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How Physicians Can Stop Hating Life Insurance (Part II)

By Ike Devji, J.D. | August 2, 2011

In our last discussion, I addressed why physicians should consider insurance a legally protected asset class and cash alternative, not just an expense. Here, we continue to examine the tactical application of insurance and how you should think about it as part of your investment and estate planning portfolio.

The Old Math is Wrong

There's a good chance that pesky life insurance agent is actually right, you really do need more insurance In the distant past of life insurance two "magic" death benefit numbers came to be a standard: $1 million on the husband and either nothing ($0) or a begrudging $250K on the wife. This allocation is clearly a product of the 1950s, when a million dollars was a lot of money and when most women were not employed outside the home. But it does not reflect today's reality.

Think about it: If you passed away today, would $1 million (or whatever amount you currently carry) be adequate to pay off your home, cover any outstanding expenses and debt obligations your family and estate would be responsible for, cover any estate tax exposure, put your kids through college and still have enough principal left to generate replacement income that would allow your family to keep the current lifestyle you provide? In almost every case we see the answer is a resounding NO.

Some simple math: a $1 million death benefit paid to your family and invested, even if it safely produces a whopping 10 percent annual return, will only produce $100K annually in income, and that's pre-tax. Would that be sufficient to replace your current income? Furthermore, many American families are now two-income families and have lifestyles and expenses based on that dual income stream. Is your spouse adequately insured to replace the income he or she generates? A simple review of most conventional investment strategies shows that nearly no other investment can provide the returns on present dollars that insurance can for your family, and certainly not with the same beta (risk calculation) or level of predictability. Many of my clients look at insurance as purchasing specific amounts of inheritance for their heirs at a fixed dollar and opportunity cost (i.e., "I can buy my kids $5 million in the future with a high degree of certainty by spending $XXX today)." How many other investments allow that calculation with any credibility?

Sometimes an Audit is a Good Thing

This is uniquely true in the case of life insurance, especially since the actuarial tables, (the things insurance companies use to figure out how long you'll live, when they'll have to pay the policy, and how much money they will make on you) have changed in your favor. Advances in education, nutrition, and healthcare mean people are healthier, or at least living longer. This means your insurance dollar goes farther than it did even a few years ago.

I routinely have all those I work with put all their policy statements together and give them to one of the insurance experts I work with across the country to review. In nearly every case except those where there have been significant changes in health conditions or very long periods since the insurance was first obtained, there is an opportunity for the insured to have greater economic efficiency. In plain English that means the insured would get more of a death benefit for the same cost, or more for less cost.

How much do I believe in this review? As one personal example a close member of my family followed my suggestion and my experts reviewed the multiple policies she had in place. We discovered that rolling one policy over to another carrier but maintaining the same premium allowed us to create a nearly 500 percent difference in what she would leave her children. In her case it was pretty simple; one of the $1 million polices she had was replaced at the same annual cost but now provided $2.5 million. We then determined that by using a life insurance trust (ILIT) we could exclude it from her estate and her kids would get the full $2.5 million, as opposed to the $450,000 they would have netted if it was in her old policy, in her own name and taxed at 55 percent. Shortly after the new policy in place she was diagnosed with a medical condition that would have made her uninsurable. She now loves insurance too.

Learn more about Ike Devji, J.D., and our other contributing bloggers here.