eQ Insight

How to buy protection insurance

to protect yourself and your family

Protection should always be considered as part of an effective financial plan. Nobody knows what the future holds and uncertainty can be scary.

Financial planning is about giving ourselves the best chance of achieving our financial goals, and at the same time preparing for any unexpected bad times.

This guide explains the major types of protection insurance, and offers a step-by-step guide on how to buy them.

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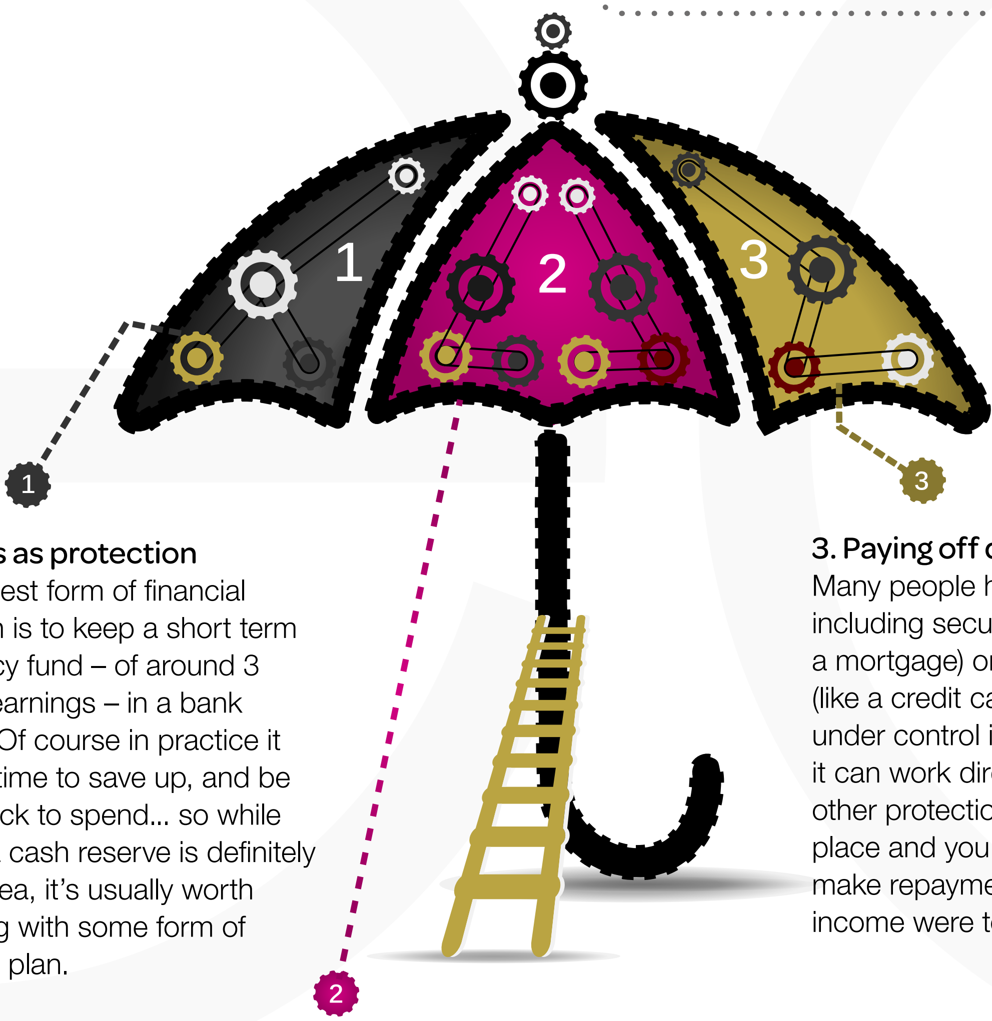
eQ investors

3 steps to financial security

Before we jump into considering specific types of insurance, it's important to see protection as part of a bigger picture. At the very least, there are three things you can do which should all work together to build financial security:

When it comes to protection, ask your financial adviser for help!

Your financial planner should be able to consider your protection needs as part of your overall financial plan: they will have all the information at hand to complete a thorough assessment of your needs, should know what questions to ask to guide you through the process, and can often access better deals than you can find online, by using specialist brokers.



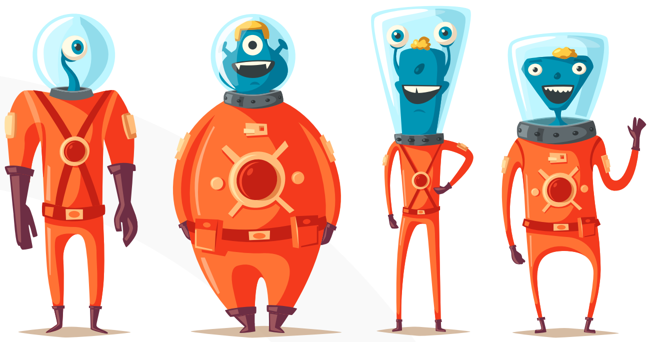
1. Savings as protection
The simplest form of financial protection is to keep a short term emergency fund – of around 3 months' earnings – in a bank account. Of course in practice it can take time to save up, and be all too quick to spend... so while keeping a cash reserve is definitely a good idea, it's usually worth combining with some form of insurance plan.

2. Protection insurance
The subject of this guide: protection insurance is all about safeguarding yourself and your family from harm. Read on to learn about some common insurance myths, the main types available, and the right way to buy them.

3. Paying off debts
Many people have debts, including secured debt (such as a mortgage) or unsecured debt (like a credit card). Keeping debt under control is critical because it can work directly against any other protection you have put in place and you will still have to make repayments even if your income were to fall.

5 myths about insurance

Unfortunately, many people are put off protection insurance for the wrong reasons. Let's separate fact from fiction:



"I'll never need it"

In truth, none of us knows what the future holds, and our health has a huge impact on how we live our lives:

- Approximately 1 in 4 people in the UK experience a mental health problem each year (Source: Mind)
- 1 in 2 people in the UK born after 1960 will be diagnosed with some form of cancer during their lifetime. (Source: Cancer Research)
- Almost 1 in 5 people in England and Wales have a health problem or disability that limits their activity (Source: ONS)

"I can't afford it"

Putting in place a basic level of protection is probably cheaper than you think – e.g. you can buy some life insurance cover for just a few pounds a month.

If you follow the steps in this guide to work out the cover you need and how much it actually costs, you should be able to find a level of protection that is affordable for you, provides real financial security, and offers invaluable peace of mind.

"Insurers seldom pay out"

This is not the case. According to official statistics from the Association of British Insurers, insurers paid out a record £5 billion in protection claims in 2017 – an increase of more than £340 million from the previous year – and virtually all protection insurance claims were paid (97.8% to be exact).

"The state will take care of me"

If you currently earn a living and something happened to you that meant you were unable to work, the state will not replace your income.

You might be eligible for Employment and Support Allowance, but payments range from around £70 to just over £100 a week (depending on your circumstances and the seriousness of your illness or disability) – which is nowhere near enough for most people to live on.

If your spouse or civil partner has died you may be able to claim bereavement benefits to help ease some of the financial worries you may be facing.

"It doesn't matter if you don't tell your insurer everything"

In cases where protection claims were not paid, it was usually because the insurer didn't know something important – usually about the claimant's medical history – which invalidated the policy.

Common reasons people don't disclose relevant information include:

- Waiting for a test result
- They are/were a social smoker
- Unsure how much alcohol they drink
- Answered for their partner who wasn't present
- Embarrassed to discuss an issue in front of a partner
- Didn't think it was relevant.

The golden rule is that if you're not sure about something, it's always best to tell your insurer.

Protection insurance: what's available?

Many people have heard of life insurance, but may not understand that there are different types – as well as other types of protection insurance that all do different things. Here's a quick overview:

Term assurance

What is it?

The simplest and cheapest form of life insurance is designed to help your dependants cope financially if you were to die unexpectedly. It does this by paying out a lump sum – known as the 'sum assured'. Insurance cover lasts for a pre-determined length of time – known as the 'term' – during which you will pay regular premiums.

Premiums depend on the sum assured, the length of the term, and individual lifestyle factors such as your age and health. Premiums either stay the same or rise with inflation. Joint policies may pay out when the first partner dies, or on the death of the surviving spouse.

Why buy it?

This sum assured can either stay the same or decrease over time. In the first instance, a level sum would provide your family with a certain amount of financial security if you died. A decreasing term assurance is commonly used to cover the outstanding balance on a mortgage that is being repaid.

Who benefits?

A lump sum will be paid directly to your chosen beneficiaries. When you buy term assurance you usually have the option for the sum assured to be paid into a trust, in order to exclude it from your estate for inheritance tax purposes.

Family income benefit

What is it?

This is a variation on term assurance that is designed to cover regular monthly expenses for your family if you died. Instead of paying a lump sum, it guarantees a regular monthly income for the remaining term.

Why buy it?

If you have children or other dependants, you may want insurance to cover the ongoing cost of childcare, school fees, or other living expenses – until, for example, your children reach adulthood.

Who benefits?

If you died, your family would receive a regular, tax-free, monthly income for the rest of the policy's term. You can decide whether you want the income to stay level or to increase with inflation.

Income protection insurance

What is it?

This type of insurance pays out a pre-agreed percentage of your salary if you are unable to work due to illness or injury. Cover is usually limited to a maximum of 50-65% of your current gross earnings, and may be level or linked to inflation. Premiums can be guaranteed or reviewable.

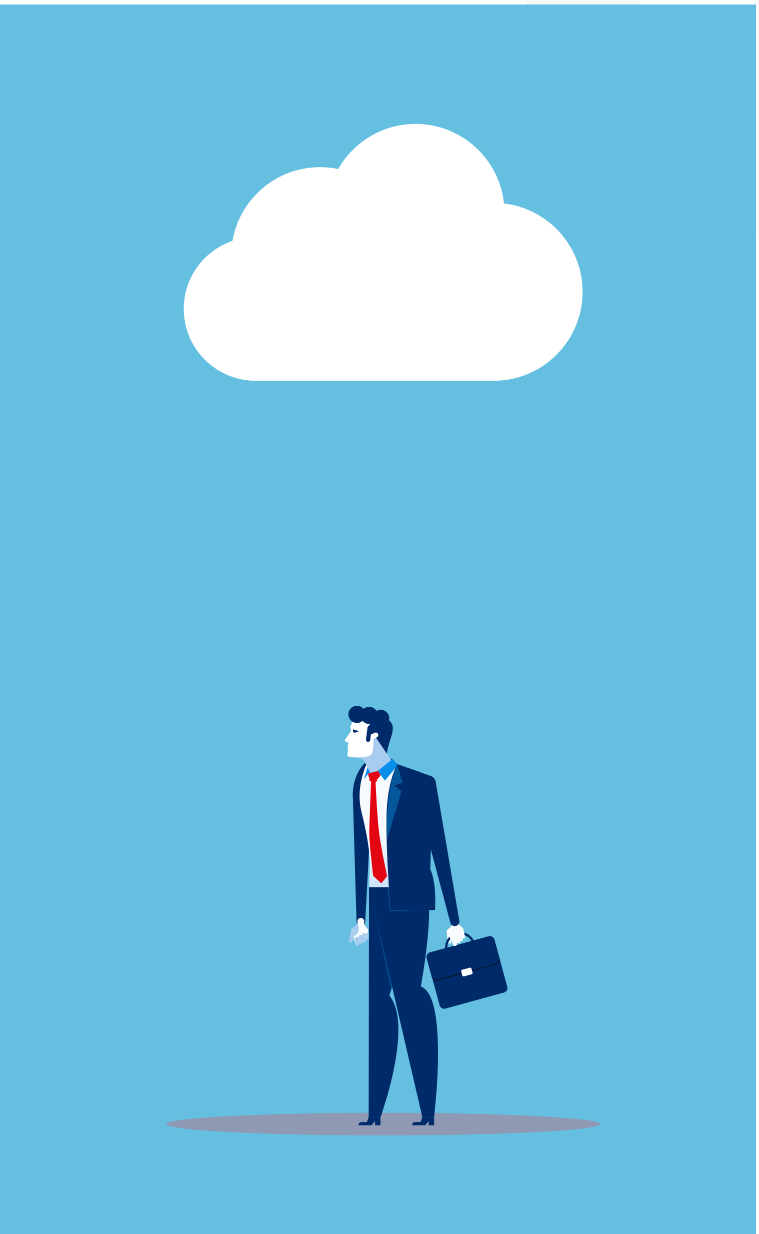
Some plans pay out for a set period of time. Others continue to pay out until you return to work or retire.

Why buy it?

If you don't have dependants this is usually the most important type of cover to have – the chances of being signed off work due to illness or injury are much higher than those of death, and state benefits are unlikely to be enough to cover your monthly essential living expenses.

Who benefits?

You – the plan will pay you a tax-free monthly income. There is a pre-agreed waiting period before the income starts (often 1, 2, 3, 6, 12 or 24 months). You should consider any existing benefits offered by your employer – the longer the waiting period, the lower the premium. Most employers will only provide sick pay for short periods, and premiums must continue to be paid during the waiting period.



Critical illness cover

What is it?

This is an insurance plan that pays you a lump sum of money if you are diagnosed with a serious illness. It only applies to a specific list of health conditions or illnesses, and does not include mental health conditions. Not all conditions are covered by all plans, so it is even more important to obtain professional advice for this type of cover.

Why buy it?

Serious illness can happen to anyone, and can cause financial hardship at a time of terrible emotional stress. Critical illness cover can help by ensuring that, e.g. the mortgage is paid off, or by providing a lump sum for private medical treatment.

Who benefits?

You and your family: if you are diagnosed with a serious illness, the plan will pay you a tax-free lump sum to help you cope.

Whole-of-life insurance

What is it?

As suggested by the name, this type of insurance lasts for the rest of your life (assuming the premiums continue to be paid) – guaranteeing that your dependants will receive the sum assured when you die. As it is open-ended, the premiums are normally a lot higher than for term assurance, and it is common for premiums to increase every ten years.

Why buy it?

This type of protection is usually used to cover an inheritance tax liability, forming part of a larger financial plan for your estate. Unlike Term Assurance there can be an investment element to these policies, and a surrender value (although cover stops if the plan is surrendered).

Inheritance tax planning is a complex subject, beyond the scope of this guide. If you are concerned about this then please contact EQ to speak to a qualified financial adviser.

Who benefits?

As with term assurance, whole-of-life plans pay a tax-free guaranteed lump sum to a beneficiary or trust, and can be held in single or joint names.

How to buy protection insurance: step-by-step

1 Decide what kind of protection you need

Our needs change over time, and it's no different with insurance. Here are some typical scenarios:

Young adult – Income protection to cover loss of earnings.

Home owner – Critical illness cover to pay off your mortgage.

Parent – In addition to the above, life insurance should be put in place to protect your family.

Later years – The need for income protection and life insurance decreases as children become independent, mortgages are paid off, and you accumulate savings for retirement. Inheritance tax protection may be an important consideration.

Working with an expert

Buying insurance through a financial planner can save you time and money. But it's important to ask the right questions. They should be able to give you good answers to the following:

- What kind of cover do I need?
- How much cover do I need?
- How did you work this out?
- How long do I need the cover?

2 Calculate how much cover you need

To work out your income protection needs, add up your household expenses, childcare costs, school fees, and any other essential monthly outgoings.

To calculate a lump sum for life insurance and critical illness cover, consider your current household earnings, any outstanding mortgage balance, credit cards or personal loans. A good rule of thumb is ten times your highest earner's salary, plus any outstanding debts.

Remember to check and subtract any cover you already have. If you're employed, check whether your employment benefits package includes 'death in service' cover (i.e. life insurance) or income protection.

3 Shop around

There are a host of online sites that offer price comparisons on protection insurance. But, as the saying goes, let the buyer beware!

- Price comparison websites make profits from commission (just like insurance brokers).
- Insurers often don't publicise their best deals online.
- Your financial planner may be able to negotiate a better deal for you.

4 Before you buy

It's important to read the small print. Insurance policies may not make for a good read, but you need to make sure that your cover provides you with the right level of protection.

Questions to ask before you buy

- Are there any policy exclusions? (Under what circumstances might the insurer not pay out?)
- Will I need to undergo a medical examination?
- What happens when my policy ends?
- What if I can't afford the monthly payments?

5 After you buy

Perhaps the most important thing to do as soon as you buy any kind of insurance cover is to set a calendar reminder – to check your cover in a year! If your circumstances change, you may need to update your cover to keep it relevant.

Here are some examples of common life events that are likely to change your insurance needs:

- Moving house, buying or selling property.
- Getting a new job, becoming self-employed, getting a pay rise, retiring or selling your business.
- Getting married (or divorced), having children (or grandchildren), having a child leaving home.
- A change in health (either yours or your partner's).
- Paying off a debt or loan (including your mortgage).
- Making a financial gift from your estate.

At EQ, your financial planner will review your protection cover at each annual financial review or life event. If your circumstances have changed, they will explain what (if any) changes you should make to your protection cover, and why. That way, you can rest assured that you and your family have the right level of protection in place.

How EQ can help

There is no ‘one size fits all’ approach with protection planning and it can be an emotional and complex matter. It is important that your insurance plan or life cover is tailored to you and your needs. To ensure this happens, why not talk to one of our financial advisers?

They will get to know you and your family’s personal and financial circumstances, working with you to establish what you need from a protection plan.

There are lots of policies available on the market, and the sheer number of options can be overwhelming. Your needs are also likely to change as your family, work and life circumstances change too.

That’s why we offer protection planning as part of our ongoing financial planning service, in addition to providing one-off advice.

If you’re looking for protection insurance, do get in touch and we’ll be happy to help.

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This guide provides general information about protection insurance and is not a personal recommendation. If you are unsure whether protection insurance is right for you or what level of cover might be appropriate, please call 020 7488 7110 to speak to a qualified financial planner.