

## Life Insurance: Payout Options

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### Filing a Claim

Life insurance pays a *death benefit* to the stated *beneficiary* at the death of the *insured*. When the insured dies, the beneficiary of the policy files an insurance claim. There are several things the beneficiary should do:

1. Obtain several certified copies of the death certificate. The funeral director will be able to help the beneficiary obtain these copies.
2. Contact the agent who sold the policy. The agent will be able to help the beneficiary with the claim process. If the beneficiary does not know the agent, he or she can call the insurance company. The contact information for both the agent and the insurance company should be written on the policy.
3. Choose how the death benefit should be paid.

### Death Benefit Payment Options

The insurance company will ask the beneficiary how he or she wants to receive the death benefit. There are several different options.

#### Lump Sum

The lump-sum option pays the entire death benefit to beneficiary at one time. The entire payment will be income tax free. The beneficiary may then use as much of the death benefit as he or she needs, and invest any remaining amount. If there is a loan against the *cash-value* account, the insurance company will subtract the amount still owed on the loan before paying out the death benefit.

- **Example:** \$100,000 death benefit – the beneficiary receives \$100,000.

### Life Income

The beneficiary has the option to receive the death benefit in guaranteed payments over the remainder of his or her life. The life insurance company will look at the person's age and gender and calculate how much income the beneficiary could receive each year from the death benefit. The payments will only stop when the beneficiary dies. If he or she dies earlier than expected, the insurance company keeps the unpaid amount.

- **Example:** \$100,000 death benefit – beneficiary (a 54-year-old male) elects the life income option. Based on his life expectancy, the insurance company promises to pay the beneficiary \$6,250 per year for life.

### Life Income with a Period Certain

With the life-income option (listed above), if you were to die in five years, you would only have received \$31,250. The insurance company would get to keep the rest of the total \$100,000 death benefit.

If the beneficiary wants guaranteed payments for life, but doesn't like the idea of the insurance company benefiting if he or she dies early, then a life income with a period certain option may be a better option. A life income with a ten-year-period certain option means that the beneficiary will receive guaranteed payments for life, or at least ten years (whichever is longer). The beneficiary can choose among different periods (five, ten, 20 years) but the longer the period, the less the payment.

- **Example:** \$100,000 death benefit – beneficiary (a 54-year-old male) elects the life income with 20 year period certain option. Based on his life expectancy, the insurance company promises to pay the beneficiary \$4,620 per year for life or 20 years (whichever is longer).

If the 54-year-old male dies in five years (after receiving \$23,100), a secondary beneficiary will receive \$4,620 per year for 15 more years.

## Joint and Last Survivor Life Income

The beneficiary can choose a life income option over two or more lives. Under this option, the payments are guaranteed until the death of last beneficiary.

- **Example:** \$100,000 death benefit – beneficiary (husband, age 54) elects the joint and last survivor option for his life and his wife's life (age 52). They receive \$5,600 per year until both he and his wife die. If he dies in five years, she still receives \$5,600 per year until she dies.

## Specific Income

With this option, the beneficiary can tell the insurance company the schedule to follow to pay the death benefit. If the beneficiary dies before the specified period ends, a secondary beneficiary may receive the remainder of the payments.

- **Example:** \$100,000 death benefit – the beneficiary chooses to be paid \$10,000 per year. He or she will receive payments until the benefit is used up. The insurance will pay interest on the money that has not been paid so the payments will last longer than ten years.

## Interest Income

The beneficiary can choose to be paid only the interest earned on the death benefit (after the death of the insured). Interest payments will be made to the beneficiary, and the original death benefit can be paid at his or her death to a secondary beneficiary or when the beneficiary reaches a certain age.

- **Example:** \$100,000 death benefit – assume interest rate is 5 percent – beneficiary receives \$5,000 per year – when he or she dies, a secondary beneficiary receives \$100,000.

*Note: Except for the lump sum option, the above payment plans include death benefit (tax-free income) and interest (taxable income). Consult your tax advisor for more information on the taxes associated with these payments.*

## Conclusion

Depending on the beneficiary's situation, he or she may like one benefit option better than another. A life insurance agent, financial planner, financial counselor, or tax advisor may be able to help beneficiary understand the dollar amounts associated with each option. If you would like more information on benefit options, see Life and Health Insurance Foundation for Education (<http://www.life-line.org>), the American Council of Life Insurers (<http://www.acli.com>), and the Insurance Information Institute (<http://www.iii.org>).

## Definitions of Terms

**Beneficiary** – The person or entity receiving the death benefit at the death of the insured.

**Cash-value** – The amount of total premiums paid for a policy minus the costs for insurance in whole-, universal-, and variable universal-life policies. The cash-value grows tax-free in an insurance policy.

**Death Benefit** – The total cash payment made to the beneficiary upon the death of the insured.

**Insured** – The person on whose life the insurance has been purchased. If the insured dies, a death benefit will be paid to the named beneficiary.

**Disclaimer:** Insurance examples used in the publication are for illustrative purposes only. The numbers may not be estimates of an actual policy. Consult your insurance agent for actual insurance illustrations.