Financial protection for you and your family

Introduction

Public surveys show that what matters most to people is their family. When it comes to the crunch, it's family we first think of, family we worry about and family that gives us most happiness. The desire to shelter those nearest to us is fundamental.

The best way to ensure financial protection is to be a long-lived high earner or by inheriting or winning a large cash sum. But apart from eating up our greens and not going hang-gliding there is not a huge amount we can do to avoid an untimely death.

Even if we cannot greatly influence the cards that nature dealt us at birth – our genes – we can at least provide for those we leave behind.

This is where life assurance and other protection policies come in. The policyholder pays a regular or single premium and in the event of the insured's death, his or her family gets a cash amount, generally many times the amount paid in premiums.

Because life assurance has been around so long, and because everyone should have some level of financial protection, more than 100 companies provide life assurance and protection policies. This makes for a competitive market which can only benefit consumers.

However, there are also many refinements on basic life cover, which provides a guaranteed death benefit if a claim occurs during the period of insurance. Life assurance can be set up for a specified period of time (term assurance) or for the whole of the insured's life (whole of life assurance). There are many other protection policies designed to protect the insured and his or her family against other life events, such as illness, accident, disablement, redundancy and long-term unemployment.

Spoilt for choice

The abundance of choice may seem like a mixed blessing. With so many options, making a decision could seem overwhelming. For a straightforward life assurance policy, you can try one of the web-based financial advice services that claims to come up with the best deal. You can find the services through an Internet search. You fill in details, such as age, medical details, gender, occupation, smoker/non-smoker and how much you want to insure your life for or somebody elses (if you have what is known as 'insurable interest' on their life). Hit 'Enter' and you know how much your premiums will be.

However, buying life assurance is not to be done without serious reflection. Lots of factors need to be taken into consideration such as – what is the right level of cover and for how long should it last? It’s really worthwhile to discuss these questions with an Independent Financial Adviser (IFA).

An IFA might well suggest, for instance, that instead of going for just a straightforward life assurance policy, you also take out a different type of protection product.

The other forms of financial protection
Simply having life assurance may not be enough. What, for instance, if you contract a near fatal disease or illness? Cancer, stroke and heart disease are the greatest risks. You may not be able to work and so lose your income; but you are still alive so your life assurance does not pay out. And to compound the problem, you may need expensive nursing care or to adapt your home, or even move house.

Except for the very elderly, it is more likely that an individual will be diagnosed as having a critical illness than that they will die in the short term. As a result a critical illness policy is more expensive than comparable life assurance. It is the type of protection policy you hope you never need to claim on, but if you do, the benefits can be a financial lifesaver.

Permanent health insurance, known as income protection makes up income lost through illness, accident or disability. Rates vary according to the dangers associated with one’s job, age, state of health and gender but PHI is thought to be of particular value to the self employed who do not have an employer to continue paying their salary if they are unable to work.

Critical illness insurance, a critical illness policy pays out a lump sum if you are diagnosed with one of a number of specified 'critical' illnesses during the term of the policy. Many life insurance companies offer policies that cover you for both death and critical illness and will pay out the guaranteed benefit on the first event to happen.

Loan protection insurance covers the policyholder if they lose their income, through illness or accident. This type of policy will help with some or all loan repayments.

Mortgage payment protection insurance is set up with a term specifically matching your mortgage term – say 25 years. The policyholder is covered for the term for the amount of their mortgage repayments as long as they keep on paying the premiums.

You need to read the small print before buying any protection policy as there will be exclusions, such as self inflicted injury or dangerous sports. An IFA can point out and explain the small print of each type of policy.

There is a further choice of protection policies that can be used to protect your income and the financial cost of any loan, mortgage or other financial commitment you may have.

Accident Sickness and Unemployment (ASU) can be taken out for any purpose to protect your income and to give you peace of mind. The benefits normally only pay for one year on a valid claim if you have an accident, are ill or become unemployed.

Most of these protection policies operate a 'deferred period' which is the period from when an event happens, that you can claim for, to when the policy starts paying out. You need to check the policy wordings carefully to ensure the policy matches your financial protection needs.

Private medical insurance can cover you for private medical treatment and you can choose to add on extra cover, such as dental cover. You may select the hospitals that you would want to be treated in close to home. As always the more benefits and the more comprehensive policy you select the more it will cost.

Long-term care insurance is designed to cover you against the cost of nursing-home care in your old age and you can pay for it as a lump sum or in regular payments.

Life assurance add-ons.
Rather than assessing the need for one or more of the range of policies, some of which overlap, you can add extras to life assurance policies. This may prove more economical – again an IFA can help you to work out the maths. Extras include critical illness cover and "waiver of premium". This means that if you cannot do your usual job because of illness or injury, the insurance provider pays the premiums to keep up your benefits until you recover. You may already have some life insurance or protection offered by your employer, so it is worth checking.

Life assurance as a form of savings
A variation is to use life insurance as a form of saving. You decide for how long you want to save and this often takes you to when your interest only mortgage needs to be repaid. At the end of the term you should receive a cash sum based on investment growth.
At the same time, if you die before the end of the term, the policy will pay out a guaranteed death benefit. These plans, known as endowments, can be issued on a with-profits or unit-linked basis.

With profits or unit linked?
If you invest in a with profits life assurance policy your premiums are pooled in a fund that has a wide spread of investments such as shares, bonds, property, gilts and cash. You may receive regular bonuses and a final bonus. Once they are

added regular bonuses cannot be taken away. The final or terminal bonus, which you could possibly receive at the end of the term, depends on the health of the fund and there is an element of doubt as to how much you will get. That risk has been highlighted by endowments taken out to repay mortgages. Millions of homeowners who expected their endowments to cover their outstanding mortgage have been disappointed.

This misfortune resulted from investment growth assumptions being too high when the endowments were taken out. As a result, endowment backed mortgages are not as popular as they were previously.

If you already have an endowment or wish to invest in one, an IFA will be able to advice you on the financial strength of the provider (which is important) and whether the endowment is appropriate for your circumstances.

Another choice – life assurance bonds.

If you have ready cash, for instance from an inheritance, you can use it to invest in life assurance bonds. Single-premium life assurance bonds vary and can be unit linked or with profits. So, again an IFA will be able to help you pick the funds that are best placed to benefit you.

If you choose a **unit-linked** life assurance policy, you can choose what you want to invest in. The choice of funds is diverse – from cash funds to emerging markets. The price of units in unit-linked funds will go down as well as up so you really need to talk to an IFA who understands your investment risk tolerance.

Particularly for life assurance bonds and endowments there is no guarantee that you will get your money back when you cash in and it is important to remember that past performance is no indication of future performance.

Tax

Generally, whole-of-life assurance policies and term assurance policies are free of personal tax if you continue to pay the premiums for the stated period. It’s a great advantage. But you must check that your policy remains free of personal tax if you wish to change it. For instance, if you surrender early (except in the event of death) you may be liable for tax.

Life assurance products can be tax efficient in other ways, for example, if a single premium life assurance bond is put in trust for the future benefit of nominated beneficiaries, in the event of a claim the benefits are outside of the deceased’s estate and therefore free of inheritance tax. This is of particular use to anyone with an estate over the Inheritance Tax threshold of £312,000 (2008/2009) who wants his or her heirs to mitigate their inheritance tax liability.

What to watch out for

The personal finance pages of newspapers are full of warnings such as 'Think before you act…such and such is a long-term investment.' Such guidance applies to life insurance and other protection products. For endowments and life assurance bonds there is no guarantee that you will get your money back. For other protection policies there may not be a cash value at anytime.

That's why it's so important to plan ahead, receive unbiased advice and consider carefully all your financial options.

"Cooling off" period

If you buy life insurance when you have received advice then change your mind and would like to pull out of the purchase you have two weeks, or longer, to do so without loss. This cooling-off period is your statutory right. It is part of a raft of consumer protection laws.

How do you make the right choices?

It's clear that choosing the right mix of financial protection is not simple, particularly when there are so many providers and products. Among the decisions you need to make are:

- how much cover should I have?
- for a specified term or for the whole of the insured's life?
- which protection policies should I have?
- which fund is most suitable?
- which provider is the most appropriate?
- do I need critical illness cover and/or income protection?

Advice from an IFA should help with all these questions. Even the first question – how much cover should I have? – is not that easy to calculate. Factors such as the age of children, who is the breadwinner of the family, how long the benefits need to be paid for and what level of cover are relevant. IFAs are used to doing the sums, they have sat exams that test that they do it properly. You can also expect an IFA to tell you about the relative strengths of a provider and how quickly they deal with claims. They will also help you with your application form which, once complete, will be sent to an underwriter at a product provider who will set your premiums.

An IFA can deal with over 100 life assurance and protection providers and will recommend the most suitable for you.

For further information on the subject contained in this guide, please contact Inshore IFA.

We can help for advice or further information please call **01425 282181** or email us at **info@inshoreifa.com.**

April 2008