarantees an additional payment to your beneficiary, often doubling the amount of your policy, should you die from an accident. May also provide payment to you on loss of limbs or eyesight as a result of an accident.
- ***Disability waiver of premium:*** Pays your premiums and keeps your policy in force should you become totally disabled (usually takes effect once you have been disabled for a specified period of time [e.g., six or nine months].).
- ***Guaranteed insurability:*** Enables you to purchase additional insurance at specified times in the future without a medical or other evidence of insurability.

## Special Built-in Safeguards in Permanent Life Policies

These are called *non-forfeiture options,* and they mean exactly that. If for any reason you are unable to pay premiums, you don't have to lose (forfeit) your life insurance. The cash value can fund the following options, spelled out in the contract:

- ***Automatic premium loan:*** The cash values already built up in your policy may be used to pay premiums. Obviously, there are limits, depending on how much the cash values have grown over the years. But it does mean you won't have to *forfeit* your policy immediately if you are unable to meet a premium. It gives you breathing space to decide what to do about maintaining your coverage.

- ***Reduced paid-up permanent policy:*** Your cash value is used to buy a lesser amount of permanent insurance. No further premium payments are required.

- ***Extended term insurance:*** Your cash value is used to buy the same amount of insurance that you currently have, but as term insurance. No further premiums are required. As the new policy is term, it expires at some point. How long it continues depends on how much cash value is available. Obviously, the higher the cash value, the longer the extended term that can be bought.

## Policy Loans

The build-up of cash values in a permanent life insurance policy can be substantial the longer you hold the policy. It's a fund that can be used, as just mentioned, to keep your policy in force if you miss a premium. It's also available to you directly as a loan:

- You may borrow any amount up to or close to the total cash value in your policy, according to your contract. It can be repaid in a lump sum or in installments. Any unpaid balance plus interest is deducted from the proceeds of the policy at the time of your death.

- Interest is charged because the pricing of your policy assumes the company will invest those funds and earn interest.

- One major advantage is the ease with which you can take out a policy loan. No credit checks, none of the usual hassle. Just request it through your agent or the branch office of your life insurance company. (If you have an irrevocable beneficiary, you'll also need his or her signature.)

- The loan may be fully or partially taxable. Check with your insurer about the tax consequences.

## Policy Dividends: How To Make the Best Use of Them

Dividends occur in *participating* life insurance policies. How you make use of them is vital to getting the best value from your life insurance.

These are the most common *dividend options:*

- ***Increase your coverage:*** Use your annual dividends to add extra amounts of coverage to your policy, at no cost to you. The most popular use of dividends, this option is called *paid-up additions* or *bonus additions.* This option also increases future cash values. Alternatively, dividends could be used to purchase one-year term insurance.

- ***Enhanced protection:*** You can combine the two options mentioned above by using dividends to purchase a combination of paid-up insurance and one-year term insurance to provide additional protection equal to a pre-determined amount. As dividends increase over time, they are used to replace the term insurance with paid-up insurance so the additional protection becomes permanent. This can be a cost-effective way of purchasing whole life insurance.

- ***Reduce the cost of your insurance:*** Use your dividends to reduce your premiums on the policy every year.

- ***Take as cash:*** You can, of course, take policy dividends in cash.

- ***Leave to accumulate:*** Leave dividends on deposit with the insurance company to earn interest or to be invested in an equity growth (segregated) fund. Returns on the latter are not guaranteed. Dividends left in the policy to accumulate can be withdrawn at any time and, on your death, accumulated dividends, unlike cash values, are <u>added</u> to the face amount payable to your beneficiary or estate. Interest earned on dividends left on deposit is subject to income tax.

- ***Premium offset:*** This concept, also called *premium offset,* is a combination of the premium reduction and the paid-up additions options. Typically, after premiums have been paid for a number of years, say, 10-15 years, future dividends are used to pay part of the premiums and the balance of the premiums is paid by surrendering some of the paid-up additions. Remember that policy dividends are not guaranteed and that projections about when your premium offset date will take effect may have to be adjusted if dividends are lower (or higher) than anticipated. This option could result in tax reporting to you as the policyholder, if cumulative dividends exceed cumulative premiums paid. Be sure to get a full explanation from your agent.

## 4 THE IMPORTANCE OF YOUR AGENT

Life insurance is a major financial commitment.

Just as you seek out expert advisors for other financial needs — bankers, stockbrokers, and the like — your choice of a life insurance agent is a key decision.

Your life insurance agent plays an important role in the financial planning process. He or she:

- Helps you assess your life insurance needs through a *financial needs analysis.*
- Arranges for the purchase of a policy.
- Provides on-going service, such as beneficiary changes, review and updating of life insurance policies.
- Assists the beneficiary in making the claim.
- Assists you with other financial planning needs (disability insurance, retirement planning, estate planning).

Agents are licensed and regulated by the provincial government to sell and service life insurance. They may also sell disability insurance, RRSPs, group insurance and segregated funds. Those who also sell mutual funds or other financial services like stocks or property and casualty insurance require a separate license. Not all agents handle every product.

Most agents are paid a commission by the insurance company issuing the product.

**DIFFERENT NAMES**

Some agents place business only with a single company; others (often called brokers) spread it around to other companies. One category is not necessarily better than the other.

Life insurance is sold by agents or brokers, and appropriately licensed financial planners and stock brokers. Here, we will simply use the term *agent.*

**CHECK OUT PROFESSIONAL QUALIFICATIONS**

Ask about professional qualifications and training the agent has had. Agents with a CLU (Chartered Life Underwriter) or CH.F.C. (Chartered Financial Consultant) demonstrate commitment to their professional development. These programs require several years of study and examinations.

## Selecting a Life Insurance Agent

As with seeking out any kind of professional advisor, ask for recommendations from someone you trust. If that's not possible, try the Yellow Pages. Phone two or three agents for a preliminary interview.

Don't be shy about shopping around for the best mix of advice and premium rates. Bear in mind that the lowest premium may not necessarily be the best buy for you; a policy that does not meet your needs is no bargain, no matter how low the cost.

Let each agent know your priorities. You are the buyer and the agent you choose will be working for you.

## WHAT TO FIND OUT ABOUT AN AGENT

■ How long has the agent been in business and what company or companies does he/she represent?

■ Does the agent belong to a professional association? *(See page 29.)* Has the agent qualified for professional accreditations?

■ Is the agent licensed in your province?

■ Will the agent provide references from other clients?

**Tip**

***What you're looking for in an agent is someone who is knowledgeable; understands your insurance needs and what you can afford; can explain your insurance options in plain language; and will continue to be a trusted advisor.***

## The Sales Interview

Once selected, an agent will sit down with you to discuss your financial goals. This is when frankness and trust must be established.

■ Be prepared to answer personal questions about your finances and family. Tell the agent what you need and what you can afford. **What you tell the agent is kept confidential.**

■ Don't accept only one solution to your life insurance needs. Avoid anyone who tries to sell you a particular plan and won't suggest alternatives.

■ Ask for proposals in writing (policy illustrations).

■ Watch out for any suggestion that you surrender your present policies. *(See pages 23-24 for more about "replacements".)*

■ Ask questions. This booklet helps you to frame questions, such as:

- What exactly is guaranteed in the policy and what is not — including premiums and benefits?
- Are any benefits from the policy subject to income tax?
- What post-sale service does the agent provide?

■ Once you've decided to purchase a policy, read the application form thoroughly before signing. Your signature authorizes the insurance company to confirm your medical history on a confidential basis. *(See pages 20-21 for more about safeguarding the privacy of personal information.)*

■ Tell the agent you expect delivery of the policy, usually within 30 days, at which time he/she should fully review the policy with you. If the policy is not what you thought you had bought, you can change your mind. *(See page 23.)*

## What You Should Know about Policy Illustrations

The policy illustration shows different cost-related features (cash values, dividends, death benefits, premiums) at various durations of the policy. Some of these features are not guaranteed (such as dividends) or may be tied to investment returns (such as some components of universal life policies). A policy illustration is just that — an illustration, designed to show you how the policy would work given a certain set of assumptions. If those assumptions change, the policy would perform differently. The illustration is not a legal document. Your policy contract is.

Questions to ask about the policy illustration:

- Are the premiums used in the illustration guaranteed? Could they fluctuate and under what circumstances?
- The illustration will probably show policy dividends (if applicable) at the level currently being paid by the insurance company. What would happen to the performance of your policy if dividends fell? If dividends rose?
- Is the death benefit guaranteed? If not, what factors is it tied to?
- If there is an investment component to the policy, what rate of return is assumed? What would happen to the performance of the policy if the rate of return were lower? If it were higher?

## Comparing Policies

Comparing the values of one policy with another can be difficult, especially given the different features and characteristics each may have. But here are some pointers should you decide to make comparisons:

- Comparing term policies is relatively straightforward, provided that the parameters are the same (e.g., $150,000 five-year renewable term insurance for a 37-year-old female non-smoker). Compare what the premium is today for each policy, but also add up what the premiums will be over a 20- or 30- year period. Renewal increases can vary significantly between policies.
- Use present value to calculate what all future premiums would cost in today's dollars. The computer software that many agents subscribe to can do this.
- Comparing permanent policies with other permanent policies is more difficult. Are the policies participating or non-participating? What features are guaranteed? What interest assumptions are made?

Once you make your decision to purchase a policy, you fill in an application to the insurance company.

The application asks for your name, age and other identifying information and spells out the amount and type of insurance policy for which you are applying, who you have named as beneficiary and how you wish to pay premiums. Typically, it also includes a health questionnaire.

The intent of the questions is to obtain information necessary to establish the nature of your risk and to issue the policy.

Your signature on the application authorizes the insurance company to contact your attending physicians and hospitals to confirm information, and to contact the Medical Information Bureau (*see page 21*).

The application is then sent to the insurance company's *underwriting* department, which reviews it for completeness, assesses the risk presented, and decides if the policy can be offered on the basis for which it has been applied.

The larger the amount of insurance applied for, the more extensive the information needed to assess risk. As indicated earlier, many factors, most commonly age, sex, condition of health, medical history, family medical history, financial situation, occupation and dangerous activities are taken into account before an application is approved.

**Tip**

***Be up-front when answering the questions on your application form. Life insurance is a "good faith" or "bona fide" contract and requires full disclosure by the applicant and insurer. Withholding or misrepresenting information could make your policy null and void.***

## Most Risks Are "Standard"

The insurer's objective is to issue a policy, not to turn away clients. About 96 per cent of applicants for life insurance receive the coverage they apply for and qualify for *standard* premium rates.

Every effort is also made to insure others who are higher risks. Many of those who because of, say, poor health or hazardous occupation, are likely to produce — as a group — a rate of mortality higher than normal, are offered life insurance as *substandard* or *special-class* risks. To reflect the higher risk, higher premiums may be charged, or other modifications may be made to the policy.

Only four per cent of those who apply for life insurance are declined.

Once a policy is issued at standard rates, the company cannot later charge a higher premium or add other restrictions because you have become a substandard risk.

If your policy is issued on a substandard basis and the cause for this no longer exists, the company will consider removing the extra premium or other modifications — if it is told about your change of situation.

## HEALTHIER LIFESTYLES REWARDED

A sign of our times is that non-smokers get life insurance at substantially lower rates than smokers. This reflects the lower risk they present. Usually, a declaration that one is a non-smoker when a policy is applied for and has been so for at least one year is sufficient to obtain the lower rates. Some companies also offer preferred rates if you meet additional indications of a healthy lifestyle (e.g., fitness, weight control, low or no alcohol consumption).

## When a Medical Is Required

Each insurance company sets its own rules for confirming the information supplied in the application and the health questionnaire. Requirements typically vary according to age and the amount of insurance. The older you are, the more likely that health information will be confirmed, for example, by a statement from your personal physician or by a medical or paramedical examination. To illustrate, a company might stipulate that no medical is required for up to $200,000 of coverage up to age 35. But for those in the 46-50 age group, a medical could be required at $50,000 coverage. Such confirmation might be required for lower amounts if the available information is incomplete or indicates a possible problem. These are illustrations only. Your agent can explain the requirements more fully.

For large amounts of life insurance or where an unfavourable health history is involved, the company may request other evidence such as an electrocardiogram or other test.

## Privacy of Personal Information

- **Life insurance companies recognize the importance of protecting the confidentiality of the personal information they obtain. All employees of insurance companies, agents, brokers, or anyone else acting for an insurance company, must comply with strict privacy rules.**

- The consent of the individual is the bottom line. Most personal information is obtained directly from the individual who applies for a policy. If information is required from any other source, the individual concerned will be notified, and his or her written authorization will be obtained whenever possible. And no information will be used for any other purpose or disclosed to any other party without the individual's consent, unless required by law.

- If you want to know what personal information an insurance company has in its records about you, you can, with proper identification, write to the company and request it. A fee may be charged to cover the administrative costs. Medical information may be released to you only through your personal physician. Also, you may correct what you believe to be erroneous personal information.

- If you do have a concern or complaint, each insurance company has an officer to handle enquiries and complaints regarding personal information.

## Medical Information Bureau (MIB)

This is a non-profit association, with a membership of about 750 life insurance companies, formed almost 100 years ago for the confidential exchange among its members of factual underwriting information. Its sole purpose is to serve as an alert against fraud or misrepresentation. When you sign an application, you authorize the insurance company to contact the MIB.

Where the applicant has a condition significant to health or longevity, the insurance company provides the MIB with a brief, coded report. These reports are mostly of a medical nature, but other factors such as an adverse driving record or participation in hazardous sports are also taken into account. This information will only be disclosed to another MIB member to which the individual has applied for insurance. An insurance company may not decline an applicant because of the information obtained from the MIB but can use the report as a basis to request further information.

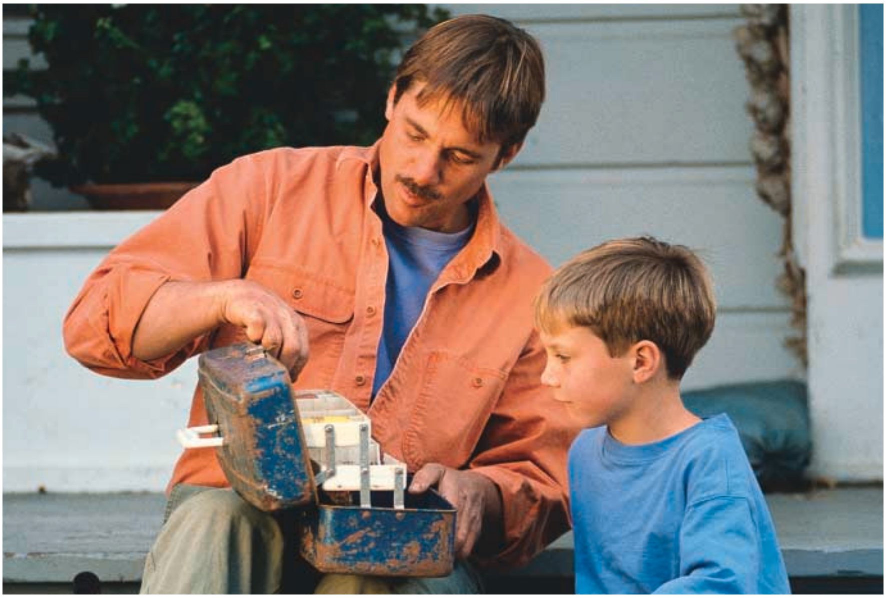
Confidentiality is closely safeguarded.

**Tip**

***Not everyone who applies for life insurance has a file with the MIB. In fact, only about one in 10 does. If you want to see if the MIB has a file on you and to verify the information, you can contact:***
***The Medical Information Bureau,***
***330 University Avenue, Ste. 501***
***Toronto, Ontario M5G 1R7***
***[416] 597-0590***

## What If There's an Error in My Application?

Failure to provide accurate and complete personal information could invalidate your insurance coverage. Occasionally, an applicant may discover that a fact has been omitted or innocently misrepresented on the application. In that case, the insurance company should be notified immediately so that any necessary adjustment can be made. If such errors are discovered when a claim is submitted, the company's action will depend on the nature of the misinformation. For example, if the age has been reported incorrectly, the insurance



company will usually adjust the benefits accordingly and pay the claim. However, if smoking status or other vital information has been misrepresented, the insurer may deny the claim and pay only a refund of premiums.

By law, a life insurance policy, including the application, is *incontestable* after two years. After that time, **except for fraud**, a company cannot deny a claim because the information you provided was incorrect or incomplete. *(For more information, see page 28.)*

## Before Final Approval: The Conditional or Temporary Insurance Agreement

If you pay the first premium with your application, the agent usually provides you with a **conditional** or **temporary insurance agreement.** This gives you interim life insurance, under certain conditions as outlined in the agreement, during the time it takes the insurance company to review your application. Sometimes, the interim coverage takes effect immediately and other times, it doesn't take effect until all evidence requirements have been met. Check with your agent.

**Tip**

***Keep your insurance policy with your financial papers. It's a good idea to keep a photocopy of the front page of the policy, along with your agent's name and number, in your safety deposit box, if you have one. Give your beneficiary(ies) a photocopy, too, and let them know where you keep your policy.***

## If You Change Your Mind, After All — the 10-Day Free Look

There is a "satisfaction-or-your-money-back" guarantee on most life insurance policies. It's called a *rescission right.*

Exactly as stated, you merely return your policy to the insurance company within *10 days of receiving* it. Premiums paid will be refunded.

If your policy has been in force for a long time before you receive the policy, say, a couple of years, an insurance company might turn down your request to rescind the policy. This is because you have been covered and the company would have paid a claim if you had died during that period. So, make sure your policy is delivered soon after you buy, and that you review it promptly.

## What about Replacing Policies?

At some point you may decide, or someone may urge you, to consider replacing your existing life insurance policies.

One key piece of advice: **Proceed with caution.** Certainly, there are some occasions when a replacement is in your best interests. And just as certainly, there are occasions when it is not. Think through the reasons for wanting to make a change. Review your needs and objectives and what different policies can do for you. Remember that it may be possible to alter your existing policies to meet your current needs at lower cost. Here are some tips to help you decide what's in *your best interests.*

### SHOULD YOU REPLACE A POLICY? SOME CONSIDERATIONS

1. Have a clear picture of your insurance needs and objectives. Work through an updated financial needs analysis. Consider the budget you have to meet those needs.
2. Review your current policy. If it no longer fulfills your needs, could it be altered to do so? If you have dividend options in an existing permanent insurance policy, can you use them to increase coverage? Don't hesitate to ask your existing agent or insurance company for help with this review.
3. Be aware of the pros and cons of both your current and proposed policies:
   - Do you fully understand the values of your current policy (guaranteed values, accumulated dividends, future values)?
   - Are you losing tax advantages or creating a tax liability if you change plans?
   - What are the cost implications of being older today or perhaps not in the same health as when you took out the policies? What evidence of insurability is required on a new policy?

- Are there circumstances where your new policy does not pay benefits (e.g., a new two-year suicide provision)? *(See page 28 .)*
- If the new policy is term, is it guaranteed renewable and convertible to another type of policy without evidence of insurability?
- Are premiums guaranteed? If not, when would they increase? What is the maximum level to which they could rise?

4. What are the professional qualifications of the agent(s) involved? What level of service and commitment can you rely on? Will the agent get a commission on the new policy?
5. If you decide to go ahead with a replacement, the agent recommending the replacement must complete a *Life Insurance Disclosure Form.* It's intended to help make you fully aware of the pros and cons of both policies. This form must be properly and fully completed. Read it carefully before signing.

**Tip**

***Make sure that the new policy is issued and in force and that you review it carefully before you request termination of your old policy. Termination requires a written request from you. The Life Insurance Disclosure Form cannot be used for this purpose.***

# 7 TODAY'S WORLD — TODAY'S NEEDS

## Self-employment: Businesses Small and Large

Self-employed individuals have a need to protect their stake in their businesses. This means liability and disability insurance, group insurance for employees, and life insurance for themselves and their key people. Here's how life insurance can be used:

- As collateral for a business loan, sometimes at the request of the financial institution making the loan. If it is necessary to assign the policy as security, a portion of the premium is deductible as a business expense.
- To fund a buy-sell agreement, and to provide surviving partners or shareholders with the cash to buy out the deceased's share and to keep the business going.
- To insure the key people in the company. Life insurance is often used as a safeguard against financial loss to the firm caused by the death of the owner, a partner or a key employee.

- To provide protection to the business person's family against the debts of the company. Unless the company is set up as a limited company, the individual (and his or her estate) assumes full personal responsibility for the business debts.

## Protecting Your Debts: Creditors Group Insurance

Did you know that your mortgage or car loan may become fully payable upon your death?

*Creditors group insurance* offered through lending institutions and car dealers repays the loan in the event of your death and sometimes disability. At the time of a major credit purchase, you may be advised of this option.

Before you sign, be aware of any restrictions or exclusions. Some policies may not pay a claim if it's related to a pre-existing condition or suicide. There may be age limits.

Also, check to see if your existing life, accident, disability or sickness insurance is sufficient to pay off your debts, or could be increased to do so.

## Using Your Networks: Association Insurance

Downsizing, contracting-out, self-employment — signs of the times that mean some people no longer have group insurance at their place of work.

Here's a suggestion: Don't overlook your memberships in professional associations, clubs, alumni groups, unions, lodges or other affinity groups.

Find out if you can obtain life, health and disability insurance through a blanket group plan (association insurance) that covers members.

Such plans can be a cost-efficient way of augmenting your existing insurance coverage. But be aware that they can also be changed or discontinued by the sponsoring group.

## Older? Insurance Can Be Found

There may be times when older people see a special need for extra life insurance. If you are in good health, you can obtain life insurance at premiums that reflect your present age.

But what happens if you are not insurable?

A few life insurance companies offer *guaranteed issue* plans — that is, life insurance policies that are issued with no medical questions asked. Typically, up to $25,000 will be issued to those between ages 50 and 75.

Be aware that restrictions apply if death occurs within the first two or three years of taking out the policy. Read the contract.

**The Consumer Assistance Centre can supply the names of the companies that provide guaranteed issue products.**

## Living Benefits

Many people suffering from a lengthy and terminal illness, such as AIDS or cancer, find themselves financially strapped to cover the growing expenses of care and infirmity, especially if they do not have adequate disability insurance.

Life insurance companies have responded to this need by making it

possible for the terminally ill to receive a partial pre-payment (called *living benefits* or *accelerated benefits*) of the death benefit from their existing life insurance policies.

Guidelines vary from company to company, but, typically, a percentage of the death benefit up to a certain limit is allowed.

A claim must be accompanied by medical documentation that the life insured is terminally ill. Sometimes a release from the beneficiary acknowledging the pre-payment is also required since it will reduce the amount he or she gets.

**Tip**

***Information about living benefits may be obtained from your agent or insurance company.***

## Life Insurance on Children

The primary reason for life insurance is to provide income to those who would suffer financially from the life insured's death. That means having insurance on the breadwinner(s) is the priority. It is unusual for a child to be an important source of family income.

Some parents arrange to have a small amount (e.g., $5,000) of insurance on each child through a rider on their personal insurance or by taking dependent insurance through their group insurance at work.

Other parents choose to take out a separate policy insuring the child. It gives the child a head start, at low premiums, on what will be one of the cornerstones of his or her financial portfolio as an adult.

And if the policy has a guaranteed insurability rider, the child will be able to purchase additional insurance in the future, regardless of disability or illness.

# 8 WHAT IT'S ALL ABOUT: PAYMENT OF THE CLAIM

It is the responsibility of the beneficiary or his/her representative to set the wheels in motion to file a claim.

**Tip**

***If the policy is individually owned, contact the agent, who can assist you with the claim. The company branch office or head office can also help.***

***If the insurance is through a group, such as an employer or union, contact the group benefits administrator.***

## What Documentation Is Needed?

In most cases, a claimant's statement on a form provided by the insurance company, and proof of death, doctor's statement or death certificate are all that's required.

## How Long Does It Take?

Life insurance companies are dedicated to considerate and prompt payment of death claims. Efforts are continually made to speed up the process. Payment can usually be expected within a week to 10 days of presenting the insurance company with full documentation.

However, there are some circumstances that can slow down the process (e.g., if the cause of death requires investigation, or if death occurs within the "contestable" period).

## What Does "Contestable" Mean?

It means that the insurance company has the legal right, during the first two years of the policy, to contest its validity on the grounds that information material to the risk has been held back or misrepresented. If it has been, the policy can be voided and premiums returned.

If there is a death during this two-year period, there may be inquiries that could result in a delay in the payment of the claim, or even in its denial.

After the policy is in force for two years, the company cannot contest it except in the case of fraud, that is, a deliberate misstatement of fact. An example of fraud is a smoker who declares himself/herself as a non-smoker in order to get a reduced premium.

## What Exclusions Might Apply?

Individual policies normally contain a two-year suicide clause. If death is due to suicide and occurs within two years of taking out the policy, the claim is not paid. If a suicide occurs after the two-year period, the claim is paid.

Group insurance plans pay for suicide deaths. Creditors insurance may not.

Your policy may also contain clauses that exclude claims or limit coverage for other reasons, for example, where death results from an act of war or from terrorism.

## Is There a Time Limit To File a Claim?

Yes. This is stated in the policy and normally ranges from 90 days to 12 months. Claims filed after that may be considered, depending on the circumstances and the insurer's ability to confirm the coverage.

## Is Interest Paid on a Claim?

Yes. Most companies pay interest from the date of death. The rate of interest is consistent with the rate of interest paid on policy proceeds left on deposit with the company. This interest is taxable.

## How Are the Benefits Paid?

Most beneficiaries choose to receive the life insurance proceeds in a lump sum. But depending on the contract, there may be other *settlement options* available.

These include taking the money as a life income in regular payments, or leaving the money on deposit with the company and collecting the interest.

## Are the Benefits Taxable?

**As a rule, the death benefit of a life insurance policy is not taxable.**

For assistance with your life insurance needs (purchasing or altering a policy, making beneficiary changes, or making a claim), contact your agent or the branch office of the insurance company.

If you are dissatisfied with a product or service, there are several steps you can take:

- Talk it over with your agent, the branch/agency manager, or the policyholder service department at the company's head office or regional office. Many companies have toll-free numbers.

- If you believe there has been a breach of ethics, contact the agent's professional association:

  Advocis
  350 Bloor Street East
  2nd Floor
  Toronto, Ontario M4W 3W8

  Independent Financial
  Brokers of Canada (IFBC)
  4284 Village Centre Court
  Suite 200
  Mississauga, Ontario L4Z 1S2

  Autorité des marchés financiers
  Place de la Cité, tour Cominor
  2640, boulevard Laurier
  bureau 400
  Sainte-Foy (Québec) G1V 5C1

- Or, you may wish to register a complaint with the Superintendent of Insurance in your province who is responsible for the licensing of agents and consumer issues. In some provinces, that office may refer you to the provincial Insurance Council, which governs agents' licensing and conduct.

## Contact the Consumer Assistance Centre

The **Consumer Assistance Centre** is a non-profit, non-sales help-line in English and French that has operated since 1973. It has been a source of information and assistance to more than 1,130,000 Canadians.

A wide range of services are offered:

- information about life and health insurance products and services, company addresses and phone numbers;

- copies of publications on disability, health and travel insurance and financial and retirement planning issues;

- help in locating misplaced insurance coverage; and

- information about Assuris.

**Call the CAC free of charge from anywhere in Canada: 1-800-268-8099. In Toronto: 416-777-2344.**

Or access CAC services through the Internet at the Canadian Life and Health Insurance OmbudService website: **www.clhio.ca.**

You can also write to the CAC:
Consumer Assistance Centre
20 Toronto Street, Suite 710
Toronto, Ontario
M5C 2B8

**Si vous désirez obtenir de plus amples renseignements en français, téléphonez sans frais au Centre d'assistance aux consommateurs en composant le 1-800-361-8070.**
**À Montréal : 514-845-6173.**

# INDEX

This work sheet will help you to estimate how much your estate would be worth if you were to die today, what income flow it can generate and what other sources of income are available to your survivors.

## (A) Estimating the Income-Producing Assets of Your Estate

**ASSETS**

*Add*

| | | | |
|---|---|---|---|
| Life insurance (including employer-provided) | ________ | | |
| Savings, cash | ________ | | |
| Investments | ________ | | |
| RRSPs | ________ | | |
| Other | ________ | | |
| **Total** | | ________ | (1) |

**LIABILITIES**

*Add*

| | | | |
|---|---|---|---|
| Final expenses | ________ | | |
| Outstanding uninsured debts (mortgages if not insured, credit card balances, income taxes, etc.) | ________ | | |
| **Total** | | ________ | (2) |
| *Subtract* Liabilities from Assets | | ________ | (A) |

## (B) Determining Income Needs

| | | | |
|---|---|---|---|
| Monthly income needs | | ________ | (3) |
| Available income | | | |
| From estate (multiply A by 0.00225, see note below) | ________ | | |
| From C/QPP or other pension | ________ | | |
| From employment | ________ | | |
| Other | ________ | | |
| **Total** | | ________ | (4) |
| *Find difference* between (3) and (4). If income needs exceed available income, proceed to Step (C). | | ________ | (B) |

## (C) Calculating Capital Needs

| | | | |
|---|---|---|---|
| *Multiply* monthly income shortfall (B) by 12 to determine annual shortfall. | | ________ | (5) |
| *Divide* (5) by assumed net after-tax interest rate (e.g., 2.7 per cent), as in Step (B) to determine **Additional Capital Required** to meet your survivors' income needs. | | ________ | (C) |

**Note:** As an illustration, assume that the income-producing assets of your estate could earn a gross return of 4.5 per cent a year. This equates to a net after-tax annual interest rate of approximately 2.7 per cent. Using this assumed net interest rate, each $1,000 in your estate will provide an income of approximately $27 a year, or $2.25 a month.

The income earned will rise and fall with interest rates, and will be affected by your actual tax rate.

## What is Assuris and How Does It Protect the Consumer?

Assuris is a not-for-profit organization that protects Canadian policyholders in the event that their life insurance company becomes insolvent. Its role is to protect policyholders by minimizing loss of benefits and assuring a quick transfer of their policies to a solvent company where their benefits will continue to be honoured. Assuris is funded by the life insurance industry and endorsed by government.

If an insolvency of a member company does occur, Assuris guarantees that policyholders will recover at least 85% of their promised benefits under a variety of products issued by life insurance companies in Canada. Assuris also provides 100% protection when benefits are below the dollar values listed below.

- Monthly income of $2,000
- Health expense of $60,000
- Death benefits of $200,000
- Cash values of $60,000

Accumulated value benefits (accumulation annuities, side funds of universal life policies, premium or dividend deposit accounts attached to a life insurance policy) are 100% protected by Assuris up to $100,000.

For more information contact the Consumer Assistance Centre at 1-800-268-8099 or see the Assuris website at www.assuris.ca.

## What Is the Role of Government Regulators?

Most life and health insurance companies that operate in Canada are regulated for solvency by the federal government through the Office of the Superintendent of Financial Institutions. The Inspector General of Financial Institutions performs the same functions for companies incorporated in Quebec.

These regulators inspect companies to assess their safety and soundness. In addition, the companies must submit annual financial statements to the regulators.

Provincial government agencies regulate the licencing and conduct of agents, contractual matters and issues relating to consumer service or complaints.

## How Do I Choose an Insurance Company?

If you belong to a group plan that provides life coverage, the group sponsor (typically an employer, union or association) chooses your insurer.

If you decide to buy individual life coverage, there are many sources of information about companies that offer it. Rating agency reports, articles from the business press and annual reports from the companies themselves—available at public libraries or on the Internet—can all provide useful insights. Your agent or broker also can be an excellent source of information about a company. References from family members, friends and trusted advisors are probably the best basis for making a decision, though.

This booklet is published by the **Canadian Life and Health Insurance Association Inc. (CLHIA).** The CLHIA is a national trade association that represents the collective interests of its member life and health insurers, which together account for 99 per cent of Canada's life and health insurance business.

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Canadian Life
and Health Insurance
Association Inc.

Association canadienne
des compagnies d'assurances
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