

7 LIFE INSURANCE

People buy life insurance to protect their dependents against financial hardship when the insured person, the policyholder, dies. Many life insurance products also allow policyholders to accumulate savings that can be used in a time of financial need. Most American families depend on life insurance to provide this economic protection: Sixty-nine percent owned some type of life insurance in 2001, according to the Federal Reserve's analysis of its *Survey of Consumer Finances*.

Americans purchased \$3.1 trillion of new life insurance coverage in 2004, 5 percent more than in 2003 (Table 7.1). By the end of 2004, total life insurance coverage in the United States reached \$17.5 trillion (Figure 7.1), an increase of 3 percent from 2003.

Three types of life insurance policies predominate the market. *Individual insurance* is underwritten separately for each individual who seeks insurance protection. *Group insurance* is underwritten on a group as a whole, such as the employees of a company or the members of an organization. *Credit insurance* guarantees payment of some debt, such as a mortgage or other loan, in the event the insured person dies, and can be bought on either an individual or a group basis. Insurance on loans of 10 years' or less duration is classified as credit insurance in National Association of Insurance Commissioners accounts; insurance on longer loans is included in individual or group policy data in this chapter. Life insurance policies offered by fraternal benefit societies are considered individual insurance.

Table 7.1**Life Insurance in the United States**

	1994	2003	2004	Average annual percent change	
				1994/2004	2003/2004
Life Insurance purchases					
Face amount (millions)					
Individual ¹	\$1,057,233	\$1,772,673	\$1,846,384	7.5	4.2
Credit	NA	122,928	151,432	NA	23.2
Group	560,232	1,050,318	1,101,599	9.7	4.9
Total	1,617,465	2,945,920	3,099,415	9.2	5.2
Policies (thousands)					
Individual	13,835	13,821	12,581	-0.9	-9.0
Credit	NA	17,126	15,402	NA	-10.1
Group (certificates)	18,390	21,946	25,872	4.1	17.9
Total	32,225	52,893	53,856	6.7	1.8
Life insurance in force					
Face amount (millions)					
Individual	\$6,448,758	\$9,654,731	\$9,717,377	5.1	0.6
Credit	189,398	152,739	160,371	-1.5	5.0
Group	4,443,179	7,236,191	7,630,503	7.2	5.4
Total	11,081,335	17,043,661	17,508,252	5.8	2.7
Policies (thousands)					
Individual	169,000	175,936	167,741	-0.1	-4.7
Credit	52,000	39,992	39,483	-2.4	-1.3
Group (certificates)	145,000	162,690	165,476	1.4	1.7
Total	366,000	378,619	372,700	0.2	-1.6

Source: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission.

Notes: NAIC does not endorse any analysis or conclusions based on use of its data. Data represent direct business of U.S. life insurers and, as of 2003, fraternal benefit societies.

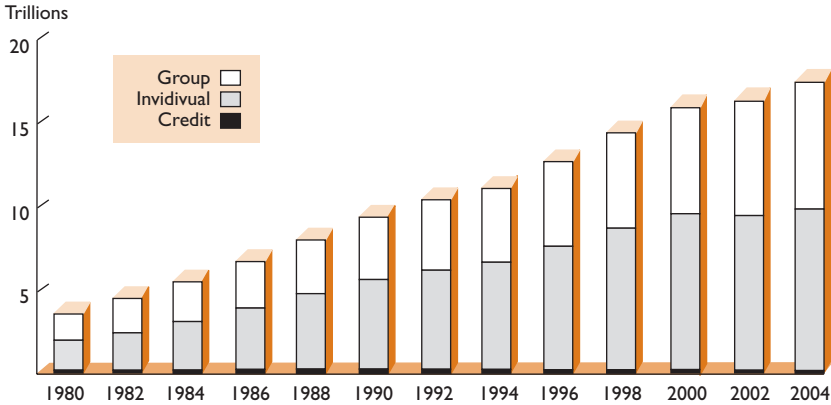
¹Policies issued by fraternal benefits societies are considered individual business.

NA: Not available.

Individual Life Insurance

Individual life is the most widely used form of life insurance protection—56 percent of all life insurance in force in the United States at year-end 2004 (Table 7.1). Typically purchased through life insurance agents, this insurance is issued under individual policies with face amounts as low as \$1,000, although larger minimum amounts are more typical in today's market. While individual life is principally used for family protection, it also is widely used for business purposes. A business may purchase life insurance to protect against the economic loss that would result from the death of the owner or a key employee.

Figure 7.1 Individual, Group, and Credit Life Insurance in Force in the United States (face amount)



Source: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission.
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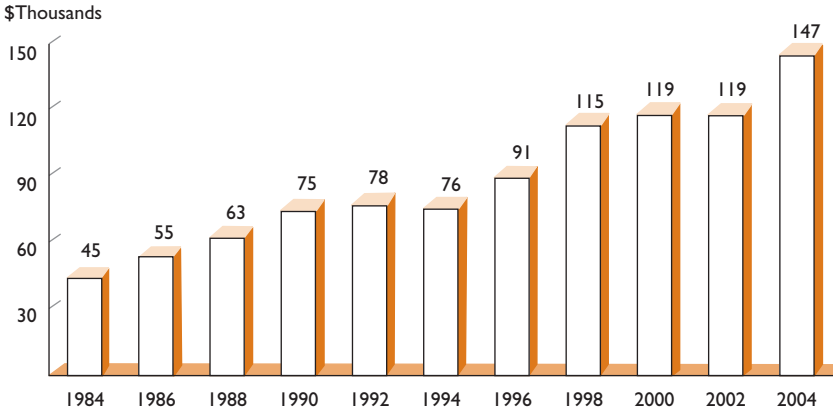
Individual life insurance protection in the United States totaled \$9.7 trillion at the end of 2004 and has grown at an average annual rate of 5 percent since 1994, when \$6.4 trillion was in force (Table 7.1).

The size of newly purchased individual life policies also grew in 2004 (Figure 7.2). The average, new individual life policy increased 14 percent to \$147,000. The number of individual policies purchased, however, fell 9 percent in 2004 (Table 7.1).

Individual life policies offer two basic types of protection: covering a specified term, or permanently covering one’s whole life.

Figure 7.2

Average Face Amount of Individual Life Insurance Policy Purchased



Source: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission.

Notes: NAIC does not endorse any analysis or conclusions based on use of its data. Data represent U.S. life insurers, and, as of 2003, fraternal benefit societies.

Types of Policies

Term Insurance

Term insurance policies provide life insurance coverage for a specified period, usually greater than one year. Term policies provide no further benefits when the term expires, and no buildup of cash value occurs. If this insurance is not renewed at the end of its term, coverage lapses and no payment would be made to the beneficiary in the event of death.

Of new individual life policies purchased in 2004, 41 percent, or 5 million, were term insurance (Table 7.2), totaling \$1.3 trillion, or 70 percent, of the individual life face amount issued. The most popular form of term insurance is level term, which offers a fixed premium.

Permanent Insurance

Unlike term insurance, permanent life (or *whole life*) insurance provides protection for as long as the insured lives. Permanent life policies also have a savings component, building cash value that can help families meet financial emergencies, pay for special goals, or provide income for retirement years.

Table 7.2 Individual Life Insurance Purchases, by Plan Type, 2004

	Policies in thousands/Amounts in millions			
	Policies	Percent	Face amount	Percent
Term insurance				
Decreasing	144	1.1	\$36,842	2.0
Level	5,076	40.3	1,165,857	63.1
Decreasing other term ¹	NA	NA	5,612	0.3
Level other term ²	NA	NA	86,676	4.7
Term additions	NA	NA	1,320	0.1
Total	5,220	41.5	1,296,306	70.2
Whole life and endowment	7,039	55.9	524,742	28.4
Not elsewhere classified	323	2.6	25,336	1.4
Aggregate total³	12,581	100.0	1,846,384	100.0

Source: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission.

Note: NAIC does not endorse any analysis or conclusions based on use of its data.

NA: Not available

¹Includes decreasing term insurance on spouses and children under family policies.

²Includes level term insurance on spouses and children under family policies.

³Does not include fraternal benefit societies.

The annual premium for traditional whole life policies remains constant throughout the life of the policy. In earlier years, the premium is higher than the actual cost of the insurance, but in later years it becomes substantially lower than the actual cost of protection. The excess amount of each premium in the early years is held in reserve as the policy's cash value. This cash value grows over time from investment earnings and future premium payments, providing funds for the cost of coverage as the insured grows older. If a policyholder decides to give up the insurance protection, he or she receives the cash value upon surrendering the policy, less any outstanding policy loans.

In 2004, direct purchases of permanent life constituted 56 percent of U.S. individual life insurance policies issued and 28 percent of the total face amount issued (Table 7.2).

Participating and Nonparticipating Insurance

Traditional whole life and term insurance policies can be purchased on a participating or nonparticipating basis. A participating policy allows the policyholder to share in the insurance company's surplus. With this type of life insurance, a

Table 7.3 Life Insurance Purchases, by Participating Status

	Individual		Credit		Group		Total	
	Face amount (millions)	Percent	Face amount (millions)	Percent	Face amount (millions)	Percent	Face amount (millions)	Percent
1995¹								
Nonparticipating	\$752,504	65.2	\$472,016	92.8	\$359,394	66.8	\$1,583,915	72.0
Participating	401,737	34.8	36,366	7.2	178,691	33.2	616,794	28.0
Total	1,154,241	100.0	508,382	100.0	538,085	100.0	2,200,709	100.0
2003								
Nonparticipating	\$1,383,062	78.0	\$100,487	81.7	\$854,204	81.3	\$2,337,753	79.4
Participating	365,983	22.0	22,441	18.3	196,114	18.7	608,166	20.6
Total	1,749,046	100.0	122,928	100.0	1,050,318	100.0	2,945,920	100.0
2004								
Nonparticipating	\$1,449,640	78.5	\$129,152	85.3	\$900,948	81.8	\$2,479,739	80.0
Participating	396,745	21.5	22,280	14.7	200,651	18.2	619,676	20.0
Total	1,846,384	100.0	151,432	100.0	1,101,599	100.0	3,099,415	100.0

Source: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission.

Notes: NAIC does not endorse any analysis or conclusions based on use of its data. Data represent U.S. life insurers and, as of 2003, fraternal benefit societies.

¹Data for 1994 is unavailable.

Table 7.4 Voluntary Termination Rates for Life Insurance Policies (percent)

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Individual	9.3	8.5	8.8	8.3	8.2	9.4	7.7	8.6	7.6	7.0
Credit	19.5	18.3	17.4	16.5	16.8	14.5	19.4	19.3	17.1	16.2
Group	7.2	7.1	7.7	7.5	8.6	9.3	11.7	9.2	9.0	9.7

Source: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission.

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policyholder receives annual dividends representing that portion of the premium not needed by the company for death payments to beneficiaries, additions to reserves, or administrative expenses. Four-fifths of individual life policies purchased were nonparticipating at \$1.4 trillion (79%) in 2004 (Table 7.3).

Table 7.5**Life Insurance With Disability Provisions, 2004**

	Policies and certificates in thousands/Amounts in millions			
	Policies	Percent of of policies in force	Face amount	Percent of face amount in force
Individual^{1,2}				
Waiver of premium	42,085	25.1	\$7,620,984	78.4
Disability income	19,788	11.8	20,435	0.2
Extended benefits	0	0.0	0	0.0
Other	5,353	3.2	40,960	0.4
Total	67,227	40.1	7,682,380	79.1
Credit³				
Waiver of premium	46	0.1	1,570	1.0
Disability income	1,424	3.6	7,497	4.7
Extended benefits	24	0.1	158	0.1
Total	1,494	3.8	9,225	5.8
Group⁴				
Waiver of premium	37,900	22.9	4,434,060	58.1
Disability income	825	0.5	38,533	0.5
Extended benefits	2,579	1.6	228,325	3.0
Other	355	0.2	173,340	2.3
Total	41,659	25.2	4,874,258	63.9

Source: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission.

Notes: NAIC does not endorse any analysis or conclusions based on use of its data. Data represent U.S. life insurers and, as of 2003, fraternal benefit societies.

¹Does not include fraternal benefit societies.

²Policies in force totaled 168 million, with a face amount of \$9.7 trillion.

³Policies in force totaled 39 million, with a face amount of \$160 billion.

⁴Certificates in force totaled 165 million, with a face amount of \$7.6 trillion.

Characteristics of Individual Policies

Lapses and Surrenders

A policy lapses if its premium is not paid by the end of a specified time, often called the *grace period*. Policyholders have different reasons for terminating their policies, sometimes using cash values to address financial emergencies or achieve long-term goals. Rates of voluntary policy termination by policyholders vary considerably among life insurers. Each company's rate depends on many factors, including the types of policies written and the ratio of new policies to older ones in force with the company.

Over the past nine years, the voluntary termination rate of individual life insurance policies has been declining, having reached 7.0 percent by 2004 (Table 7.4).

The life insurance business vigorously seeks to minimize the lapsing of policies. For example, agent training focuses on realistic identification of clients' life insurance needs, and careful analysis of the use of family income for protection. Since the voluntary termination rate is higher for policies on which loans are outstanding, companies urge that loans be used only in genuine financial emergencies, and that they be repaid promptly.

Most insurers offer policyholders time after their policy is delivered to consider whether to keep the policy. These companies will refund the premium in full if, within the prescribed time, the policyholder decides not to keep his or her policy.

Some policies that lapse still have a cash value, entitling the policyholder to some form of payment under a cash surrender value *non forfeiture option*. All coverage under the policy terminates at the time of the surrender.

Disability Provisions

Besides the benefit payable upon death of the insured, many life insurance policies or policy riders provide disability benefits to cover financial losses that result from a sickness or injury. The most common supplementary benefit is waiver of premium. Of individual life policies in force in 2004, 25 percent, or 42 million, allowed the premium to be waived during disability (Table 7.5), representing \$8 trillion, or 78 percent, of the individual life face amount in force.

GROUP LIFE INSURANCE

Group life insurance is a contract between an insurance company and some group to insure all of the group's members, usually under term coverage. Common examples are employer-provided life insurance and insurance offered through unions and professional associations. Employees or other group members receive certificates denoting their participation in the group coverage. In 2004, group insurance represented 44 percent of all life insurance in force.

Group purchases rose 5 percent in 2004 to \$1.1 trillion (Table 7.1). At the end of 2004, group life insurance provided \$7.6 trillion of protection, 5 percent more than a year earlier.

Group insurance contracts can provide benefits beyond term insurance. Employees often can retain coverage after retirement by paying premiums directly to the insurer. Many policies also offer survivor benefits, usually continuing monthly payments to the spouse of an employee who dies before retirement; payments may extend for life or to the age at which Social Security retirement payments become available, but cease on remarriage. Contingent benefits to dependent children in the event of a spouse's death are available as well. The initial value of these survivor benefits can range from three to 10 times an employee's annual salary.

As with individual life policies, group policies can be purchased on either a participating or nonparticipating basis. Most group life policies are nonparticipating (Table 7.3)—85 percent of those purchased in 2004, at \$901 billion.

Over the past nine years, the voluntary termination rate of group life insurance policies has generally been rising. The 2004 rate of 9.7 percent is up from the 9.0 rate a year earlier (Table 7.4).

Group policies also provide disability benefits (Table 7.5). Of group life policies in force in 2004, 23 percent, or 38 million, provided for waiver of premium, comprising 58 percent of the group life face amount in force at \$4.4 trillion.

CREDIT LIFE INSURANCE

Credit life insurance pays the balance on loans of 10 years' or less duration if the borrower dies before repaying the amount due. At year-end 2004, \$160 billion of credit life insurance was in force, up 5 percent from the previous year (Table 7.1).

Credit life, commonly part of consumer credit contracts, is term insurance, generally decreasing in amount as a loan is repaid. It protects the borrower's family, as well as the lender, against unpaid debt that may be left at death. Life insurers issue credit insurance through lenders such as banks, finance companies, credit unions, and retailers, who in turn make arrangements with borrowers.

As with other life policies, credit policies can be purchased on either a participating or nonparticipating basis. Of credit life policies purchased in 2004, 85 percent, or \$129 billion, were nonparticipating (Table 7.3).

Table 7.6**New Policy Claims Resisted or Compromised
(thousands)**

	2000 ¹	2003	2004
New claims in dispute	\$172,714	\$266,739	\$322,992
All other claims resisted	427,952	573,053	649,876
Total claims in dispute	600,665	839,792	972,868
Amount paid for new claims	11,387	20,013	15,872
Amount paid for claims previously resisted	65,445	59,882	88,527
Total amount paid	76,831	79,896	104,400
Amount resisted at year's end²	278,885	424,194	430,291

Source: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission.

Notes: NAIC does not endorse any analysis or conclusions based on use of its data. Data represent U.S. life insurers and, as of 2003, fraternal benefit societies.

¹Data for 1994 is not available.

²Not equal to subtracting total amount paid from total claims in dispute. The amount paid for claims disposed of usually varies from the amount claimed.

POLICY CLAIMS RESISTED OR COMPROMISED

From time to time, life insurers find it necessary to delay or deny payment of claims due to material misrepresentation, suicide within the contestable period, or no proof of death, among other reasons. In 2004, \$323 million in new claims along with \$650 million in other claims were in dispute. Of this amount, \$104 million was paid in 2004 and \$430 million still resisted at the end of the year (Table 7.6).

Table 7.7**Life Insurance Purchases, by Year**

Year	Policies and certificates in thousands/Amounts in millions					
	Individual		Group		Total	
	Policies	Amount	Certificates	Amount	Policies/ Certificates	Amount
1940	17,872	\$10,039	285	\$691	18,157	\$10,730
1945	16,212	13,289	681	1,265	16,893	14,554
1950	20,203	22,728	2,631	6,068	22,834	28,796
1955	21,928	37,169	2,217	11,258*	24,145	48,427*
1960	21,021	59,763	3,734	14,645	24,755	74,408
1965	20,429	90,781	7,007	51,385+	27,436	142,166+
1970	18,550	129,432	5,219	63,690+	23,769	193,122+
1975	18,946	194,732	8,146	95,190+	27,092	289,922+
1980	17,628	389,184	11,379	183,418	29,007	572,602
1985	17,637	911,666	16,243	319,503*	33,880	1,231,169*
1986	17,116	934,010	17,507	374,741+	34,623	1,308,751+
1987	16,455	986,984	16,698	365,529	33,153	1,352,513
1988	15,796	996,006	15,793	410,848	31,589	1,406,854
1989	14,850	1,020,971	15,110	420,707	29,960	1,441,678
1990	14,199	1,069,880	14,592	459,271	28,791	1,529,151
1991	13,583	1,041,706	16,230	573,953+	29,813	1,615,659+
1992	13,452	1,048,357	14,930	440,143	28,382	1,488,500
1993	13,664	1,101,476	17,574	576,823	31,238	1,678,299
1994	13,835	1,057,233	18,390	560,232	32,225	1,617,465
1995	12,595	1,039,258	19,404	537,828	31,999	1,577,086
1996	12,022	1,089,268	18,761	614,565	30,783	1,703,833
1997	11,734	1,203,681	19,973	688,589	31,707	1,892,270
1998	11,559	1,324,671	20,332	739,508	31,891	2,064,179
1999	11,673	1,399,848	26,912	966,858	38,584	2,366,706
2000	13,345	1,593,907	21,537	921,001	34,882	2,514,908
2001	14,059	1,600,471	26,036	1,172,080	40,095	2,772,551
2002	14,692	1,752,941	24,020	1,013,728	38,713	2,766,669
2003‡	13,821	1,772,673	21,946	1,050,318	35,767	2,822,992
2004‡	12,581	1,846,384	25,872	1,101,599	38,453	2,947,983

Sources: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission; LIMRA International.

Notes: NAIC does not endorse any analysis or conclusions based on use of its data. Data represent direct business and exclude revivals, increases, dividend additions, and reinsurance acquired. 1940–73 data exclude credit life insurance. Beginning with 1974, data include long-term credit insurance (life insurance on loans of more than 10 years' duration). Data represent U.S. life insurers and, as of 2003, fraternal benefit societies.

*Includes Federal Employees' Group Life Insurance of \$1.9 billion in 1955, \$84.4 billion in 1981, and \$10.8 billion in 1985.

+Includes Servicemen's Group Life Insurance of \$27.8 billion in 1965, \$17.1 billion in 1970, \$1.7 billion in 1975, \$45.6 billion in 1981, \$51 billion in 1986, and \$166.7 billion in 1991.

‡Includes fraternal benefit societies.

Table 7.8 Life Insurance in Force, by Year (millions)

Year	Individual		Group		Credit		Total	
	Policies	Amount	Certificates	Amount	Policies ¹	Amount	Policies/ Certificates	Amount
1900	14	\$7,573	—	—	—	—	14	\$7,573
1905	22	11,863	—	—	—	—	22	11,863
1910	29	14,908	—	—	—	—	29	14,908
1915	41	20,929*	\$100	—	—	—	41	21,029
1920	64	38,966	2	1,570	*	\$4	66	40,540
1925	94	65,210	3	4,247	*	18	97	69,475
1930	118	96,539	6	9,801	*	73	124	106,413
1935	114	88,155	6	10,208	1	101	121	98,464
1940	122	100,212	9	14,938	3	380	134	115,530
1945	149	129,225	12	22,172	2	365	163	151,762
1950	172	182,531	19	47,793	11	3,844	202	234,168
1955	192	256,494	32	101,345	28	14,493	252	372,332
1960	195	381,444	44	175,903	43	29,101	282	586,448
1965	196	539,456	61	308,078	63	53,020	320	900,554
1970	197	773,374	80	551,357	78	77,392	355	1,402,123
1975	204	1,122,844	96	904,695	80	112,032	380	2,139,571
1980	206	1,796,468	118	1,579,355	78	165,215	402	3,541,038
1985	186	3,275,539	130	2,561,595	70	215,973	386	6,053,107
1990	177	5,391,053	141	3,753,506	71	248,038	389	9,392,597
1991	170	5,700,252	141	4,057,606	64	228,478	375	9,986,336
1992	168	5,962,783	142	4,240,919	56	202,090	366	10,405,792
1993	169	6,448,885	142	4,456,338	52	199,518	363	11,104,741
1994	169	6,448,758	145	4,443,179	52	189,398	366	11,081,335
1995	166	6,890,386	147	4,604,856	57	201,083	370	11,696,325
1996	166	7,425,746	139	5,067,804	50	210,746	355	12,704,296
1997	162	7,872,561	142	5,279,042	47	212,255	351	13,363,858
1998	160	8,523,259	152	5,735,273	46	212,917	358	14,471,449
1999	162	9,172,397	159	6,110,218	46	213,453	367	15,496,069
2000	163	9,376,370	156	6,376,127	50	200,770	369	15,953,267
2001	166	9,345,723	163	6,765,074	48	178,851	377	16,289,648
2002	169	9,311,729	164	6,876,075	42	158,534	375	16,346,338
2003‡	176	9,654,731	163	7,236,191	40	152,739	379	17,043,661
2004‡	168	9,717,377	165	7,630,503	39	160,371	373	17,508,252

Sources: ACLI tabulations of National Association of Insurance Commissioners (NAIC) data, used by permission; Spectator Year Book.

Notes: NAIC does not endorse any analysis or conclusions based on use of its data. Data represent direct business and, beginning with 1959, include Alaska and Hawaii. 1994–97 data for individual amount and group certificates were revised. Individual and group categories include credit life insurance on loans of more than 10 years' duration; credit category is limited to life insurance on loans of 10 years' or less duration. Totals represent all life insurance (net of reinsurance) on residents of the United States, whether issued by U.S. or foreign companies.

*Fewer than 500,000

‡Includes fraternal benefit societies.

¹Includes group credit certificates.