

OWN AN INVESTMENT-LINKED POLICY? DON'T GET OVERLY WORRIED.

BY CHRISTOPHER TAN

Since my last article on why using term insurance is the best way to protect our risks, I told myself that I would stop writing about insurance and move on to something else. However, due to the recent spat on regular premium investment-linked policies (ILPs), many have encouraged us to share our objective views on this subject.

To recap, ILPs are insurance policies that combine life insurance with investments into unit trust. Part of your premiums goes to pay for insurance charges that cover your needs, and part of it is used for investing. However, as these policies are structured in a way where insurance charges will increase over time, it is technically possible that these charges may be more than the premiums payable, and begin utilising the investment value to pay for these said charges, until they are fully depleted. If and when that happens, the policy may lapse or you may have your cover lowered. It is this realisation that has sent fears amongst policyholders across the country. Unfortunately, whilst many reports have highlighted all the problems associated with ILPs, little has been written on what one should do if you own one.

For a start, let me state that we are not an advocate for ILPs, but, to be fair, I think that this issue on ILPs have, to a certain extent, been blown out of proportion. Although it is generally true that there is a

possibility for these policies to lapse or coverage lowered, my opinion is that we need to be careful and more specific as insurance charges and premiums vary from insurer to insurer. Table 1 showed the estimated insurance charges by one of the insurers in Singapore, for a female non-smoker having an \$80,000 death, disability and illness ILP insurance. Annual premium at age 25 is \$1,300. **What conclusions can we deduce from the numbers?**

1. Insurance charges increase tremendously from age 40 to age 50
2. Insurance charges for critical illness increased at a higher rate.
3. If you have bought the ILP at a young age, and by that we mean age 40 and below, you would still have a majority of your premiums allocated to investments.
4. Even if total insurance charges at age 50 goes up to \$1,030 p.a., which is a huge jump, your policy will not lapse.
5. At age 60, you should have accumulated a decent sum of "cash

TABLE 1 (Numbers assumed for maximum protection option)

Age	Insurance charges For death & disability cover per '000 per year	Insurance Charges For Critical Illness per '000 per year	Total insurance charges out of \$1300 p.a. premium
Age 25	\$1.26	\$0.64	\$152
Age 35	\$1.26	\$0.91	\$174
Age 40	\$1.30	\$1.30	\$208
Age 50	\$4.55	\$8.33	\$1,030

values” to fund the extra insurance charges should it increase beyond the \$1300 p.a. premium. Though your “cash values” will depend on market situation then, let’s not be too extreme to say that you will lose everything.

So, what does all that means to you?

1. If you have a competent adviser, you should never have been advised to buy an ILP when you are age 40 and above, unless of course, you have certain unique requirements. Given the nature of an ILP, I would think that most owners of ILP and the younger lot.
2. If you have bought an ILP when you were younger, you should not be so worried that you will lose your cover when you become older.
3. If you have unfortunately bought one when you were much older, you should not be overly worried too, as it is likely that you should still have your required cover at age 60. And if you have been following this column, you will not be too worried about losing cover beyond that age, as most of the time, you will no longer require or have very low insurance needs.
4. If you have bought a regular premium ILP for the purpose of investing, you really need to re-think about whether you want to continue the plan, as such policies are not meant for such a purpose.
5. Some insurer offer sum assured guarantee (subject to certain conditions) till age 65 and as such even if market performance is bad and your premium cannot cover the insurance charges then, you will not lose or have to reduce your cover.

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So, what should you do if you own an ILP?

Except for hospitalisation and surgical cover, and a small cover (like \$100,000) for alternative medicine if you contract a major illness, your insurance cover will reduce over time and by the time you reach retirement, you should have little or no insurance needs at all. As such:

1. Read your policy to check whether your premium will be able to cover the insurance charges at a later age. Also, check to see whether your insurer offer sum assured guarantee up to a certain age, before you decide whether you need to do anything at all.
2. Know how much cover you need. You may be pleasantly surprise that you are over-covered and can terminate some of these ILPs, and get some of your monies back.
3. If you still need the cover, you can explore replacing it with a more appropriate and cost effective policy. However, you need to carefully weigh the cost against the benefits from both the financial and non-financial perspectives. Some things to consider would be
 - a. Are there savings if you switch to another policy, after taking into calculation the new premium and the cost of surrendering your ILP?
 - b. Has your health changed since you bought the ILP, and as such surrendering the ILP may be a bad idea?
 - c. It is generally believed that policies with critical illness benefit bought before July 2003 is more lenient when it comes to claim. Are you prepared to accept the new definitions?

Often times, restructuring your insurance can give you better cover at a lower cost. However, as it is a complex process, be sure to get professional advice before you decide. To have an understanding on your current insurance situation, you can use the tool that we have created at www.commissionsfreeinsurance.com or www.commsfree.com.

I hope the writings above have helped you allay some of your fears and also given you some ideas on what you can do if you own an ILP. But more importantly, I hope that this ILP saga has caused you to realise that when it comes to insurance, it is best to keep it pure and simple. Use term insurance to cover your needs. Use investments such as unit trusts to invest your monies. If you try to

put the two together, it may get too complicated for your liking.

By now, I hope you understand why Providend is so single-minded and passionate about using term insurance. It is simply the most sensible and cost effective way to protect yourself.



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