HAVE YOU CONSIDERED RETURN OF PREMIUM TERM LIFE INSURANCE?

A very good opportunity arises with a type of term life insurance known as return of premium term (ROP term). As you probably already know, with term life insurance you pay a much lower premium for a given amount of coverage than for permanent insurance, but term insurance typically only provides coverage for a stated period or "term" and does not provide any cash value that can be used for many purposes. ROP term is a different twist. Like regular term insurance, this policy pays the stated death benefit during the term period. It costs considerably more than regular term insurance. However, if the insured survives to the end of the period, it generally returns all of the premiums paid during the period as a lump sum at the end of the term (and the policy usually expires at that point, though some policies do allow continuation of the coverage at increased rates). The insurer can do this by structuring the product so that the investment income it earns on the premiums collected over the period is sufficient to pay claims, expenses and commissions and still make a profit after returning the premiums at the end. These policies also generally develop a cash value that is a percentage of the total premiums paid, with that percentage getting larger the longer the policy is held.

If you start with the premise that you have a need for a specific amount of term insurance and need to purchase that amount in one form or another, the idea is to compare a regular term plan to a return of premium term plan. Because you get all the premiums back with an ROP term plan, the key is to determine what interest rate is required to be earned on the difference in premium between the two products in order for that difference to accumulate to the return of premium amount at the end of the period. This is the critical point – you will pay an incremental premium every year in order to get ALL of the premium back at the end of the period, so what would I have needed to earn on that difference?

Here's an example from a well-known insurer from a couple years ago. Their premium for $1,000,000 of regular 30-year term for a male, age 35, in the best class available, is $1,785. The corresponding premium for ROP term is $4,014. The annual difference is $2,229, and the ROP amount after 30 years is $120,408 ($4,014 x 30). The interest rate needed on the difference to accumulate to the ROP amount 30 years hence is **3.56%.** Then, when you consider that the ROP is a **non-taxable** return of basis and therefore the return must be grossed up by the combined marginal tax rate (assuming 40% in this example), the effective pre-tax rate to compare increases to **5.9%.** Then, consider that this rate of return is <u>guaranteed</u> for 30 years by the carrier. This can be a very compelling case for the additional premium.

Clearly, the decline in interest rates over the last 15 years has made this product design more difficult and therefore more expensive (as have more stringent regulations

regarding the cash value buildup), but there are still a small number of products in the market (I've recently seen offerings from Assurity Life and State Farm). And the duration of these products is typically at least 20 or 30 years, as shorter periods don't give the carrier enough time to accrue the necessary investment income.

Additionally, there are term-like permanent plans that offer similar ROP benefits at specific points such as the end of the 20th or 25th policy year.

If you can find it, ROP term deserves your consideration. Talk to your financial professional about what is right for you.