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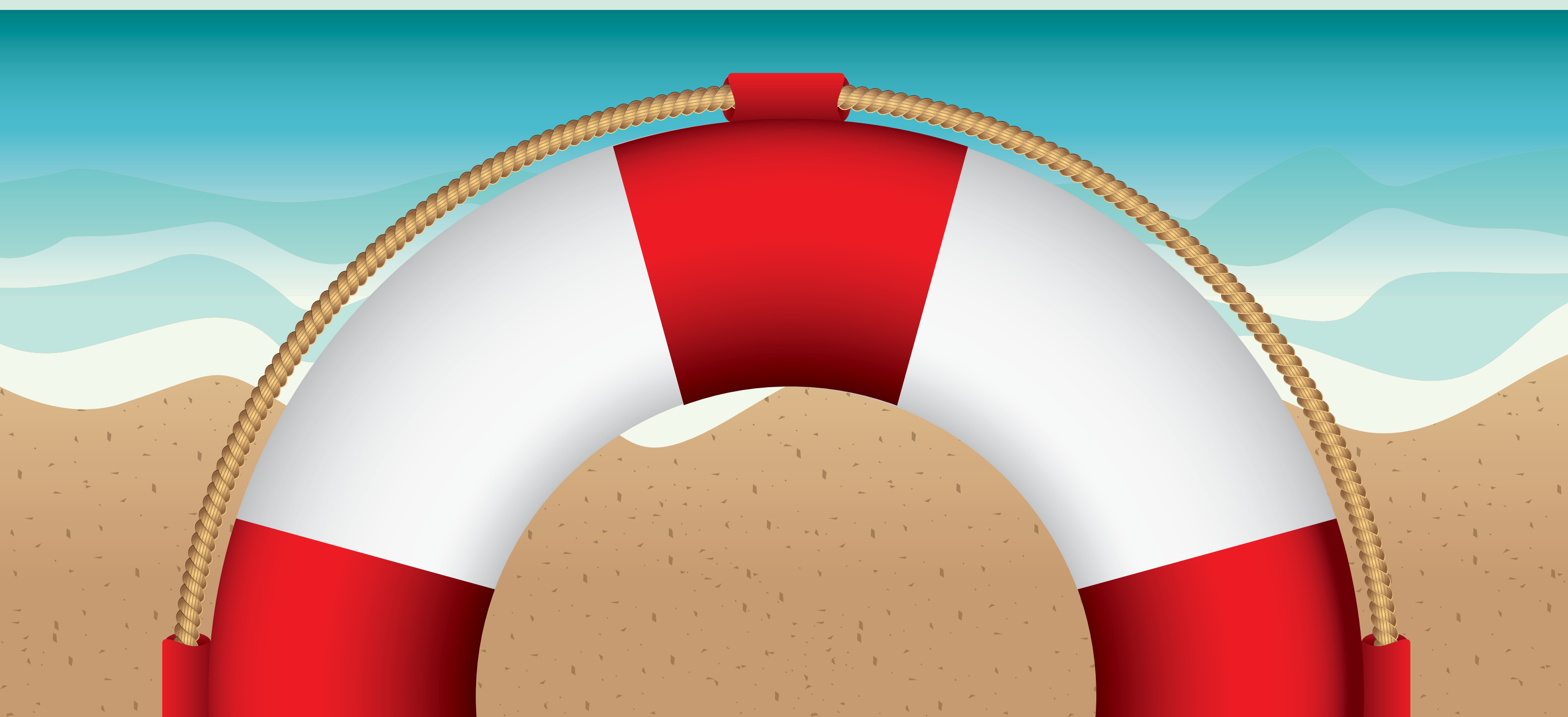
Term Insurance Buying Guide

Looking to secure your wife's and children's financial future? Read on



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CHAPTER 1

Introduction

Myth busted: You have life insurance but not term insurance. Term plans offer high cover at substantially lower premiums than other types of insurance.

The purpose of term insurance is to cover the financial aspect of risk. It is necessary for the breadwinner like a father or husband who has to take care of financial requirements of the wife, children and parents. The way to go about it is to calculate how much insurance cover you need and then buy a good term insurance of that amount that actually pays in the hour of need.

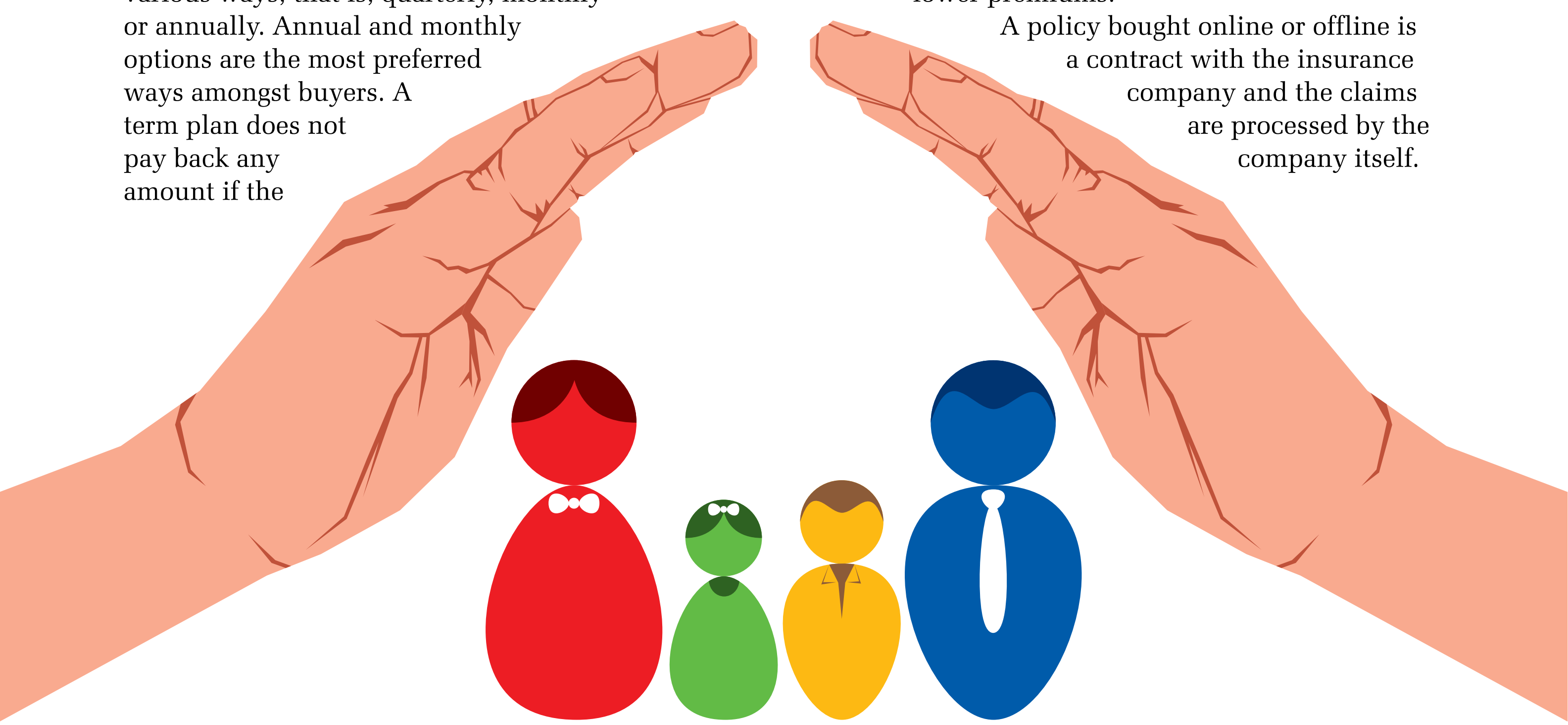
What is term insurance?

Term insurance is a basic and the simplest form of life insurance which pays the insurance amount known as Sum Assured to the beneficiary/nominee in case the insured dies. The insured has to pay a premium towards the policy which can be paid in various ways, that is, quarterly, monthly or annually. Annual and monthly options are the most preferred ways amongst buyers. A term plan does not pay back any amount if the insured survives through the tenure of the policy. Being the cheapest form of life insurance, term plans are able to offer a high insurance coverage at premiums substantially lower than other types of insurance.

How to buy a term plan online?

Buying online is a preferred way amongst buyers and we also recommend that one should buy a term plan directly from an insurance company's website. This makes it easy on pocket for the entire policy term. The online plans are cheaper than their offline counterparts as the insurance company does not have to pay any commissions to the agent, a benefit which they pass on to the consumers in the form of lower premiums.

A policy bought online or offline is a contract with the insurance company and the claims are processed by the company itself.



What is term insurance?

Claims are processed by the claims department of an insurance company.

Process to buy online

1. Go to insurance company's website. Select the online plan you wish to purchase.

2. The online portal will initially ask you to enter the personal details such as gender, your smoking habit, date of birth or age, policy term and amount of sum assured. On basis of these basic details the company calculates and give you a premium quote. If you are stuck somewhere, you may either call customer care number or take help of online agent through chat facility.

3. You need to fill other details such as employment details, health details, address along with nominee details required by the company and pay the premium through netbanking or other digital modes. Insurer provides you an option to e-verify your identity and address by simply providing Aadhaar number. This will allow insurer to process your application faster. Policy will be issued faster as no separate documentation is required for Address & Identity Proofs.

4. Companies give various provisions to submit the required documents. You can upload on their website, email or simply whatsapp it to them for faster processing.

Online term plans are cheaper and provide a longer Free-look period.

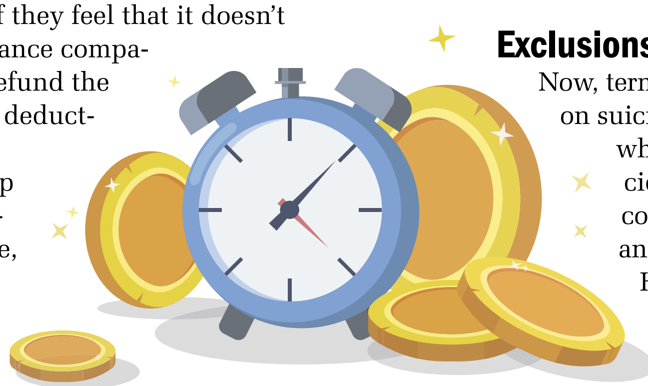
We recommend

- Calculate the required life cover using a detailed need analysis as mentioned in Chapter-4. However, as a thumb rule, it should be at least 10-12 times of your annual income. Also, do not round off the cover. Every penny of life cover is important.
- Go for the policy term till the time you will be earning. For example, till the age of 60 or 65 years.
- Annual premium turns out to be cheaper than monthly premium because of loading.
- Choose the payout option that best suits your requirement. Income payout option comes at lower premium.
- Smoking habits should be indicated correctly. Even if the applicant smokes only occasionally, he falls in the category of smokers. Most of the insurance companies consider you a non-smoker only if you haven't smoked at all in the last 5 years.
- Make full disclosures of any existing and previous medical conditions. If any material fact is not disclosed, the insurance company may repudiate any claim arising out of the insurance policy on the basis of non disclosure.
- Keep your PAN/AADHAAR handy while filling the form. Aadhar card alone is enough for age, identity and address proof.

Depending on your age, the insurance company may ask you to go through any medical tests as well.

Free-look period

This is the biggest advantage of buying online. Apart from online discounts on premiums, policy holders also get 30 days free-look period. A lot of policy-holders don't realize that they have the option of cancelling their online policy within first 30 days of its commencement if they feel that it doesn't suit them. The insurance company will be liable to refund the premiums paid after deducting the expenses incurred towards stamp duty, medical examination, etc. Therefore, make sure to study your policy document thoroughly during the free-look period.



Premium payment

It is extremely important to pay your renewal premiums on time to keep your policy in force. You should set reminders for premium payment or you may consider setting up standing instructions for premium payments on time. Missing a premium may lead to lapsation of the policy which is a risky affair and defeats the purpose of buying a term plan. Insurance companies provide a 15-30 days grace period to revive the policy in case you forget to pay the premium on or before the due date. If policyholder fails to pay the premium within the grace period, the policy shall lapse without any value.

Exclusions

Now, term polices provide insurance money on suicide after a year. However, if insured, whether sane or insane, commits suicide within one year from the date of commencement of policy, the insurance company forfeits death benefit. However, some insurance companies may reimburse the premiums paid till date after deducting expenses incurred by the company.

Tax deduction

Premiums paid towards term plans and critical illness rider are eligible for deduction under Section 80C and 80D of Income Tax Act 1961.

Steps to buy insurance online

Select a plan on insurer's website: A plan could be a plain vanilla term plan or a term plan with critical illness or accidental benefits.

Fill up the required information: Various companies have introduced new ways of filling the application form. It has now become much more easier to buy on mobile.

Upload documents: Photo, age proof, identity proof, address proof and income proof.

Pay premium online: Choose the option monthly/annually accroding to your budget and suitability.

CHAPTER 2

Do You Need Term Insurance?

You must adequately insure yourself if your demise will cause financial hardship to your loved ones.

Life insurance isn't needed for everyone at every stage of life. You do not need life insurance if you do not have any financial dependants. On the contrary, you must adequately insure yourself if your demise will cause financial hardship to someone - your parents, spouse or children.

Here's a broad framework to think about your insurance needs at different stages of life.

Single with no dependants

Do you need life insurance if you are single and have no dependants? The answer is no. If you have dependants such as aged parents then the situation is different and you can consider buying life insurance.

Life insurance need: None, except in case of dependants. You should consider buying it in the next one year.

Dual income with no kids

With double income and no dependants, sometimes you have more money than ways to spend it. Whatever the lifestyle, you do not ordinarily need life insurance unless there is a substantial inequality of earnings between the spouses or outstanding liabilities such as credit card bills, mortgages, and car loans.

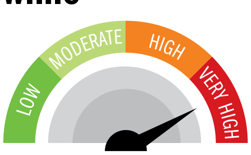
Life insurance need: Moderate, if there is a substantial inequality of income and/or outstanding liabilities. Buy it in the next three months.

Just married or have been married

Does your family consists of a breadwinner and a homemaker? Such a family usually depends on the sole breadwinner's income and is vulnerable to the loss of that income.

Life insurance need: Very high. You should consider buying it immediately.

Young parents or have been parent for a while



Mothers often take a break from work for periods ranging from a few months to several years. Sometimes this entails a complete change in role to that of a homemaker. This can result in the family being largely or wholly dependent on the earnings of the husband and hence vulnerable to a steep drop in those earnings. There's also the cost of raising a child - toys, books, schooling and yes the latest PlayStation - all of which go up with inflation.

Life insurance Need: Very high, to finance household expenses and child rearing including those ever rising school fees. Consider buying it immediately.

Second innings

Retirement - that time in life when you hang up your boots and watch the sun set. You take up the hobby you always wanted to pursue, move to a hill-station or just spoil your grandkids silly. At this juncture, you are typically living off a pension or your savings and you need to think of the immediate rather than the distant future. This is not the time to buy life insurance unless you have a spouse, children or grandchildren who are dependent on you financially. Also don't forget - the premium increases dramatically with age.

Life insurance Need: Moderate, if there are dependants.

Do you need term insurance if you are an SIP investor?

You should buy Term Insurance Plan (TIP) even before you start investing through a Systematic Investment Plan (SIP) if you have financial dependants.

The size of the term insurance cover should be decided carefully. It depends on many factors such as your annual income, your family's monthly expenditure, their goals and your age, and others. Read more on this in Chapter 4 where we explain how you should go about estimating your term cover. Here are two simple 'Rules of 10' to consider. One, for every 100 rupees of SIP, spend 10 rupees on the TIP. Two, ensure that the life insurance cover you get from your TIP is about 10 times of your annual income.

Let's look at a quick example. Say you have an annual income of ₹5 lakh and you do a monthly SIP of ₹5,000. According to the two Rules of 10, either your life insurance cover should be ₹50 lakh or your TIP should be ₹500 per month. Simple, isn't it?

If you are just married or have recently become a parent, you must buy term insurance today.

CHAPTER 3

Are You Buying the Right Term Insurance?

It is prudent to opt for a product that is fairly-priced, however one must remember that cheap does not mean the best.

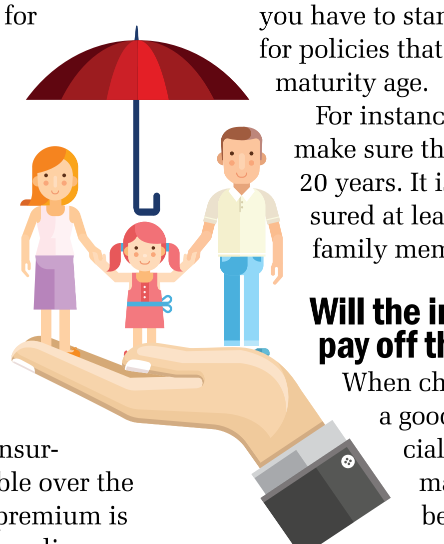
One must compare the price of policies from different insurers and their claim settlement ratio. Some policies give discounts on higher sum assured or charge a lesser premium from women. However, sometimes discounts can also be a marketing gimmick with the premiums for these policies weighing on higher side.

Is a cheap policy always good to select?

It is prudent to opt for a product that is fairly-priced, however one must remember that cheap does not mean the best. When you compare two insurance products, if all the features are more or less same, the price is the deciding factor. One must scan all term insurance plans and pick a policy that offers pure life insurance at a bargain. You may consider monthly premium payment option if paying in one go is difficult for you, but don't settle for a cheap plan if it doesn't meet your requirements.

Term insurance policies are associated with level premiums or increasing premiums depending on the type of policy and the insurance company. In term insurance policies the mortality risk of the insured increases year by year and therefore the cost of insurance also increases yearly. Consequently, the premium chargeable also increases annually. However, in many term policies the insurer averages out the premium chargeable over the entire policy period and the average premium is charged as a premium throughout the policy tenure. But some insurance companies may have a clause to revise the premium every 5 years.

There are a few companies which offer a flexibility of premium payment with monthly option. Some policyholders may find it more convenient. One must explore the options available to choose the most suitable one. Monthly premium options are generally costlier than annual premium option because of loading.



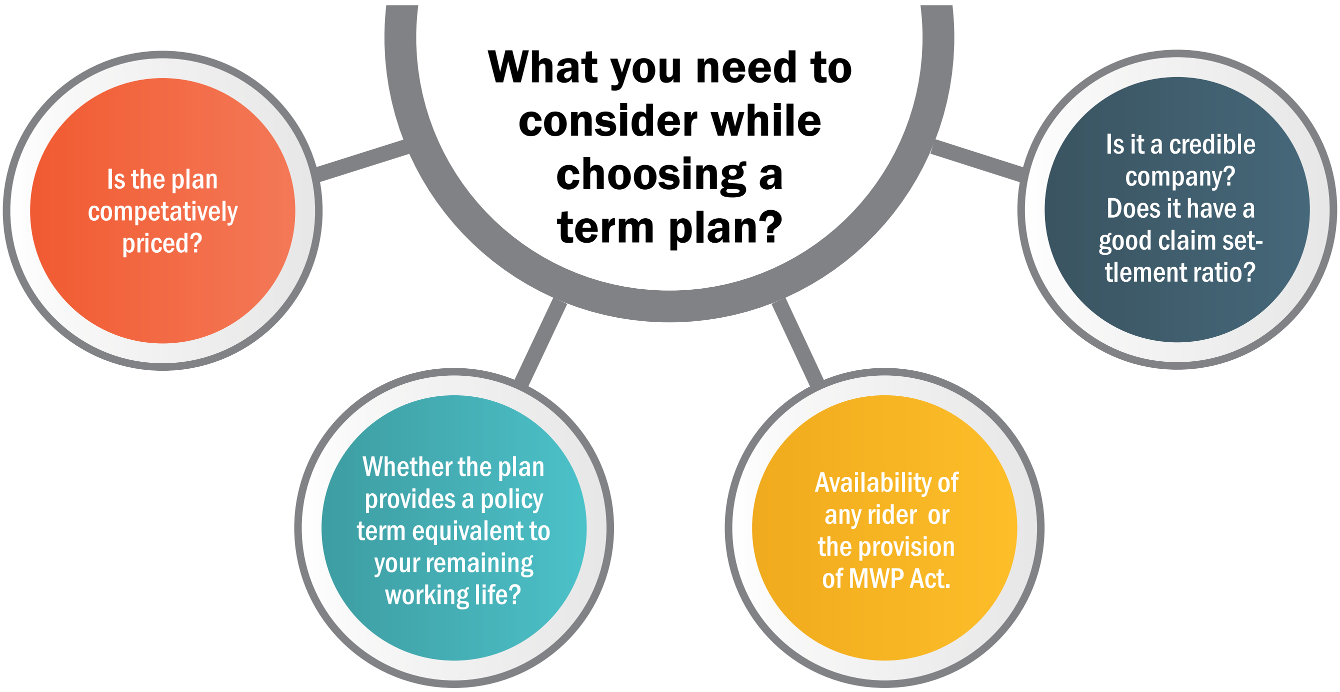
What should be the policy term?

Before buying any term insurance plan, an individual must assess time left to retire. Time remaining to retire here does not necessarily mean retirement from your job, it means the time period till your family members will depend on you for their financial needs. Once you know the number of years for which you have to stand as the financial support, look out for policies that offer the matching policy term and maturity age.

For instance if you plan to retire after 20 years, make sure that you take a minimum policy term of 20 years. It is fundamentally important to be insured at least till you pass on the baton to another family member.

Will the insurance company be there to pay off the claim?

When choosing a life insurance company it is a good idea to make sure that it has financial strength and longevity. You want to make sure that the company is going to be around later in life when you need them. The insurer you choose must



have the credibility and integrity to fulfil this promise.

Choose a plan that comes from highly credible company. Claim Settlement Ratio is a good way to look at the credibility of a company. Claims settlement ratio is the total number of death claims approved by an insurance company, divided by the total no. of death claims received by the insurance company.

However, since the Insurance Act prohibits denial of claims after three years except in cases of fraud, it is advisable to look beyond the Claim Settlement Ratio and also consider factors such as claim amount settled ratio, corporate governance record, solvency ratio, assets under management (AUM) and instances of violations of IRDAI norms. Claim Paying Ability (CPA) ratings & CRISIL rating may be useful.

Is there a provision of MWP Act?

Married Women's Property (MWP) Act, 1874 enables a married man to protect an insurance policy only for the benefit of his wife and/or children. In case of a death claim, the policy proceeds are received by the trust and can only be claimed by trustees (wife and/or children). It cannot be claimed by creditors, relatives or form a part of the will (estate of the proposer).

For instance, if you are a salaried person with a home/personal loan or the owner of a business and have accumulated debts, your creditors will have the first claim on your policy proceeds in the event of your death. When you buy a term insurance online under MWP Act, your wife and/or children will be the only ones who will have access to the claim amount – enabling you to secure their future financially.

Are the right riders available?

A term insurance rider is an additional benefit in a term insurance policy that gives you supplementary coverage. Such riders give additional benefits apart from the core life cover which pays only at death of the policyholder. Some of the important riders to consider are as follows:

Accidental Death Benefit Rider: Accidental Death Benefit rider pays an additional sum to the nominee in case the insured dies in an accident. The rider is extremely cheap to buy and usually provides a cover equivalent to the sum assured under the term plan.

Critical Illness Cover: A critical illness benefit pays a lumpsum with no sub limits or conditions if a specified illness is diagnosed. In some plans the rider may pay you only a portion of the sum assured. It is important to look a little deeper (survival period clause and illnesses covered) into this benefit with the rise in lifestyle diseases.

Waiver of Premium: The policyholder is not required to pay future premiums on the policy in the event of an accident or mishap as defined by the rider. In such cases, the future premiums get waived off but your policy remains in force.

Don't unnecessarily take a term plan with high cover or a longer policy term.

CHAPTER 4

How Much Term Cover Do You Need?

Thumb rule says to have a life cover equivalent to 10-12 times of your annual income. But there is more to it.

When faced with the prospect of figuring out how much insurance to buy, most people pluck a figure out of the air--something that just seems adequate. This is not the way to make this important decision.

The ideal way of making this decision is to unemotionally create a financial plan that your family should follow if you die suddenly. Here are some heads to consider.

Loans and debts: As far as possible, take debtors' insurance so that your debts can be paid off straightaway. If you have a housing loan, the lender has probably made sure that you already have such insurance for that loan. Other loans need to be considered. While you can add these to your main term insurance, taking a policy where the insurance company will directly pay off lenders has the advantage that your survivors will not be tempted to carry the loans.

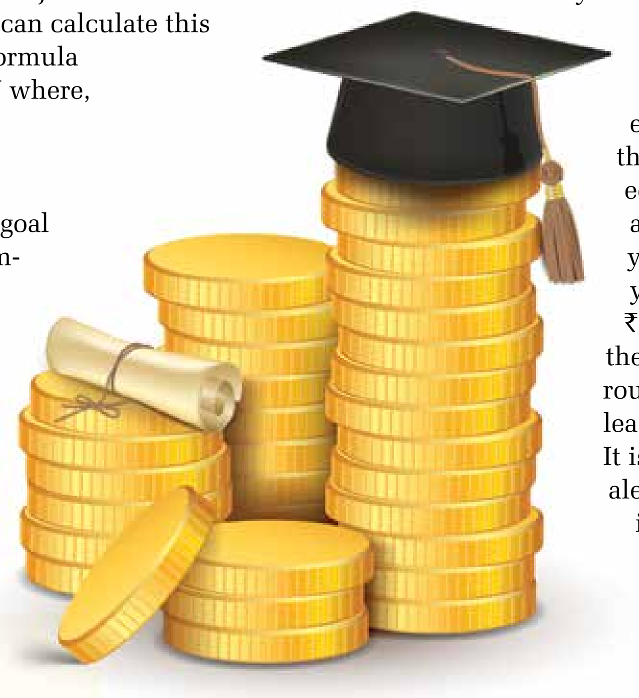
Do not waste money in insuring unsecured personal debt like that for credit card. The card issuer cannot make your family pay so there's no need to cover that, unlike say, vehicle loans where you wouldn't want the family car to be possessed by the lender.

Future Expenses: The hardest part of providing for future expenses such as higher studies of children, daughter's marriage, etc. is estimating and allowing for inflation. Take a reasonable, at least 7%, inflation rate into account. Let's illustrate with an example - Suppose you would need ₹20 lakh in today's value on your child's marriage, assuming you have

10 years to the event and 7% rate of inflation, you would need an inflation-adjusted sum of ₹39 lakh after 10 years. You can calculate this future value using the formula

$$FV = PV*(1+R/100)^N$$ where,

FV is Future Value
PV is Present Value
R is rate of inflation
N is number of years to goal



Education: Insurance companies are making some attempts at designing policies that will ensure that your children's education is paid for. What you ideally need is a policy that is conceptually term insurance, that is, which does not have any payout if your children get educated during your lifetime.

Living Expenses: Estimate what living expenses are going to be and estimate the investment needed to yield that much return. Your term insurance should be for this amount. Make a realistic financial plan and not an idealised one.

CALCULATE YOUR SUM INSURED:

A. Loans and other debt
B. Future expenses/living expenses of family adjusted for inflation.
C. Saving and investments

Formula = (A + B) - C

Sum assured should be based on current lifestyle, annual family income, annual expenses, current investments (if any) and liabilities like home loan or education loan overhead. The final value after considering these figures will be the life value of prospective insured.

If you find the above process to calculate the required cover too cumbersome, there is an easy way.

A widely used thumb rule to estimate the ideal life cover says that you should have a life cover equivalent to 10-12 times of your annual income. For example, if your annual income is ₹9 lakh, you should have a life cover of ₹1.08 crore (₹9 lakh X 12). Here, the insurance cover should not be rounded off to ₹1 crore as it would lead to under insurance by ₹8 lakh. It is believed that an amount equivalent to 10-12 times of your annual income should be sufficient to take care of your dependants.

However, this thumb rule is only meant to give you an estimate and does not give you an accurate figure.

Most insurance companies provide a 'Human Life Value' calculator on their website to ease the task of calculations as it is very important to find out an ideal cover. It is better to be over insured rather than being under insured.

THUMB RULE

Term Cover = 10-12 times of your annual income

Do not round off your life cover to ₹1 crore or ₹50 lakh. Every single penny is important in case of death.

CHAPTER 5

Are You Choosing the Right Payout Option?

Buying an adequate term cover is not sufficient to financially protect your loved ones. Selecting the right payout option is equally important.

Earlier, payouts used to happen only in lumpsum. But these days, insurance companies offer several options to choose from. Different firms may call them by different names but in essence they are more or less the same. Here's a primer.

Lumpsum

As the name suggests, the entire death benefit is paid to the nominee in lumpsum at one go. This option would work well if the nominee can carefully manage the money so received to fill the financial vacuum created by the demise of the insured, be it to meet the family's living expenses or any other goals. In fact, a financially literate nominee may be able to derive better returns by wisely investing the lumpsum payout than what is implicit in the payouts of other two options. But if that's not the case, you may consider the other two payout options because the very purpose of buying insurance will get defeated if the nominee ends up squandering the money received in lumpsum.

Monthly income option

In this option, the death benefit is paid in equal monthly instalments over your chosen period, say 10-15 years. For example, a term plan of ₹50 lakh with a monthly income payout option may pay around ₹40,000 to ₹50,000 every month for the next 10 years. These are indicative numbers and the actual payouts may differ from plan to plan and depending upon the number of years over which you want to stagger the payout.

This option should appeal to those who want to provide for the living expenses of their financial dependants post their demise, without entrusting the job of managing the money with the nominee. It has the added advantage of lowest premiums in comparison to the other two payout options.

Here's how the four payout options differ in case of a 30-year term insurance plan with sum assured of ₹50 lakh for a 30 years old healthy man.

	PAYOUT OPTION			
	Lumpsum	Monthly income	Increasing monthly income	Lumpsum + Monthly income
Payout	₹50 lakh in lumpsum	₹40,000 to ₹50,000 per month for 10 years	Starts with ₹42,000 per month; Keeps increasing by 10% every year for 10 years	₹5 lakh in lumpsum followed by about ₹42,000 per month for 9 years starting after one year of the insured's death.
Annual premium (approximate)	₹6,200	₹5,200	₹7,800	₹5,200

Increasing monthly income

Almost similar to the monthly income option, except that the monthly payouts increase every year at a pre-determined rate mentioned in the policy document. For example, the payout may be ₹42,000 per month in the first year, which increases by 10 per cent to around ₹46,000 per month in the second year and further to ₹50,600 in the third, and so on. This makes a lot of sense as the living expenses keep increasing with inflation over a period of time. Therefore, what looks like an adequate monthly income today may not be so a few years hence. But note that this is also the costliest payout option since the premiums you have to pay are the highest here.

Lumpsum+Monthly income

This is precisely a combination of the lumpsum and monthly income option. Here the nominee would receive a specified portion, say 10 per cent, of the sum assured as a lumpsum immediately on your demise. This can help him/her to pay off outstanding debts or any other immediate expenses which might occur. The balance of the sum assured is paid in equal or increasing monthly payouts. For example, a 30 year policy with ₹50 lakh cover may pay ₹5 lakh (10 per cent) as a lumpsum immediately on death and ₹40,000 to ₹50,000 every month for the next year 9 years.

TIPS TO FILL ONLINE APPLICATION FORM QUICKLY

- Keep your Aadhar and mobile registered with UIDAI handy. It would pre-populate the form with most of your details.
- Take a note of your height, weight and medical history. The form will ask for it. Also, you might have to undergo certain medical tests before the policy is issued.
- Scan your PAN, latest salary slips and Form 16. You might have to upload them as income proofs.

We recommend

- Go for the lumpsum payout if the nominee can deftly manage the money received as death benefit.
- Monthly income will suit those who don't want to leave the job of managing the money to the nominee. Go for increasing monthly income if you don't mind paying the extra premium.
- Choose lumpsum + monthly income option if you want your nominee to receive a partial amount as lumpsum to take care of the immediate needs followed by a monthly income for recurring expenses.

Summary

- You must buy life insurance if you have financial dependents.
- Term insurance is the best and the only form of life insurance you need.
- Carefully estimate the amount of insurance you need depending upon your annual income, your family's monthly expenditure, their goals, etc. As a thumb rule, it should be at least 10-12 times of your annual income.
- Ideally, the policy term should last till the time you expect to earn.
- Provide full and correct disclosures in all respects, including any existing medical conditions. Else, the insurance company may forfeit your policy.
- Buying insurance online directly from the insurance company's website is a preferred way as it is cheaper than buying it offline.
- Buy your policy under MWP Act to ensure that nobody else other than the nominee can stake a claim to the payout in case of your death.
- Choose the payout option that best suits your requirement. Go for the lumpsum option if the nominee can deftly manage the money received as death benefit.