

COMMENTS ON PERSONAL LIFE INSURANCE

This article discusses basic principles of life insurance and values for living.

Term life insurance is a contract that provides a death benefit for a specified period or term of time. This used to be known as yearly renewable term, which meant you could keep it for one year at a time, and just drop it whenever the need for life insurance ended. Strangely, term now is being sold as coverage for 5, 10, or even 20 years - a very long term of time - and a large part of the human economic life cycle.

Term is appropriate when the insured wants life insurance for a very specific need or for a very short duration. It can be appropriate when people have no free cash flow but need large amounts of life insurance. It can be appropriate where the need for life insurance expires in the short run: such as for specific needs: getting teens through college, when a business loan or partnership will expire in a few years, to weather a business depression, adjusting to your new home, job loss, losses in real estate, etc.

*Term life insurance generally carries an initially low premium. This premium inevitably increases, because the premium represents the cost for the insurance company to cover its mortality risk and actually provide a benefit. At the end of that term, the policy almost always costs more, for the simple reason that an insured is older and naturally more likely to die. So if people live to retirement age, or even a reasonable life expectancy (which is rapidly increasing) **they long outlive a term policy.***

*Increasing cost is not the only problem with term life; it is **INSURABILITY.***

Insurability** is the mysterious notion of acceptability to the insurance company, i.e. whether a person has health and a reasonably normal life expectancy. Insurability is as much an art as a science, and it changes with time. For example, years ago smokers were given standard rates; then medicine revealed a connection between smoking and mortality; now smokers pay higher rates. Diabetes was once considered uninsurable; wonderful improvements in health care increase life expectancy, which is reflected in insurability. **The point is that insurability is not up to YOU, it is up to the insurance company, because they are administering this for us, and sooner or later everybody becomes uninsurable, so, it is wise to have one's life insurance in place by then.

Term life, therefore, is deceptive, in pricing and in value. In terms of pricing, a closer look at the numbers will reveal that in almost every case term life represents a great deal for the insurance company (and maybe the agent) but a terrible value for the people actually paying out the money! - if the need for the life insurance lasts any more than just a few short years, which is pretty much the only time "term" works at all. This fact is blissfully overlooked but many consumer magazines and financial reporters.

Please Consider:

- 1. Fewer than 1 % of term policies payout in death benefits.
That fact in itself speaks volumes - why buy something you will lose?*

2. *Insurance companies collect your premiums on term policies for several, or many years, while paying out nothing in return. They keep your money, invest it, build marble castles, etc. This is good? For whom?*
3. *The term premium carries a mortality charge that in most cases is higher than the mortality charge on a permanent policy. Permanent policies have other profit elements designed into them, but, with a good company, the policyholder has the opportunity to participate in PROFITS, which are distributed to you as DIVIDENDS.*
4. *The commission on term life is higher as a percentage, in many cases, than a commission on permanent life insurance. It has to be, because insurance companies are competing to get brokers to sell their products. With permanent life insurance, the commission binds the agent to you contractually and morally for many years; he becomes your financial partner - for LIFE! (if only all our relationships last that long!). Your agent should give VALUE - education, consultation, advice, coordination, and yes, motivation. If you are not confident of this, get somebody else. You're entitled.*

This quality is unique among professionals, especially when we consider that your agent does not get paid until well after you are properly served - unlike the doctor, who gets paid whether or not you get well, or the lawyer, who gets paid whether or not you win your case, or the accountant, who gets paid regardless of the taxes you pay.

5. *I have been in the financial services business for many years, and I find it interesting that commissions on permanent policies have been going down, while commissions on term policies have been going up. The point is that permanent policies have always been an excellent consumer value and are increasingly so. Improvements in medical care, a more educated and therefore autonomous society, technology, greater social tolerance and the health sciences all have improved personal life expectancy: all this is reflected in the values passed on to consumers in permanent life insurance, in the costs and benefits.*

If term life is such an excellent value, then, why is most of the cost of term life directed right to the agent who sells it? Would you buy a car if most of the ticket price went into the salesman's commission? Commissions on some term policies exceed 100% of the term premium itself, a fact I find just astonishing. If term life is such a good value for consumers, then, why is everybody selling it? Simple - it is extremely lucrative.

6. *These products are priced two ways: first they are priced actuarially. This accounts for the likelihood of death at various ages, use of money, expenses, etc. Second, they are priced to market, i.e. according to competition and what people are willing to pay. Because life insurance is a contract, not a mere product like motor oil, it must be priced scientifically - according to sound mathematics and economics. Otherwise, it would not work, and there could be no contract.*

The insurance companies understand the use of money; a close look at the total cost of term life - the true cost - the sum of premium, plus income tax, plus lost interest - is evidence that term life has planned obsolescence designed into it - consumed and disposable, like so many other things in our society. It has become commoditized, reduced to the status of a product, instead of a CONTRACT, which it really is.

But life insurance was invented, and works best when it is used to replace Human Life Value - the monetary value of a person's productive power - his/her earnings.

- 7. These companies have billions; they spend tons on consumer studies, and know more about your buying preferences than you. They know that you will buy term, pay for years and when the premium increases beyond your comfort zone, you will cancel it. When somebody dies the first question we hear is about life insurance; and everybody knows if a life insurance agent is at the funeral. But the insurance company doesn't care either way, and they will keep all the money you paid in, plus all the interest they earned all those years, foregone by you, MONEY you gave up.*

***But someday you WILL die.** Only people you love and who love you will care.*

The life insurance company will continue quite handsomely because they understand the use of money. That is why they build marble palaces, take huge salaries and bonuses, and the final insult: they convert policyholder equity into corporate or executive equity with legal gaming, i.e. bonus, options, loans, or the latest tax maneuver called the mutual holding company plan. This new creation did not even exist just a few years ago, but it does now, thanks to a new law, and more companies will try to shelter income with it.

Furthermore, when you do die, it is highly unlikely that the insurance company or the IRS will build a marble castle dedicated to the memory of your premiums.

Companies are entitled to make a profit, of course, for if there is not enough money to do business, they go out of business, and the people who get hurt most are the customers, the ones who need it most. Or, the insurance company shuts down one operation and starts up another one. The question is: who should get the profits, the managers or the customers? In the old days - right up until the mid-1990's - mutual insurance companies gave profits back to policyholders in the form of dividends. There are still a few of this old breed left, and well run. They hold to a higher standard. The Knights of Columbus is the only major company with the highest financial ratings (AAA) that operates as a charitable corporation. That is a unique and powerful benefit.

Profits on permanent life do not appear for about 10 years, and then over the life of the average policy look like this: 1 % for the mortality charge, 1 % for the administration charge, and 1 % for the sales agent. The rest of the money goes to you, inside your policy in the form of cash reserve values. The internal rate of return on the cash value element of a permanent cash value life insurance policy over a 20 year duration is about 5%, and considering that is essentially a no risk, tax sheltered, liquid, creditor proof, nonprobated contract which cannot be denied except if a beneficiary conspires to murder you, that pays a known sum upon death far in excess of your cost basis, that makes it not only truly unique, but quite attractive, considering that no other instrument even comes close. Reason requires we examine all the benefits, not just one.

But forget all that hyperbole for a moment. When the chips are down do you want to Increase your risk, Reduce your risk, or Eliminate your risk? Then calculate returns.

Some wise owls, especially financial writers in the popular press, expound a theory called "BUY TERM and INVEST the DIFFERENCE". This is a simplistic approach and upon examination will prove to be dead on arrival. The theory is you only have a fixed savings, a percentage of

your income, and therefore you cannot afford permanent life insurance, so you will be forced to capitulate and buy the cheap, inexpensive term life; and the difference between the whole life premium and the term life premium should be put into some great mutual fund. Some mutual funds do a great job, but not the job of life insurance. Get the right tool for the job. Don't try to compare apples and oranges, or try to compare Mickey Mantle with Willie Mays, it cannot be done. This is not to say that all persons must wear the same size hat - rather, that a 'no brainer' approach guarantees one thing: a poor choice.

There are several problems with this theory about term and invest.

*First, it is exclusionary. It is based on scarcity thinking. It says you have a limited income, a fixed income, and therefore a limited ability to save. This is nonsense. **We live in America, land of the free and home of the brave, in a time of rapid global technological, communications, social, and economic change. People are more mobile than ever, more educated than ever, more intelligent than ever, more demanding than ever, healthier than ever and living longer than ever. This will continue. The history of man for the last millennium is toward greater personal, economic and political freedom and this will continue indefinitely. Ain't no going back!** So we can expect with every good reason to have more money in the future than we do now, if we are smart enough to do the right things, and ignore stupid ideas like Term and Invest.*

Secondly, it ignores human nature. Human beings are "self interested". We want to feel good. We marry the one we think will make us happy, raise children, affiliate with birds of the same feather, do the job or game or art or craft or whatever it is our hearts desire, to get what we want. We also consume as much as possible, buy stuff, and spend all that we earn and more. None of these is rational! Saving money is an unnatural process and sometimes painful, because it actually forces us to deny our first impulse, which is to get, not to give; Saving is Giving Up. We spend everything we make as soon as we get it. As evidence for this law, I cite my lovely wife, and most men if honest, agree that this is true of most women. So we would rather spend than save, and in America, man we like to live it up! Everybody wants to be rich. Why not!?

What they don't recognize is that the rich got rich because they did something better than everybody else: they saved money! And guess what they do even when rich? Save money - Much more as a percentage of income than most, even in hard times.

In my experience, especially when dealing with self-made men who started with nothing, there is a dramatic change in the thinking of such people - they start to look upon money as a resource, a tool to be used, a piece of equipment, a partner - that is, they see money as CAPITAL, a talent to be directed, employed, utilized - which is very different than seeing money as a medium of exchange. A medium of exchange has no value in itself - and that is why middle class people spend money to get what they want, THINGS, which do have value. But upper class people use money to make money. This is exactly what Adam Smith describes in The Wealth of Nations. And that is why some people have a lot of money, and most do not.

This notion is very simple, but very radical; and once you get it, it changes your life.

So term and invest ASSUMES that people will save on their own, a false assumption. People really like the systematic, forced savings, of life premiums - that we save money on time, each time. Over time, that really makes a difference, because just one month of missed savings means you lose the savings PLUS the growth, the interest that money would have earned. Life insurance actually forces you to save; that premium does not disappear, it buys the big death benefit if you die young, and goes on account into your policy. This is called cash reserve value, and is liquid, competitive, has tax preferences, creates lasting value, and contributes to your wealth and social wealth.

Permanent Life Insurance Guarantees an Inevitable Gain, in many ways.

So we see the deceptive nature of term life. But Term & Invest also assumes - a level, fixed, unending compounded growth rate. This is the most dangerous assumption. Simply put, if the assumptions were true, then we would all be rich, because we would put the assumptions to the test and they would work, and we would have the money and already be rich. But since we aren't all already rich, the assumptions must not be true.

Therefore the theory is not true. There is no single formula, no magic bullet.

The theory assumes we are not smart enough to find a way to manage our money for optimal results, for maximum benefits, with reason, discipline, insight, and charity.

Term and Invest does not factor in the effect of taxes, which is the largest expense facing us. Taxes take more of our income than housing, education and savings - combined! So if you like paying taxes, I suggest you do term and invest, because it guarantees you will pay more taxes, dollar for dollar, than if you purchased a good quality whole life from a top company.

There is only human capital: knowledge and applied intelligence.

*Life insurance is the only financial vehicle that **marries the money to the person**, thereby **capitalizing** the resources and unique values that Person contributes to our human family. This is the most important concept on planet earth: that EACH human life has real value well beyond the obvious. **Each of us is IMMEASURABLY INVALUABLE!***

Some people believe that they really do not need the life insurance after they retire, as their earning power has ended. This is brainless. Just because people have stopped working does not mean they have become useless and valueless. They believe that because the kids are grown they not have a need for permanent life insurance, so, they just drop it. Well, first, as that cancels the contract, it guarantees that they have permanently parted with their paid-in premiums, so they lose all that money, all the taxes they paid to earn that money to pay those premiums, all the interest they could and would have earned on both the premiums and the taxes, and worst of all, they permanently part with the inevitable benefit, which is inevitable because it is paid upon the inevitable event of your death! Second, it is based on how you see the world today. But people change! How many of us see the world at 45 the same way we did at 25? Based on my experience, extant from 1981, I assure you, at age 65, it is altogether different.

The older we get, the more we realize that life is short, that perhaps we did not do all that we wanted, that there is so much more we want, yet due to problems in living, health conditions, or lack of money, we cannot actualize every dream and desire. Life insurance helps alleviate that, indeed, it greatly accelerates our pursuit of happiness, as we see that it guarantees a known sum of money each year, dead or alive.

Some people believe that persons who are aged or handicapped or suffering should stop living. I do not. If the love of family, community and country is still there, then of course it is desirable to have life insurance payoff after a long and happy life. If you are charitably inclined, then, life insurance makes a capital gift - tax deductible -far in excess of premiums paid in. Or, you can take your money out as a retirement supplement. Or do both. Why not? In this example, life insurance endows a rich legacy, far in excess of the premiums paid in. When you actually die, then, it pays big time.

Of course that is impossible with term, only with permanent.

Term and Invest does not factor in the loss of the use of money based on the sunk cost of the term life, or the lost opportunity cost of the money lost to taxes or carrying costs of the investment - the time and effort involved in researching an investment, the record keeping, accounting, or sweat equity. Ask anybody who has invested in real estate, or lost money on a hot stock tip. Not to mention the worry involved with their risk. No to mention the loss of use of the money - and all the interest, dividends, and capital gains that could and would have ensued had that money not been lost in the first place. Are we really going to pretend that sweat equity and worry have no value? If they have no value then what are we worrying about? The simple truth is that sweat equity and worry have tremendous value – tremendous cost – except – we do not know the result!

One of The most gratifying things in life is when we when you know the results ahead of time. Isn't it altogether better to know our financial means ahead of time? Wouldn't that be great?

Given your choice of a financial partner, indeed, the one you quite literally want to replace your economic life value, which would you bet your life on? The one who takes all your money, or the one who takes 1 %, gives you all your money back, and then divides the profits with you? Quite simply, whole life costs less than term, over time.

It is not only the unique powers of permanent life insurance that make it attractive; it is what it allows us to do. It allows us the freedom to live the life we want to, to build and create with confidence, knowing we have a guaranteed foundation that will never fail, it is a veritable fountain of money. That no matter what happens, life insurance is there for today & tomorrow - and the money it creates will work for you, your children, and your children's children - with no risk, worry, or maintenance required. How much is that worth?

So after knowing all this, if you really believe that term is the better buy, go that way. But in my whole career, I have never had anyone complain about whole life after 10 years, because by then they have all their money back, and the life insurance itself has been almost free. They have been able to save and create an immediate, indestructible estate. There is no better way to create wealth than to install a healthy amount of permanent life insurance as the heart of your financial plan. It will weather all the storms of life, and when you check out, we will check in. You can count on it.

My most astonishing realization was that really rich people - Wayne Gretzky, Bill Cosby, Bing Crosby, Walt Disney, J.C. Penney, Larry Bird, Malcolm Forbes - each had a ton of whole life. Why is that – because they are stupid? Why does every major bank, every major corporation, and every US President own a ton of permanent life insurance – because they are stupid? It is not something they need, like dental work.

Rather, it is a positive good in its own right: it fully complements an integrated strategy, it enhances and enriches other investments while it protects, and it accelerates the pursuit of happiness. It has withstood the test of time. When you check out, it will check in, you can count on it, and there is not much in this life that offers such certainty.

Permanent life insurance is the best investment on the planet - bar none.

Everybody should own as much as they can get.

If everybody owned permanent life insurance, everyone would have certainty in their lives, we would have money when it is needed most, we would never lose any money, and in time we would eliminate poverty in the world, forever, and all the problems that go along with it including war and famine. Any of these reasons alone should be sufficient. Together, it should be irresistible.

It has been said that I am an idealist, and I hope, even despite my advancing age, that I never stop yearning for peace on earth.

I hope by my work I have contributed to your wealth and wellbeing, to your pursuit of happiness, to your peace of mind and to peace on earth.

Thank you.

Very Truly Yours,

James V. Aulenti, ChFC