

Financial Underwriting Guidelines & Tips

Life Insurance is intended to protect against economic loss due to the unforeseen or premature death of the insured.

The purpose of financial underwriting is to determine whether the amount of coverage applied for and in force bears a reasonable relationship to this loss.

Income Replacement and Estate Conservation

Income replacement coverage establishes security against loss by providing funds to repay personal debt and continue income. In effect, the goal is to determine an amount that maintains the previous lifestyle. This amount is referred to as the Human Life Value. Traditionally, this value is calculated via a multiple of income approach. Income in this context would include salaries, wages, and bonuses. As income replacement needs diminish with age, estate conservation often becomes an issue. Life insurance proceeds are legitimately used to satisfy the, at times, significant costs associated with estate transfer, thereby avoiding a forced sale of assets at death. While the 100% marital deduction, which can be exercised on a first death, and the current \$1,500,000 exemption (*) complicate the underwriting approach, underwriters can comfortably estimate estate liabilities at 50% of the gross estate on substantial net worths. This formula can be limiting in that the anticipated growth in value of the estate's assets are not considered. * Federal estate Tax Unified Credit for years 2004 – 2005.

Income replacement and estate conservation needs may be considered concurrently. The primary focus is income, augmented by net worth when indicated. The basic formula is:

Income x Multiple for Age, or Current Net Worth (whichever is greater)

Use the Multiple of Income by Age, table to calculate the amount of insurance that SBLI generally considers to be reasonable for married applicants. For those who are single, just use one-half of the amount calculated.

Age	Multiple of Annual Earned Income ¹
To age 40	Up to 20 x salary
41-55	15 x salary
56-60	10 x salary
Age 61 and up	5 x salary
Table 17: Multiple of Income by Age	

¹Occupations with fluctuating income levels require close analysis. Reduced multiples should be considered in those instances where reported income figures may be suspect, sources may not be knowledgeable, the applicant is new to the occupation, changes occupation frequently, or the occupation itself has little potential for growth.

Estate Conservation

- As income replacement needs diminish with age estate conservation often becomes an issue.

Key: IT MUST MAKE SENSE!!

Personal Creditor Insurance

- Used to repay outstanding indebtedness on the death of the debtor. Rules of thumb:
- Provide the amount and purpose of the loan and terms of repayment.
- Generally, we will insure 80% of the loan.
- Collateral assignment form is required.

Personal Bankruptcy

- Individuals petition the courts for bankruptcy relief under Chapter 13 or Chapter 7 of the code. Rules of thumb:
- Generally, cases involving bankruptcies will not be considered until the bankruptcy has been resolved for at least 2 years.
- Underwriting may ask for copies of the bankruptcy petition and/or final discharge papers.

Juvenile Insurance

- There should be a relationship between the amount applied for and the parent's insurance program. General guidelines:
- Limit this amount to a maximum of 50% of the breadwinner's insurance amount.
- Insurable Interest is generally limited to parents.
- All juvenile siblings should have similar amounts of coverage.

Charitable Giving

- The use of life insurance in charitable giving is most often simply an attempt to provide an uninterrupted continuation of an existing pattern of giving.
- Generally, annual contribution x 10 = Charitable amount of life insurance.

Business Insurance

Life Insurance is often used to alleviate the financial strain caused by the death of an owner or key employee.

Purpose: To maintain the same financial position that existed prior to the loss, not to enhance the financial position of the organization.

Among the forms business insurance takes on, the more common are

1. Buy/Sell
2. Key Employee (AKA – Key Man)

Buy/Sell:

- Identification of major owners and their respective ownership positions are required.
- A determination, and how arrived at, of the Book Value and/or Market Value of the business should be provided.
- Partners or owners are normally insured in proportion to their percentage ownership.

Key Employee (Key Man):

- Purpose of this coverage is to protect the company against economic loss and facilitate replacement in the event of the untimely death of a key person. There is no benefit to the insured's heirs as there is in Buy/Sell.
- A Key Employee is defined as someone who:
 - possesses special skills
 - is a source of business for the firm
 - holds a patent in his/her name
 - his/her name and personal reputation in the industry carries a value for the company
 - individuals who have partial ownership in the business
 - highly paid individuals
- 3 – 5 times the employee's salary is generally considered a reasonable amount of coverage.
- Amounts in excess of this may be justified when extenuating circumstances exist. Explanation is required.

Business Loan (Creditor) Insurance:

- Lenders may insist on coverage of owners to pay outstanding principle balance due to owner's premature death.
- Beneficiary should be the creditor, as their interest may appear.
- Underwriting may ask for documentation of the loan.
- Collateral assignment form is required.