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Does An Insurance Policy Illustration Influence Your Purchase? [801 words]

Computer-generated illustrations should only guide — not determine — your life insurance purchase decision, because they cannot unequivocally tell you what the actual costs and benefits will be.

A life insurance illustration is prepared by an insurance company's actuaries — its number crunchers — to show you how a policy may perform over time. Using various assumptions about your age and health status, type of policy, etc., it illustrates the *hypothetical* benefits for every year you may own a policy, which means that actual costs are normally higher or lower than illustrated.

Term insurance illustrations show the current and maximum annual premiums, total premiums paid to date and the death benefits of a policy. Permanent life insurance illustrations tend to be longer and more complex than term life illustrations. (This is because term insurance protects you for a limited, specified period of time, while permanent insurance combines a death benefit with a savings component.) With permanent illustrations, the insurance company has to project its estimated investment returns, expenses and mortality charges years into the future. As a result, other than the "guaranteed" numbers you see, the actual cost of permanent insurance benefits is generally higher or lower than illustrated.

Make Your Illustrations Meaningful

Perhaps it's best to think of a life insurance illustration as a kind of diagnostic tool — it's useful but not fully predictive. Once you understand its limitations, you can use it intelligently to buy an actual policy. Here's how.

To make comparing the relative costs of similar policies easier, all illustrations include a cost index that reflects policy premiums, cash values and dividends (if applicable). When you compare costs, it won't do to merely subtract the cash values and dividends you expect to receive from the premiums you'll pay. You'll need to adjust for the fact that premiums are paid over time. Not to fear, however — the cost index does the math for you. You simply compare the cost indices of the policies you're considering.

The most important thing to remember when using cost indices is that a policy with a small index number is generally more cost efficient than a comparable policy with a larger index number. The following rules of thumb are also important:

(1) You should make cost comparisons only among similar life insurance policies. "Similar" policies provide essentially the same basic benefits and require premium payments for

approximately the same period of time. The more similar the policies, the more reliable the cost comparisons.

(2) Compare index numbers only for the same kind of policy, for your age and for the amount you intend to buy. Since no one company offers the lowest cost for all types and amounts of insurance at all ages, it is important you get the cost indices for the actual policy, age and amount you intend to buy. If one company's policy is a good buy for a particular age and amount, don't assume that all of the company's policies are equally good buys.

(3) Small differences in index numbers could be offset by other policy features, or differences in the quality of service you may expect from the company or its agent. Therefore, when differences in the cost indices are practically negligible, your choice should be based on something other than cost.

(4) Life insurance cost indices only apply to new policies and should not be used to determine whether you should drop a policy you've owned for years. If such a replacement is suggested, ask for information from the company that issued the existing policy before replacing it.

(5) Finally, before making a purchase decision, be sure you can afford the premiums, and that you understand the policy's cash values, dividends and death benefits. Also assess how well the insurance company or agent will provide ongoing future service to you as a policyholder.

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