



# Life Insurance: Providing Financial Protection

Life insurance is a key component of Americans' ability to take individual responsibility for the financial futures of their families and businesses. It is unique in guaranteeing the delivery of financial security at precisely the moment it is needed, while contributing significantly to the nation's storehouse of savings and investment capital.

A big fear for many American families is the death of a wage-earner or caregiver, leaving the surviving family members unable to cope financially. Life insurance offers peace of mind through immediate financial protection for dependents.

Life insurance enables individuals and families from all economic brackets to maintain independence in the face of financial catastrophe, helping relieve pressure on government entitlement programs. For this reason, there has been strong public support for continuation of current tax policy for life insurance products.

By providing tools for self-protection and savings, life insurance is an efficient way to promote personal responsibility and foster less dependence on government programs. A recent survey showed that three-quarters of Americans agree that life insurance is a critical part of a financial plan.<sup>1</sup>

## SUCCESS OF THE PRODUCT

Life insurance protects families from financial loss from the death of a loved one. It enables families to pass on more assets from one generation to the next, providing a source of reliable liquid assets when the need arises to pay for death-related expenses. Very few Americans can self-insure the risk of premature death through their own financial means. Life insurance makes managing this risk affordable through the pooling of risk. Industry data shows that in 2007, there were 158 million individual life insurance policies in force providing more than \$10 trillion of protection. Sixty-five percent of American families are protected by life insurance.<sup>2</sup>

Permanent life insurance has an additional advantage—it is guaranteed to remain in force for one's whole life, regardless of age. By design, the level premiums of permanent insurance are used to both pay for the term cost of a policy's face amount and to create a savings component (cash value), which helps cover the rising cost of insurance as one gets older. If an insured's needs change and death benefit protection becomes less acute, the policy's cash value can be used to pay various expenses, such as those for tuition or long-term care. Or, the cash value can be converted into a retirement income producing annuity that can guarantee regular payments for life or for a specified period of time, an option also available to beneficiaries of life insurance policies. Some policies allow an insured to collect all or part of the death benefit if he or she becomes terminally or chronically ill. Fifty-nine percent of the individual life insurance policies issued in 2007 were permanent policies.<sup>3</sup>



AMERICAN COUNCIL OF LIFE INSURERS



NATIONAL ASSOCIATION OF  
INSURANCE AND FINANCIAL ADVISORS



<sup>1</sup> ACLI, *Monitoring the Attitudes of the Public*. 2004.

<sup>2</sup> "Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances." *Federal Reserve Bulletin*, 2006.

<sup>3</sup> ACLI, *Life Insurers Fact Book 2008*, forthcoming.

Businesses use permanent life insurance to protect against financial uncertainty and secure their employees' futures. By owning life insurance on key employees, businesses have a secure funding source to pay for important employee and retiree benefits and to protect jobs and families from financial loss and instability that can result from the death of an owner or key employee.

### **CURRENT TAX TREATMENT**

Policy-makers have long-recognized the important social policy served by encouraging individuals and families to protect themselves against financial risks, rather than depend on government to do so. Since its inception in 1913, the tax code has provided that death benefits—and the cash value in permanent life insurance—are not subject to income tax.

Premiums are paid with after tax dollars—there is no deduction for premiums paid. Earnings on a permanent life insurance policy's cash value are not taxed as long as the policy remains in force. However, if a policyholder gives up his or her insurance protection, earnings in excess of the total premiums paid are subject to tax.

The protection afforded by life insurance is an important societal benefit that public policy has consistently validated. This policy has been reviewed several times over the last century, and each time Congress has chosen to preserve the current tax treatment of permanent life insurance.

### **CONCLUSION**

The current tax treatment of permanent life insurance encourages individuals, families, and businesses to efficiently manage risk and prepare for long-term financial needs, despite a general environment that focuses more on the short-term. Any changes to public policy must not limit or disadvantage the critical protection only permanent life insurance can provide.

### **ISSUES AND TRENDS**

- The financial plans of 65 percent of American families include life insurance.<sup>4</sup>
- These families are covered by life insurance policies and group certificates that provide more than \$19 trillion worth of protection.<sup>5</sup>
- In 2007, there were 11 million individual life insurance policies issued.<sup>6</sup>
- Of all the individual policies issued in 2007, 55 percent were permanent insurance policies.<sup>7</sup>
- In 2007, beneficiaries of life insurance policies received \$56 billion in death benefits. Of this total, individual life insurance policies accounted for more than three-fifths.<sup>8</sup>

### **AALU**

Founded in 1957, the Association for Advanced Life Underwriting (AALU) is a professional trade association representing 2,000 life and health insurance agents and financial advisors nationwide. The mission of AALU is to promote, preserve and protect advanced life insurance planning for the benefit of its members, their clients, the industry and the general public.

[www.aalu.org](http://www.aalu.org)

### **ACLI**

The American Council of Life Insurers (ACLI) is a Washington, D.C.-based trade association. Our 373 member companies represent 93 percent of the industry's total assets, 91 percent of life insurance premiums, and 95 percent of annuity considerations in the United States. They offer life insurance; annuities; pensions, including 401(k)s; long-term care insurance; disability income insurance, reinsurance; and other retirement and financial protection products. [www.acli.com](http://www.acli.com)

### **NAIFA**

NAIFA was founded in 1890 as the National Association of Life Underwriters. It comprises 750 state and local associations representing the business interests of 200,000 members and their employees nationwide. Members focus their practices on one or more of the following: life insurance and annuities, health insurance and employee benefits, multiline, and financial advising and investments. NAIFA's mission is to advocate for a positive legislative and regulatory environment, enhance business and professional skills, and promote the ethical conduct of its members. [www.naifa.org](http://www.naifa.org)

### **NAILBA**

The National Association of Independent Life Brokerage Agencies (NAILBA) is a nonprofit trade association with 353 member agencies in the U.S., representing 100,000 producers who deliver more than one billion dollars in first year life insurance premiums annually. NAILBA is dedicated to fostering the growth of its member agencies by providing educational resources, industry standards and a collective voice for legislative and regulatory efforts. Each of NAILBA's members commits to a statement of responsibilities to ethically and responsibly serve their clients' best interests. [www.nailba.org](http://www.nailba.org)

<sup>4</sup> "Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances." *Federal Reserve Bulletin*, 2006.

<sup>5</sup> ACLI, *Life Insurers Fact Book 2008*, forthcoming.

<sup>6</sup> Ibid.

<sup>7</sup> Ibid..

<sup>8</sup> Ibid.