



## **LIFE INSURANCE**



The information provided in this document is meant for the sole use of Active Duty service members, retirees, their families, and those individuals eligible for legal assistance. The information is general in nature and meant only to provide a brief overview of various legal matters. Rights and responsibilities vary widely according to the particular set of circumstances in each case. Laws can vary across states, services, and civilian jurisdictions and laws are changed from time to time. Do not rely upon the general restatements of background information presented here without discussing your specific situation with a legal professional.

Life insurance is an important tool for providing financial security for your family members. Through life insurance, you can create an immediate estate of sufficient size to assure adequate income for your family members upon your death. In determining your life insurance needs, consider the desired monthly income you would like your survivors to have, as well as the various military benefits available for military survivors, including the Survivor Benefit Plan and Social Security.

There are basically two types of life insurance: term insurance and cash value insurance. Term insurance provides pure protection for a stated term of years and does not build any cash value. Premiums paid provide insurance coverage for the term only. For example, if you have a 1 year term policy and you die 9 months from the date the policy was issued – you are covered; if you die 1 year and 1 day from the issue date – you are not covered. Premiums generally increase as you age, although you can purchase level term policy for a stated period (5, 10, 15, 20, 25 years). While your premium will not increase during the length of the term, the initial premium will be larger than a standard term policy but lower in later years. Generally, individual term insurance is an excellent vehicle to provide protection against premature death for a temporary or intermediate period of time.

Cash value insurance can be either whole life, universal life, or variable life – all provide for a guaranteed death benefit and build up cash value. Whole life insurance provides a guaranteed death benefit with premiums at a set rate for life up to age 95 or older. Whole life typically offers a fixed, progressive increase of cash value against which the insured may borrow, or which the insured may realize upon surrender of the policy, or use to pay the premiums on the insurance policy. Universal life is a combination of a renewable term policy and a cash accumulation account. The premium is first applied to the cost of term insurance to provide the death benefit, with the balance credited to a fund where it earns interest. Variable policies allow the client to allocate cash values among a number of investment choices, such as stocks, bonds, money market funds, or a combination thereof. Variable life usually requires the payment of fixed premiums with a death benefit at least equal to the policy's face amount.

If you own or retain control over the life insurance contract, the value of the proceeds paid upon your death will be included in your gross estate for estate tax purposes even though the proceeds are paid to a designated beneficiary. The proceeds received by the beneficiary are not considered income to the beneficiary and are not subject to federal or state income tax (although there may be a state inheritance tax).

Service members contemplating the purchase of commercial insurance should look closely to determine whether the policy has a "war clause." Such clauses typically allow insurance companies to avoid payment on a contract of insurance if the service member is killed in war or by a "military service hazard."

You have the right to name any person(s) you choose as the beneficiary(ies) of your life insurance policy(ies). You should review your life insurance policies regularly to ensure the persons you desire to receive your insurance benefits are named as beneficiaries. If you originally used the designation "by law" when you named the beneficiaries of your Servicemembers' Group Life Insurance (SGLI) policy, you should consider whether you may be better served by revising that form at your personnel office to



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specify the actual people you want to be your beneficiaries. Your legal assistance attorney can advise you on beneficiary designations, including a trust.

Low cost life insurance, Servicemember's Group Life Insurance (SGLI) with a benefit of up to \$400,000, is available for military members through payroll deduction.

The Veterans' Opportunities Act of 2001 extends life insurance coverage to family members for those members insured under the Family Servicemember's Group Life Insurance (FSGLI) program. Children are insured for \$10,000 each at no cost. SGLI coverage for spouses is automatic unless the servicemember declines coverage in writing; however, there is an increased cost for this insurance above what the member pays for his own SGLI coverage. Spousal coverage requires payment of a premium that is determined by the spouse's age and the amount of coverage selected.

Members may purchase up to \$100,000 of FSGLI coverage for a spouse, in increments of \$10,000. However, they will not be able to purchase more FSGLI coverage for a spouse than they have for themselves. Each dependent child will automatically be insured for \$10,000.

### **Frequently Asked Questions**

**Q: WHY WOULD I NEED LIFE INSURANCE?**

A: Life insurance has two major functions: 1) to replace the earning power of the breadwinner, and 2) to provide liquidity for an estate. You can use life insurance to provide financial security for your family members or to pay any estate tax that may be owed at your death.

**Q: HOW MUCH LIFE INSURANCE DO I NEED?**

A: That depends on many factors. Everyone's life insurance needs differ. You need to decide whether you need life insurance to provide for the financial security of your survivors or because your estate will be subject to estate taxes. If for financial security, then calculate how much income your survivors will need and determine if your assets (savings, investments, home equity, survivor benefits available for your survivor) are sufficient to cover the survivor's needs. If not, life insurance may fill the gap.

**Q: IS LIFE INSURANCE TAXED?**

A: Life insurance proceeds paid to your beneficiary are not subject to federal income tax. If you own the life insurance policy when you die, however, the proceeds are included in the value of your estate for estate tax purposes. You are generally considered an owner of a policy if you have the right to borrow against it, change the beneficiaries, or revoke, cancel, or assign the policy.

To remove the life insurance proceeds from your estate, you could have someone else, such as your beneficiary or a life insurance trust, own the policy. There are advantages and disadvantages to these alternatives that should be discussed with an attorney.

**Q: IF I AM TERMINALLY ILL MAY I SELL MY LIFE INSURANCE POLICY?**

A: Maybe, if your policy agreement allows it. Servicemembers' Group Life Insurance has an accelerated benefit option as do many commercial insurance policies. Accelerated benefits may be payable when an individual is diagnosed as terminally ill or chronically ill. The individual may receive the payments directly or may assign the life insurance contract's benefits to a viatical settlement provider. A viatical settlement provider is a person engaged in the trade or business of purchasing life insurance policies on the lives of terminally ill or chronically ill individuals if the person is licensed to buy life insurance



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policies under such circumstances. Generally, a terminally ill individual is an individual whom a physician has certified as having an illness or physical condition expected to result in death in 24 months or less. Generally, a chronically ill individual is one who cannot perform at least two activities of daily living (bathing, dressing, eating, etc.) for a period of at least 90 days.

### **Q: WHO SHOULD I NAME AS MY BENEFICIARY?**

A: The owner of a life insurance policy can name almost anyone as a beneficiary. Generally, the most common path for a married individual is to name his or her spouse as the beneficiary, with the children named as contingent beneficiaries. However, this may not be the best course of action if you have children from a prior relationship that you wish to benefit or if you want to take advantage of the federal estate tax exemption.

### **Q: WHAT HAPPENS IF I NAME MY CHILDREN AS MY BENEFICIARIES?**

A: If you name minor children as beneficiaries, you should consider using UTMA, UGMA or a trust to hold the proceeds until the child reaches majority or the age you specify in the trust document. In most cases, insurance companies will not pay life insurance proceeds to minor children, or incompetent individuals without the appointment of a legal guardian. Additionally, you should think carefully before naming specific children as beneficiaries if you might have or adopt additional children. If you name A, B, and C as beneficiaries and D is born, she will be left out. If the insurance proceeds are substantial, using a trust as beneficiary may offer advantages. Only a trust is flexible enough to meet changing circumstances and needs and only a trust can protect against a second estate tax when the primary beneficiary dies.

### **Q: I NAMED MY SPOUSE AS MY BENEFICIARY AND NOW WE'RE DIVORCED, SHE WON'T GET THE MONEY, WILL SHE?**

A: If the policy that names your former spouse as your beneficiary is under SGLI – then your former spouse will get the proceeds of the policy. For commercial insurance policies, whether the divorce will void the former spouse as your beneficiary election depends on state law. In most states, a divorce will void the designation of the former spouse as a beneficiary of an insurance policy. Even in those states, the best course of action is to execute a new beneficiary designation form removing your former spouse and substituting your new beneficiary. For SGLI, it is imperative that you execute another SGLV 8286 designating a new beneficiary.

How much, if any, life insurance you need depends on your personal situation. You should discuss your life insurance needs and beneficiary designations on life insurance policies with your legal assistance attorney.