

RETIREMENT | FEATURE

Whole Life Insurance Can Bolster Your Retirement Portfolio. Here's How to Use It.



By Neal Templin
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DREAMSTIME

The 401(k) revolution has turned millions of American workers into their own pension plan managers. Now, as a growing number of these workers retire, they must convert their investment portfolios into regular income.

It isn't easy. [Retirees can't depend upon bonds for income](#) because yields are so low. But if they bet too big on equities, their [savings could get savaged in a](#)

[market downturn](#), crimping their retirement.

Enter whole life insurance. Whole life insurance has been derided for years because of high premiums and complexities. Buy cheaper term insurance and invest the rest, the conventional wisdom goes.

But a number of academics say that whole life, a form of permanent life insurance that builds cash value, can buttress investment portfolios and even boost retirement income if used correctly. They say that its stable growth allows consumers to pursue higher-risk, higher-return strategies with their other investments, while leaving more money to their heirs through the policy's death benefit.

Wade Pfau, a professor of retirement income at the American College of Financial Services, compared a 40-year-old who buys term insurance and makes a large 401(k) contribution with an identical worker who buys a \$500,000 whole life policy and makes a smaller contribution to his 401(k). Because the worker with whole life is building cash value in his policy, he or she can safely allocate a higher percentage of the 401(k) to equities than the other worker, Pfau says.

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The upshot: At age 65, the worker with the whole life policy has a 401(k) account that is equal in size to the other worker in a buoyant market and 17% smaller in a

bad market. In either scenario, Pfau calculates, the worker with whole life comes out ahead because he has \$210,000 in cash value that he can borrow against in retirement.

Retirees can use this money to avoid tapping their retirement portfolios during bear markets. "You don't have to spend during downturns," Pfau says. (The College of Financial Services receives funding from the financial industry, including insurers, but says it's a fully accredited university and its research is independent. Pfau, who has done work for the insurance industry, says he is transparent about the assumptions used in his whole life calculations.)

If you're interested in buying a whole life policy, here are a few things to keep in mind:

How whole life insurance works: When you buy a whole life policy, you are buying both life insurance and a tax-free savings vehicle. Each year a growing part of your premium goes into the savings vehicle. The cash balance in it grows tax-free at an interest rate guaranteed by the insurer.

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Most whole life insurance is sold by mutual companies such as Mass Mutual, Northwestern Mutual, and New York Life. They have a long history of paying dividends to policyholders on top of the guarantees. The dividends end up

increasing both your cash balance and your death benefit.

You can tap the cash value by taking loans out against it. The loans are tax-free and don't have to be repaid but reduce the death benefit your heirs will receive.

Don't wait too long to buy whole life: The sweet spot for buying whole life is from age 35 to 45. That gives of time for the cash value to build up before retirement. In addition, people that age are unlikely to be rejected by the insurer because of health issues, and premiums are cheaper because insurers expect them to be around for a long time.

Buy whole life and term insurance: Because it contains a savings component and lasts your entire life, whole life is far more expensive than term insurance, which provides a death benefit only for a certain period of time. That means if you rely upon whole life for coverage, you may have trouble affording adequate insurance for your family,

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David Babbel, a retired insurance professor from the Wharton School of the University of Pennsylvania, advises consumers to buy both types of insurance. The whole life policy will be in effect for your entire life. The term insurance is for your work life, and protects your family from the loss of income if you die. As you near retirement, you can let the term insurance expire and keep the whole-life

policy in place.

Pricing for whole life is opaque: If you want to buy term insurance, you can go on the internet and quickly look at quotes. You may have to go through a health exam before getting the policy, but buying term insurance is simple and transparent.

Not so with whole life. You'll probably have to go through an insurance agent to get a quote. The agent gets a commission of up to a year's premium for selling a policy, so he or she is not exactly independent.

Whole life insurance is a complicated product, and a good agent should be able to explain all the nuances. There are three main financial variables: the size of the premium, the size of the death benefit, and how quickly it builds cash value.

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An advertisement for a virtual event. The background is dark with blue and purple geometric shapes. On the left, there is a white circle containing the Dynatrace logo (a square with a circle inside) and the word "Perform" in a large, bold font. Below "Perform" are the words "TRANSFORM" and "FASTER" in a smaller font. On the right, the text reads "A live virtual event to change the way you work" in a bold font, followed by "Feb. 8 - 11". At the bottom right, there is a blue button with the text "Register free". A small "X" icon is in the top right corner of the ad.

If you're concerned about the biggest possible death benefit for the smallest possible premium, insurers will sell you a policy that does that but builds cash value slowly. If you want to build cash value as quickly as possible, the insurer will give you a policy with bigger premiums.

Whole life can help you get more lucrative annuity payouts: In today's world of low interest rates, some financial experts recommend that retirees buy lifetime

income annuities to provide a bigger stream of retirement income. Married couples typically purchase joint survivorship annuities so that the money will keep coming after one of them dies. The joint annuities, because they pay until the second spouse dies, have lower payout rates.

But if you have a whole life policy, you can responsibly buy a single-life annuity with a higher payout because you know your spouse will receive money from the whole life policy when you die.

Universal life or variable life don't offer the same protection: Insurers sell other permanent insurance products in which the cash value growth can fluctuate because of market conditions or how the insurer performs.

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That makes them different propositions than whole life where your interest and annual premium is guaranteed for the life of the policy by the insurer.

"The difference between whole life and universal life is the transfer of risk from the company to the insured," says Jason Sanger, a Madison, Wis., insurance agent who sells software to optimize the use of whole life policies in financial plans.

If markets underperform or the insurer underperforms, such policies can lose

value and even lapse in certain situations, Sanger says.

· **Whole life is insurance for market downturns:** A whole life policy provides an emergency reserve to protect you from having to sell assets during a down market.

Jeff Miller, a Northwestern Mutual wealth management adviser, points to a client who retired in 2007 and saw his stock-heavy portfolio fall by about half during the 2007-09 recession. For 16 months, Miller says, the client drew down the cash value of his life insurance policy to support his monthly budget. "It was not the time to be selling equities," Miller says.

He didn't resume taking money out of his investment portfolio until the market had recovered much of its losses, Miller says, something that might not have been possible without the cash cushion.

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