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How Much Life Insurance Do You Need?

In Canada, two out of every 1,000 persons age 40 are expected to die in any one year. No one can determine exactly which two will die. However, if all 1,000 paid $100 for the mutual protection, the two that did die would each leave their estate $50,000.

This is the basic premise on which insurance is based. The insurance companies act as the intermediary and holder of these funds until they are paid out. The premiums you pay are based on your perceived risk (age, health, occupation, etc) determined by extensive study on the part of the insurance companies and the amount and type of insurance you may wish to purchase.

Life insurance should be purchased with a view to providing your family with two basic forms of protection:
a) An amount to pay off debts and death-related expenses, and
b) A capital sum for investment to provide immediate and/or future income for your dependents.

How to Determine What Life Insurance You Need

How much will you need? Every individual is different. You have different income levels, different expenses, more or less financial assets built up already and so on. How much money will your family need? First they will need some money to bury you and pay off your debts. Second they will need some ongoing income to replace what you were providing. On page 4 and 5 you will find worksheets where you can fill in the appropriate amounts.

The first pool of cash will be needed to pay your last expenses and ease your family's way. A Last Expense fund should include money for the funeral, legal and accounting fees, and administration of your estate. An amount of $10,000 would be a basic minimum.

You may require a fund to pay any income taxes that are due on your death. If you have just employment income then there should be few additional taxes. If you own stocks or investment real estate, Revenue Canada assumes that you sold them the day that you died and there may be taxes owing on any capital gains.

From this first pool of cash you will have to pay off any debts that you have outstanding, including the mortgage. This will allow your family to continue with their lives without having to worry about continuing to pay for old debts. You may have mortgage or loan insurance to help pay for your debts, this amount should be listed below under What You Have Now.

If you have children that have not finished their education, then you should set up a fund for this purpose. If this amount is going to be funded as a result of your death, you can be generous. What was the ideal fulfillment of your goal of educating your children? Put that amount down for the education fund.

If you do not yet have an emergency fund then you can set money aside for this purpose from your estate. Life is going to be tough enough for your family, no need to burden them further by not having some cash available to pay for basic living expenses. Set aside between 3 to 6 months of expenses in this fund.

Total up the amount needed in this first pool of cash.

Next look at the continuing income requirements of your family. How much of your income will your family need to replace? How will your family replace this income? Do you expect your partner or children to get jobs or do you want to set aside a lump sum of capital that when invested will replace your income? How long do you want this lump sum of capital to last?

You can look at your Cash Flow Worksheet to see what you contribute towards the family expenses now. This can be reduced by a certain amount because the family will no longer have to feed and clothe you. To this amount you could add an amount for income taxes and subtract the amount of income your family will receive that they do not receive now (i.e. CPP Survivor and Orphan's benefits, or partner returning to work).

To determine the amount of capital needed to generate the desired monthly income, multiply the monthly income by the appropriate factor for the length of time you wish the income to continue from the following table.

Years Income Must Last	Multiply by
5	50
10	110
15	150
20	200
Lifetime	300

These factors are an estimate to determine the amount of capital required based on an interest rate of 5% and inflation of 2%.

Add this amount to the first pool of cash. This is the total amount of cash that you will have to leave behind for your beneficiaries.

How to Determine What You Have

Where will this money come from? It usually comes from two sources, the capital you have accumulated and life insurance. What capital do you already have? Look at your Net Worth Statement, put down what you already have saved in Liquid Assets, Investment Assets, Retirement Assets and Personal Assets (which your family would sell).

Second put down what you already have in life insurance. This may be group life insurance from work or an association, or life insurance on your loans or private life insurance that you have purchased in the past (do not include accident insurance, you cannot guarantee that you will die by way of accident). Add this amount to what you have saved already.

Subtract the amount that you have available upon death from what you require at death. This is the amount of additional life insurance that you require.

What Type of Life Insurance

Once you have determined how much, if any, life insurance is required, you must decide what type of insurance to carry. There are a multitude of products available. However, when all the window dressing is removed, there are really two types of coverage available, permanent (Whole Life) and temporary (Term).

Term insurance provides protection for a specified period of time. It may be one year, five years, 10 or 20 years, or to age 65 or 100. If you do not die within the specified period of time, there will be no payment. This is similar to your car insurance, if you do not have an accident; the insurance payments were "wasted".

Whole Life insurance provides for permanent protection. In other words, it will pay out **when** you die not only **if** you die within a certain time period.

The type you select will depend on your decision on the benefit provided versus the cost. While you are unemployed, you may want a term insurance policy to tide you over until your next job. Then you can apply for group life insurance through your new employer.

Insurance Planning Worksheet

Capital Required:

Cash Requirements			
Last Expense Fund	$________		
Income Taxes due	_________		
Mortgage and Other Loans	_________		
Education Fund	_________		
Emergency Fund	_________		
Total Cash Requirements			$________
Income Requirements			
Monthly Objective	$________		
Factor to produce required income	_________		
Total Income Requirements		$________	
Total Capital Required			$________

Capital Available:

Cash Available				
Liquid Assets		$________		
Investment Assets		_________		
Retirement Assets		_________		
Personal Assets to be sold		_________		
Total Cash Available			$________	
Insurance Available				
Group Life Insurance	$________			
Mortgage and Loan Insurance		_________		
Private Life Insurance	_________			
Total Insurance Available				$________
Total Capital Available				$________
Additional Capital Required			**$________**	

Insurance Planning Worksheet — Partner

Capital Required:

Cash Requirements

Last Expense Fund $________

Income Taxes due __________

Mortgage and Other Loans __________

Education Fund __________

Emergency Fund __________

Total Cash Requirements $________

Income Requirements

Monthly Objective $________

Factor to produce required income __________

Total Income Requirements $________

Total Capital Required $________

Capital Available:

Cash Available

Liquid Assets $________

Investment Assets __________

Retirement Assets __________

Personal Assets to be sold __________

Total Cash Available $________

Insurance Available

Group Life Insurance $________

Mortgage and Loan Insurance __________

Private Life Insurance __________

Total Insurance Available $________

Total Capital Available $________

Additional Capital Required **$________**