Chapter 1

Answers to Review Questions

1-1. The five questions that must be answered when constructing a basic marketing plan are

- **What are my objectives?** You market and sell for a reason, to earn income. Your marketing plan must begin with income objectives that will translate into activity objectives (the level of various marketing activities needed to attain income objectives).

- **What am I marketing?** The key to answering this question is to view financial products and services as tools that enable people to achieve and/or protect their dreams. To market financial products successfully requires helping people connect the idea of achieving their goals and protecting the necessary assets and income for achieving their goals with the products and services designed for these very purposes. Therefore it is important for the advisor to describe and discuss his or her products and services in terms of the results they will achieve for the prospect.

- **To whom am I marketing?** Ideally, the advisor will set appointments with qualified prospects—people who need and want the advisor’s products and services, can afford them, can qualify for them, and can be approached by the advisor on a favorable basis. Imagine the increased efficiency and effectiveness of the advisor’s marketing efforts if he or she could market to a large group of such prospects that share identifiable common characteristics and needs, and have a communication (networking) system. Such a group of people is known as a target market.

- **How will I market to them?** For each target market selected, the advisor must choose and apply prospecting methods to access qualified prospects. These prospecting methods should reflect the prospecting source, the most probable financial needs and goals, and the target market’s preferences. In addition, the advisor must identify and implement appropriate ways to position his or her personal brand and products and create awareness of them. Finally it includes using effective methods for approaching prospects effectively to set appointments.

- **How effective am I?** A basic marketing plan identifies metrics to measure and evaluate marketing effectiveness. The most common measures are effectiveness ratios.

1-2. The eight steps of the selling/planning process are

- **Identify the Prospect.** Effective selling begins with getting in front of qualified prospects. This step involves target marketing, which operates on the premise that
people tend to congregate with people of like values and characteristics. By definition, a target market has a networking system. If the advisor behaves professionally and provides valuable products and services, referrals are very likely.

- **Approach the Prospect.** In this step, the advisor contacts the prospect with one objective in mind: to set an appointment. The approach should be based on a relevant, potential need the prospect may have.

- **Meet with the Prospect.** In the initial meeting with a prospect, the advisor’s objectives are to establish rapport, describe his or her services and the process involved, ask some thought-provoking questions, and listen attentively. Based on the prospect’s responses, the advisor establishes a mutually beneficial reason to do business, describing it in the form of a value proposition.

- **Gather Information and Establish Goals.** Using a company-approved fact finder, the advisor asks a lot of questions to gather personal information, qualitative data, and quantitative data.

- **Analyze the Information.** The advisor analyzes the information gathered by creating and/or examining appropriate financial statements; identifying obstacles to desired goals; looking at the prospect’s current insurance coverages, savings and investments; analyzing possible alternatives; and so on.

- **Develop and Present the Plan.** The advisor develops a plan. In addition to summarizing the client’s situation and the findings of your analysis, the plan should include recommended actions.

- **Implement the Plan.** If recommendations are based on the information gathered using a properly completed fact finder, implementing the plan should simply be the logical next step in working together. That does not mean the prospect will not have some concerns or objections. This is the step in which they will arise typically. An advisor should be prepared to address them as well as to motivate prospects to take action in general. Finally the advisor should assist the prospect with acquiring any necessary products and services.

- **Service the Plan.** This is the step in which you turn customers into lifetime clients. Service cements the relationship with a customer, giving you the opportunity to make additional sales and obtain referrals. Some service is reactive: the customer initiates it by requesting a needed change. What differentiates one advisor from another, however, is the proactive element of his or her service strategy. Proactive servicing strategies, such as monitoring the plan through periodic financial reviews and relationship-building activities enable an advisor to stay in touch with customers. It is this high-contact service that builds clientele.

1-3. In a client-focused approach to selling and planning, the objective is to cultivate a mutually beneficial, long-term relationship with a client, someone who follows your advice consistently, buys from you again, and refers you to others. (Note that for our purposes, a person who pays an annual retainer, asset management fee, and so on is a repeat buyer.) In other words, the end result is an ongoing relationship that benefits both parties. The initial sale is an intermediate, rather than final, step.
1-4. Target marketing is a process in which the advisor aims products and services at a well-defined target market. A target market is a group of prospects that meets the following criteria:

- The group is large enough to provide a continual flow of prospects.
- Members in the group have common characteristics that distinguish them from nonmembers. At least one common characteristic provides a basis for customized marketing messages and approaches.
- Members in the group have a common need or common needs, usually attributed to a common characteristic.
- The group shares information through a formal or an informal communication or networking system, making it more likely for an advisor to be referred and for the advisor’s reputation to precede him or her. A communication system is the most important criterion in defining a target market.

The advantages of a target market include the following:

- Successful target marketing will result in enhanced referability due to the communication network.
- Concentrating on a few target markets enables the advisor to tailor postsale service strategies to facilitate deeper relationships, which generally translate into increased loyalty.
- Gaining a reputation within a target market for being the expert will discourage other advisors from trying to penetrate the market.
- Target marketing results in higher profits through lower acquisition costs.
- Working with people with whom the advisor has a lot in common typically will increase the advisor’s job satisfaction.

1-5. The first step of the target marketing process is to divide your natural market into market segments, groups of people with common characteristics and common needs. The segmenting step involves one of two approaches:

- A very basic and effective approach to segmenting your natural markets is to analyze your personal background and history. Brainstorm to identify the types of people with whom you think you would like to work. In some cases, you will readily identify groups (markets), in other cases you will identify types of personalities for which you will need to take an additional step of identifying where you might find such people.

- A second approach is based on the process used by marketers in other industries. Although it is applied here toward past personal production, it can easily be applied to segment a newly appointed agent’s friends, family, and acquaintances list. Furthermore, one could apply it to the undifferentiated, or general, market. This approach involves completing the following:
  a. Identify your top 20 clients. These are people you enjoy working with and not necessarily those who generate the highest amount in commissions or fees.
  b. Select relevant segmentation variables. There are generally four types of segmentation variables that marketing experts use to divide a market: geographic,
demographic, psychographic, and behavioristic. Choose variables that will help you find groups of qualified prospects.

c. Apply the segmentation variables. Make a chart with columns for the client’s name and for information corresponding to each of the demographic variables you chose. Enter the information for each client.

d. Identify market segments and create profiles. Analyze the information you have gathered for commonalities. Look for groups with a communication network. Examine the segmentation variables that would indicate that a client belongs to a group with a system for networking. Groups may be found through variables such as occupation, employer, hobbies or other interests, social or religious organizations, and neighborhood or homeowners associations. Look at commonalities of product, need, and motivation. Finally assess variables related to profit generation, including compensation, and quantity and quality of referrals.

1-6. In the targeting a market step, you narrow your target market options and select one or a few to test and pursue. The following activities are recommended for completing this step:

- **Create selection criteria.** Take the top five or so market segments you identified and compare and prioritize them using criteria of your choosing. Such criteria will depend largely on your product mix (including services). You can group criteria into three main categories: fit of resources to segment’s needs, level of potential compensation, and level of competitiveness.

- **Conduct market research.** If you do not know enough about the market segments you have identified to evaluate them accurately, you will need to conduct market research. You can begin your initial research on the Internet or at the local library. The information does not have to be precise; a very rough estimate will do fine. Select your best potential target markets from the market segments you have chosen, and prepare and conduct a market survey.

- **Assess other factors.** Advisors who sell only one product will typically utilize a product specialization strategy in which they market one product to multiple target markets. One best practice is selecting target markets that are related to one another. A second strategy, the single-segment concentration, involves marketing one product to a single market segment. This approach is applicable for advisors who are targeting high net worth clients (dentists, doctors, professional athletes, and so on). Advisors who sell multiple products will choose from a selective specialization coverage strategy, which involves marketing a few products to multiple target markets, or a market specialization strategy that specializes in one market’s needs. Advisor’s who sell property and casualty insurance along with other insurance and financial products can use an undifferentiated full-market coverage strategy for the auto and homeowners insurance but use one of the other coverage strategies for their other products. You may identify some market segments that do not have a communication network. Most likely, this will happen if you segment by need and motivation. Look a little deeper to see if there is the potential for targeting this market segment within larger undifferentiated groups that do have a communication.
network or some reasonable proxy. If you find a strong correlation between certain characteristics and buying behaviors, ask the question: “Where can I find people like this?” Often a group of people may lack common financial needs. If there is a communication network and a perpetual supply of new members, consider segmenting the market segment by life cycle (age) and/or life stage (marital and family status) and targeting them according to the unique needs of each of the resulting market segments.

1-7. Positioning your personal brand and products involves the following:

- Your personal brand is an amalgamation of the qualities, characteristics, personal experiences, and skills that make you who you are. It is critical to identify the relevant, unique aspects of your personal brand and position them appropriately in your target market. The process includes the following steps: identify a relevant, unique position; put it in writing; test it; establish your position; and monitor and protect it.

- Advisors need to help prospects see the need for their products and services. Just as advisors must provide a compelling reason to be chosen as advisors, they must also provide a compelling reason for a prospect to purchase products. An advisor must appeal to the prospect’s logic by identifying relevant facts that pertain to the needs of the target market and individual prospects. In addition, an advisor must appeal to the prospect’s emotions by identifying the emotional reasons to buy that flow from the financial need that the prospect has for the products.

1-8. Common prospecting methods used to identify people who know you favorably include the following:

- Service transactions are typically initiated by the client (a change to a policy, contribution amount, mutual fund account, and so on). When clients contact an advisor for service, they are thinking about financial matters. This is a perfect time to see if prospects need other products or services.

- The purpose of a periodic financial review is to monitor the client’s progress in meeting financial goals and identify any new financial needs they may have. They are a staple in every advisor’s prospecting arsenal, and applicable to nearly every financial product or service.

- Seminars for clients are better thought of as client education events that are designed to achieve one or both of the following objectives: to create awareness of financial needs and methods for addressing them, and to help clients with ancillary aspects of their goals that cannot be addressed with your products and services.

- Introduction of your practice involves meeting with friends and family and giving a concise 10-minute overview of what you do for a living. A more indirect approach is to use your friends and family as a sounding board for the various target markets they represent. The advisor can ask their friends and family members to answer a market research questionnaire, to respond to particular marketing ideas, to provide feedback on telephone approaches, or to role-play the interview process.

1-9. Common prospecting methods used to identify people recommended by those who know you favorably include the following:
• Personal recommendations are the referrals an advisor receives from clients, friends, and family. Personal recommendations are the dominant prospecting method among most advisors.
• A second way to generate referrals is by identifying a center of influence (COI) within a desired target market. A COI is an influential person you know, who knows you favorably, and who agrees to introduce you or refer you to others. Using a COI is indicated when you can identify a person or persons whom the target market looks to for guidance and leadership. For example, all of the businesses may use a particular CPA or attorney. The president of an association is a potential COI.
• Networking is the process of continually sharing ideas, resources, and prospect names by non-competing businesses that target the same market. It is indicated when there are other professionals and businesses that specialize in working with your target market. Two forms include tips clubs and NetWeaving.

1-10. Common prospecting methods used to identify prospects among people who do not know you at all include the following:

• Personal interaction requires mastering the art of listening and the art of small talk, and showing a genuine interest in others. It also requires an ability to ask meaningful but innocuous questions that help you qualify a prospect. A good interaction is subtle and natural and avoids the appearance of shameless personal marketing.
• Another prospecting method is to sponsor or establish a formal presence at a public event that appeals to your target market. You could sponsor a child safety fair at a local school, coordinating your efforts with the local police department.
• Once you have established a good reputation, you will have the opportunity in some target markets to conduct group presentations, in which you educate a group of your target market constituents about a particular topic on which you are an expert. It is different than a seminar in that, in most cases, it is not appropriate to give a sales pitch.
• Another prospecting method is direct response, which involves sending letters with reply cards that prospects can return if they are interested in an appointment or more information. Sometimes, the letter will offer a small gift, such as a road atlas or a free booklet, to prospects who respond to the direct mail letter and agree to a free consultation with the advisor. An alternative is to use e-mail, if e-mail addresses are available. If prospects are not on a do-not-call list, advisors may follow up with a phone call to set an appointment.

Answers to Self-test Questions
1-1. B page 1.2
1-2. B page 1.5
1-3. D page 1.18
1-4. C page 1.26
1-5. D pages 1.23–1.24
1-6. C pages 1.32–1.33
1-7. B pages 1.33–1.39
1-8. D pages 1.13–1.14
1-9. A pages 1.36–1.39
1-10. A page 1.8

Chapter 2

Answers to Review Questions

2-1. Life-cycle marketing operates on two generalizations:

- From birth to death, people experience common life events that affect their financial and insurance needs. Many life events inherently create or increase a prospect’s need and/or ability to pay for insurance and/or other financial products. Life events serve as a trigger that raises a prospect’s awareness of financial needs or increases his or her interest in meeting them. More often than not, life events are partial triggers that require some advisor-initiated contact to raise awareness of the resulting financial need and/or opportunity.

- In the past, life events occurred in a fairly predictable pattern over a person’s life. The evolution of societal norms has changed the order and timing of some of these events. For example, people are marrying later in life. Despite these changes, the life-cycle paradigm is viable because life events still tend to occur within certain age ranges, or life-cycle market segments. The five segments are as follows:
  a. Youth—Ages 0 to 19. These are the growing and learning years marked by dependency on adults. Youth is characterized by physical, emotional, and intellectual development. This is the stage of life when people are most impressionable. Toward the end of this phase, the teenage years involve a search for identity.
  b. Young Adulthood—Ages 20 to 37. The early part of this phase involves transitioning from depending on parents to becoming independent and establishing one’s own identity. It is often a time for making commitments to work, marriage, and family. Toward the middle of the phase, one tends to reexamine commitments made to career, marriage, assumed roles and lifestyles.
  c. Middle-Years Adulthood—Ages 38 to 58. In the earlier years of this phase, many people begin searching for real meaning to life and/or attempt to hold onto lost youth. Some may experience a mid-life crisis as dreams and reality are reconciled. Toward the middle of the phase, the realities of life have been generally accepted. For most, the importance of one’s career increases with the decreasing responsibilities as a parent. Toward the end of this phase, some may be in the position of retiring. Those who are not are making preparations for retirement.
  d. Mature Adulthood—Ages 59 to 75. These are the fulfillment and yearning years. Many people achieve some self-actualization during these years. It is common for a renewed focus on the spiritual dimension to emerge. The early part of this phase is usually when people are preparing for retirement or retiring. Wealth
accumulation is important early on; toward the end of this phase more attention is placed on seeking new achievements and education, working in the service of others, and enjoying leisure time and accumulated wealth.

e. **Old Age—Ages 76 and up.** Old age is when a person becomes a seasoned citizen. It is the wise and fragile phase of life, a time to remember and recall the past. This phase encompasses the consumption and distribution of wealth. Long-term care is a key issue and often a major concern. Demographically, there will be three times as many women as men.

2-2. Prestige building is your public relations campaign to position your personal brand favorably in your target markets. The limit to prestige-building activities is your imagination. Methods for prestige building include the following:

- Social mobility refers to a person’s movement within and impact on a community. The result of social mobility is a reputation within the community. Some of the more common ways to increase social mobility include the following:
  a. Community Involvement. If the target market coincides with a social, civic, business, charitable, or religious organization, this is usually the preferred method for creating awareness of who you are and what you do. Remember to involve yourself only with organizations and causes that you support personally. In addition, determine a realistic view of your capacity for involvement to help you make decisions regarding your level of commitment. Aim for visibility and not shameless self-promotion. There are four levels of involvement to consider: sponsorship and giving, volunteering, joining, and leading.
  b. Writing. If you can write short articles and your target group has a newsletter or reads certain publications, then write an article and have it approved by your compliance department.
  c. Speaking to Groups. Some organizations will offer their members free educational seminars about pertinent topics. If this opportunity is available and you are comfortable speaking to groups, let the appropriate persons in the organization know your availability and the topics about which you would be willing to address. The goal of these speaking engagements is first and foremost to establish your reputation as an expert. Keep promotional information to a minimum—a business card and/or a personal brochure.
  d. Other Media Opportunities. There are other media opportunities, including local radio and television. There are many financial advisors who host their own 1-hour radio or television show on local public access channels. Others find their way on to local radio talk shows and local television news, and into newspaper articles as financial experts. Let local media know you are available, and inform them of the topics on which you can provide expert opinion. If they call you, the exposure is free and will help establish you as an expert in your field.

- The personal brochure is typically a one-page (usually front and back) document that introduces the advisor. Treat it as the prospect’s first impression of you. It should
impress, inform, and create interest. Your brochure should communicate your value proposition and should appeal to your target market.

- An Internet presence should be considered especially if your target market consists of members who are younger (although increasingly, older people are utilizing the Internet to conduct research).
- Although traditionally geared to relationship building and marketing to current clients, newsletters can be used with prospects as well.
- Advertising is the use of persuasive messages communicated through the mass media. The ultimate goal of advertising is to create new clients. For the purposes of financial products, advertising seems best suited to create awareness of an advisor’s personal brand rather than to induce prospects to purchase specific products. The premise for using advertising is that prospects typically want to work with advisors with whom they have some level of comfort and trust. All things being equal, they will want to work with an advisor they have at least heard of rather than a total stranger. Advertising promotes in a prospect a level of familiarity with the advisor. It may predispose the prospect to a favorable response when the advisor does finally approach him or her. In using advertising, it is helpful to determine how members of your target market find advisors like you; identify places a high concentration of your target market frequents; select advertisements that are appropriate to your target market; and implement methods to track the effectiveness of your efforts.

2-3. A preapproach is any method used to stimulate the prospect’s interest and precondition him or her to agree to meet with you about potential financial needs.

2-4. A seminar is a prospecting method in which you, alone or as a part of a team of professional advisors, conduct an educational and motivational meeting for a group of people. Seminars are distinct from speaking to groups in that a seminar’s objective typically is to produce appointments.

- Advantages of seminars include the following:
  a. Prospects who agree to a follow-up appointment are really coming to a fact-finding interview because they already have an understanding of their potential need and how the product can help them. In other words, a seminar is like conducting an initial interview for several prospects at one time, which is a tremendous time saver.
  b. Assuming that you and any other presenters give educational and motivational presentations, seminars build your credibility as an expert.
  c. Seminars allow you to maximize your public speaking skills.
  d. The natural next step of a seminar is either asking for an appointment or setting the expectation that you will be calling for one.

- Important steps for conducting seminars include the following:
  a. Define your objective. Determine what you want the seminar to accomplish.
  b. Set a budget and work to stay within this constraint.
  c. Determine how many people to invite. Start by setting a goal for the number of attendees you wish to have. You will need to invite more than the desired number
of attendees. One rule of thumb is to invite 10 people for each desired attendee. Once you have determined how many people to invite, create a list of names from your prospecting sources.

d. Choose content that is relevant to your target market’s needs. Make sure it is approved by compliance.

e. Select the presenters. This may mean using another speaker, such as a company expert, to present the bulk of the material.

f. Choose a date and time that avoids holidays and dates that coincide with important local or national events that interest your target market. Also consider how the time of day may affect your target market’s willingness or ability to attend.

g. Select a site convenient for the members of your targeted group. Parking may be a prime consideration in urban and suburban areas. The location should also be neutral. It is generally recommended that you do not use your office.

h. Announce the seminar. The invitation should clearly inform the prospect that the seminar will be educational in nature. It should provide the topic, date, time, and length of each seminar session as well as any fees to be paid. The seminar title should be clear and relate to the perceived needs of the targeted audience. In addition to the invitation itself, your letter should contain a response mechanism (a telephone number, e-mail address, or a stamped, self-addressed postcard) for more information. It is important to monitor both the mailing of the invitations and the response rate. Careful monitoring will allow time for you to make adjustments, if necessary.

i. Check the facility by visiting it while another meeting is in progress. This will give you the opportunity to evaluate the lighting, the sound system, and the visibility of any screens you will use with a projector. You can assess how well everyone in the room can see the speaker and judge whether the ambiance of the room reflects the feeling you wish to convey to your audience. Consider what audiovisual equipment or visual aids, such as an easel or whiteboard, you will need before you begin calling facilities.

j. Prepare a feedback mechanism that asks for attendees to provide their names, addresses, and phone numbers.

k. Address miscellaneous details such as nametags, pens, paper, and handouts.

l. Conduct an effective follow-up campaign. Many advisors end their presentation by telling their audience that the advisor will contact each attendee to answer any questions that might result from the seminar. Others bring their appointment book to the seminar and schedule appointments right then and there.

2-5. Guidelines for choosing effective preapproach letters include the following:

- Select letters that reflect your target market’s needs.
- Generally the shorter the better.
- Postcards are often more effective than letters because there is no envelope to open.

2-6. If you feel your company’s standard letters are not adequate, obtain company approval to draft your own.
The objectives for writing a preapproach letter are to trigger your prospect’s interest by highlighting briefly a problem or need; to communicate the relevant parts of your value proposition related to meeting that problem or need; to prepare the prospect for your call, or to request for written permission to call if the prospect is on a do-not-call list.

Guidelines for writing include the following:

a. Aim to write something that grabs the prospect’s attention.
b. If possible, establish a basis for your contact by referring to how you heard of the prospect.
c. Describe the most probable and acute financial need that the prospect faces and you can address.
d. Link that financial need to an appropriate emotional need.
e. Do not overstate the need; that is manipulative.
f. In communicating your value proposition, keep it to one or two sentences. Avoid platitudes and clichés.
g. Confirm the credibility of any statistics you use, and use them responsibly and appropriately (do not overuse them).
h. Pay strict attention to wording, grammar, spelling, and punctuation.
i. Ensure that the letter conveys an image of professionalism by using quality stationery and typeface.
j. Ask a current client from your target market to review the letter’s message and appearance.

The logistics for using preapproach letters include the following:

a. No letter is good enough to do a selling job by itself. An efficient and effective follow-up system is crucial to the success of any direct mail program. Do not send letters to more prospects than you can follow up with in a week.
b. Consider addressing letters by hand. Some advisors have found that handwritten addresses increase the probability that prospects will open the letters.
c. Affix postage with an individual stamp rather than a postage meter. Some advisors highly recommend the use of commemorative stamps.
d. Consider including an attention-getter in the envelope. One advisor includes a dollar bill to pay the prospect for reading the letter. Another advisor includes a Band-Aid with a health insurance preapproach letter.
e. E-mail is another way to send a preapproach letter. If you are dealing with a technically savvy target market, e-mail may be more effective than regular mail.

The steps for creating an effective telephone approach script include the following:

a. Greeting. In the greeting, you will introduce yourself and confirm that the prospect is willing to talk to you. This is your opportunity to make a good first impression. Open your conversation with “Good morning” or “Good afternoon.” Identify who you are and what company you represent. As a matter of courtesy, ask the prospect if he or she has time to talk. Pushing your agenda on the prospect may turn a “not right now” into “not ever.”
• **Creating Interest.** In this step, you will explain why you are calling and implement a method designed to pique the prospect’s interest so he or she will agree to meet with you. There are at least two different methods used to create interest. On the one hand, some advisors take a direct approach and simply address the prospect’s most probable financial needs as indicated by the prospect’s life-cycle segment. A second method for achieving this objective is to ask an open-ended question that allows you to uncover potential needs the prospect has. The advisor can provide a list of the most probable needs, applying the life-cycle marketing strategy, and asking the prospect which of these needs he or she considers most pressing. Depending on the prospect’s answer to the question, you can follow-up with questions designed to uncover a logical basis for the appointment. In other words, you are looking for a good logical foundation upon which to position your request for an appointment.

• **Asking for the Appointment.** This is the reason you are calling. In asking for the appointment, you are going to first offer a value proposition, a clear and compelling reason why the prospect should meet with you based on the prospect’s most probable need.

• **Prequalifying.** For those advisors who believe in prequalifying, this would be an appropriate time to do so. Prequalifying involves asking the prospect a few questions to ensure the meeting will not waste the prospect’s and the advisor’s time. The questions are related to underwriting issues (for insurance) and/or suitability issues. Some advisors ask a question to identify any third party who may influence the prospect’s decision, such as a CPA or an adult child.

• **Ending the Call.** In this step, you confirm the appointment and affirm your desire to meet the prospect. Depending on where you meet, you may either have to give or obtain directions.

• **Handling Objections.** Unfortunately, prospects often have objections to meeting with you. You will find that they will usually fall into one of four categories: no hurry, no money, no need, and no trust. Rather than be caught off guard and have no idea how to handle objections, write a script for each of the more common ones you face. A common strategy for handling objections is to use the “Feel, Felt, Found” technique. This technique works well for objections that the advisor feels need no further clarification and are simple to handle. The “Acknowledge, Clarify, Resolve” technique works for all objections. The steps are as follows: acknowledge the objection; clarify the objection; resolve the objection; and use an escape close.


• Some of the important limitations include the following:
  
a. Sales calls to persons who have placed their residential or mobile phone numbers on federal or state DNC lists are prohibited.
  
b. Calls cannot be made before 8 a.m. or after 9 p.m.
  
c. Sellers must maintain an in-house DNC list of existing customers who do not want to receive sales calls.
  
d. Sales callers must, at the beginning of every sales call, identify themselves, the company they represent, and the purpose of the call.
e. Telemarketers may not intentionally block consumers’ use of caller identification.

- The exceptions to these limitations are the following:
  a. Established business relationship. A business relationship exists in which a product or service is in place, and for 18 months after that product or service is no longer in effect or active. Several states have stricter requirements. If a consumer contacts an advisor, whether by phone, mail, e-mail, or in person, to inquire about a product or service, an existing business relationship exists for three months after that inquiry.
  c. Prior written permission. Advisors may make calls to persons on the DNC lists if they have a signed, written agreement from the consumer in which he or she agrees to be contacted by telephone at a specified telephone number. An e-mail from the prospect that clearly grants permission and identifies a number to call should suffice. Advisors may not call persons on the DNC list to ask for written permission to be called.
  d. Personal relationship. Calls may be made to people with whom an advisor has a personal relationship, including family members, friends and acquaintances.

- Advisors cannot contact prospects who are referred leads unless they receive written permission from the prospects to do so. They can work within the rules by doing any of the following:
  a. Ask for personal introductions. An arranged meeting over lunch, a cup of coffee, a round of golf, and so on would be ideal. This would give you a little more time to build rapport and probe for needs.
  b. Ask for an e-mail recommendation. The best method for using e-mail is to have the referrer write an e-mail recommending you to the prospect and letting the prospect know that you will be in contact with him or her. The referrer should carbon copy (Cc) you so that you have the prospect’s e-mail. Then you may send an introductory e-mail along with a requesting for permission, a phone number, and a best time to call. Have your e-mail approved by your compliance department, if necessary.
  c. Send a direct mailer with response cards. If the prospect does not have an e-mail address or the referrer is reluctant to give it out, consider sending a prospecting letter with a compliance-approved response card. The card should request a signature and a phone number to call.
  d. Invite the prospect to a seminar. Ask the referrer to jot a recommendation on a 3 x 5 index card. For example, “Lance really helped me make some important financial decisions.” Mail the recommendation along with an invitation to a seminar you are holding. If the prospect comes to the seminar, you will have an opportunity to gain permission to call face to face.

2-10. Two aspects for projecting a professional phone image are the following:
  - Attitude:
a. Be cheerful and smile. Your smile can be heard over the telephone.
b. Wear proper business attire to help you feel more professional; it will show in your voice.
c. Stay low-key, relaxed, and do not press too hard.
d. Stay healthy. Illness and fatigue will affect how you sound. Many people stand up to aid both their energy level and breathing.
e. A good way to start a telephoning session is to stand up and stretch, especially your stomach muscles to relax your diaphragm.
f. Breathe from your stomach, not your lungs, to relax your voice and give it more presence.
g. Be courteous. Listen to the prospect and do not interrupt.
h. Pay attention to what is said, think about it, and then respond. Pausing to think about what your prospect has said does not show weakness; it shows consideration.
i. Approach every call like it’s the only one you will make that day. Act as if that person is the most important person in the world.
j. Speak conversationally. You are prepared and you have practiced the script, but it should be so well prepared and practiced that it sounds spontaneous.
k. Practice your telephone approach until you know it by memory, but keep it in front of you when you make your calls. Its presence will give you extra self-confidence.
l. Keep your conversation brief.
m. Use the prospect’s name once or twice; avoid overusing it like telemarketers do. Remember, though, that no one is flattered if you mispronounce it.
n. If you are calling with a referral or a reference of any kind, use it. It will help establish you as a person to be taken seriously.
o. Always watch your use of words. Speak carefully using proper grammar. Don’t stammer. Try to eliminate non-words (like “um” or “er”) completely.

• Voice:
a. Speak in your natural voice. You should sound relaxed and sincere. Try to make every call sound as if you are calling a good friend.
b. Speak clearly. It takes the listener a few seconds to get used to a new voice, so your first few sentences are critical.
c. Keep a good posture. Sit up straight or stand up to get the most out of your voice.
d. Listen to what others give back as feedback. If you are asked to repeat yourself often, you may need to improve your enunciation.
e. Speak distinctly. If this means slowing down, then slow down. Your message is worth it.

2-11. Prospecting and selling activities:
• Activities you will want to track include the following:
a. number of contacts attempted
b. number of contacts made (spoke to the prospect)
c. number of appointments made
d. number of initial meetings or interviews  
e. number of fact finders conducted  
f. number of closing interviews  
g. number of sales made  
h. number of hours spent setting appointments  
i. amount of commission and/or fees  

- Keeping accurate records of your daily prospecting and selling activities enables you to generate effectiveness ratios for setting appointments and making sales. These ratios will provide valuable data you can use to make decisions about target markets, approach scripts, interviewing techniques, and so on.

**Answers to Self-test Questions**

2-1. B pages 2.5–2.6  
2-2. B page 2.17  
2-3. C pages 2.35–2.36  
2-4. A pages 2.24–2.25  
2-5. C pages 2.28–2.29  
2-6. B pages 2.36–2.37  
2-7. D pages 2.38–2.39  
2-8. D pages 2.2 and 2.4  
2-9. B page 2.8  
2-10. C page 2.20  

**Chapter 3**

**Answers to Review Questions**

3-1. When you work with clients using an integrated planning approach, you aim to propose recommendations regarding their products within the context of the prospect’s overall financial situation and needs. This will involve being aware of the client’s needs in the following planning areas: general financial situation, insurance planning and risk management, employee benefits planning, investment planning, income tax planning, retirement planning, and estate planning. For those areas that you lack expertise, consider referring prospects to non-competing advisors who can assist them. You may even form a team of specialists and serve as its manager, coordinating the team’s efforts as well as contributing your expertise in your field of specialization.

3-2. Budgeting and cash flow management are the most basic tools of financial planning. Communicating the importance of these processes and helping the client through them can be among the advisor’s most valuable services. Budgeting is the process of creating and following a specific plan for spending and investing the resources available to the client. A working budget model should be established, followed by a comparison of actual and expected results. By monitoring the budget, the client and advisor can recognize problems as
they occur and even anticipate problems, providing a means for financial self-evaluation and a guideline to measure actual performance.

3-3. The financial planning pyramid uses four levels: wealth foundation, wealth accumulation, wealth preservation, and wealth distribution. The pyramid in its entirety represents an integrated and comprehensive financial plan. The individual blocks illustrate how most people feel comfortable building their financial plans—one or a few blocks at a time. The term building-block approach is used to describe this incremental approach. The various levels provide some guidance as to a general order in which to address financial needs. The first level represents the foundation, the basic needs that should receive primary attention. Failure to address these needs leaves any savings and investments vulnerable should an uncovered loss occur. Thus basic insurance products, a simple will, and an emergency fund form a wealth foundation.

Once the foundation is in place, a person can begin buying products in the wealth accumulation level such as CDs, stocks, bonds, mutual funds, real estate, and so on. Once assets are acquired, wealth preservation tools are needed. When the accrual of assets reaches a threshold, a person will need to consider products such as umbrella liability and long-term care insurance to preserve assets from lawsuits or the potential need for long-term care. Most likely, with increased wealth will come additional property that will need to be insured, such as a summer home, a boat, a jet-ski, and so on. At the wealth distribution level, products are needed to manage retirement income to ensure it will last. In addition, estate planning tools are used to conserve the estate for heirs and provide for charitable causes.

3-4. The young-adult market segment can be grouped into the following subsegments:

- single—individual with no partner and no kids
- dual income with kids—individual with a partner and kids
- dual income with no kids—individual with a partner and no kids (referred to as DINKs)
- single income with kids—individual with a partner and kids where the partner is not employed outside of the home. Also included in this grouping are single parents.

Common characteristics in the young-adult market segment include the many firsts that a person experience: the purchase of a first car and first house, a first marriage, first child, and first divorce.

Common needs in this segment include the following:

- Final expenses—Final expenses are needed to cover burial, probate and administrative costs, any state inheritance or federal estates taxes due, and any medical expenses associated with death.
- Emergency Fund—This is the recommended three to six months of living expenses needed to keep a person afloat in the event of losing a job or being disabled. For a single person, three months would be adequate while six months would be more appropriate for those individuals with children.
- Debt Liquidation—Credit card debt begins to mount during this phase. You could provide some wise counsel regarding the advantages of paying off these balances and providing for their liquidation at death. Car or personal loans would also fall under this category.
• Disability—Protection against loss of income due to disability should be addressed as soon as a person begins earning an income. For young adults, it now becomes a pressing need.

• Retirement—It’s never too early to begin saving for retirement. Systematic saving over a working lifetime is a key to supplementing other retirement programs. The old rule of thumb is to tuck away 10 percent of annual income. Young families with modest incomes should start with something, even if they cannot make a total commitment to this 10 percent guideline at first.

• Will—This is the point in life when most people should have a first will.

3-5. While the need for life insurance receives a great amount of attention, the need for disability income insurance is often obscured or never discussed. But studies show that

• a 30-year-old has a 24 percent chance of being disabled for at least 90 days before reaching age 65
• at age 45, the chance of suffering a disability is only reduced to 21 percent
• a person disabled for 90 days will probably go on to be disabled for at least four years.

• Despite these statistics, very few people have adequate protection against long-term disability. The public may purchase life insurance for their family’s protection, but they have largely neglected their own income protection, even though the odds are far greater for a person to be disabled than to die. Statistics comparing the incidence of disability as compared to death at various ages show that up to age 42 the chance of suffering a disability of at least 90 days is at least three times greater than the chance of dying.

3-6. Terms associated with disability income insurance:

• Total disability. The definition of disability differs from one company to another, and from one contract to another. These differences become extremely important to the eventual payment of a claim. The definition can be very narrow, providing very limited coverage. An example of this kind of definition is the inability to do any kind of work. Conversely, the definition can be more specific, defining disability more liberally and providing coverage that is more comprehensive. Defining disability as the inability to perform your own occupation is a more specific definition and more beneficial to the insured. Policies may also have a mixed definition of disability, using, for example, the own-occupation or own-occ definition for an initial period of disability (typically two years), then changing to a less liberal definition. Such a provision would pay benefits for the first two years if the insured is unable to perform the material and substantial duties of his or her occupation, but would only continue paying benefits beyond the two-year period if the insured was unable to work in any occupation for which he or she was reasonably suited by education, training, or experience.

• Elimination period. This is the period the insured must be disabled before benefits are payable. It may range from 30 days to one year (although 30- 60- and 90-day elimination periods are most common). The longer the waiting period for benefits, the lower the premium will be.
• **Residual disability.** Residual benefits in disability policies represent a further refinement in the partial disability definitions. Under residual disability coverage, benefits are proportionate and based on a percentage of lost income. If needed, they are usually payable for the contract’s entire benefit period instead of the limited time available under a partial disability definition. Thus the residual benefit encourages the disabled to return to work. The definitions are numerous, some even incorporating various qualification periods as trigger dates to enact benefits. Study these details to fully understand the policies you sell, or are selling against.

• **Cost-of-living adjustment rider (COLA).** The benefit provided by this rider attempts to adjust the base amount of coverage to reflect cost-of-living changes due to inflation. The insured usually must be disabled for at least 12 months. Some companies offer a flat percentage of the base amount while others tie the payment to the Consumer Price Index. The cost-of-living rider is used only at claim time. When the insured recovers, benefits return to the original level unless a special rider is provided to maintain the increased level of benefit.

• **Future increase option (FIO).** As in a similar rider to a life insurance policy, the future increase option allows the insured to increase coverage at stated future dates as income eligibility increases without any medical underwriting. Income verification is required.

### Answers to Self-test Questions

3-1. A pages 3.33–3.34  
3-2. B page 3.14  
3-3. A page 3.6  
3-4. B page 3.33  
3-5. D pages 3.31–3.32  
3-7. B page 3.33  
3-8. B page 3.35  
3-9. D page 3.22  
3-10. C page 3.24

### Chapter 4

### Answers to Review Questions

4-1. The more carefree days of young adulthood for most people eventually give way to a more serious outlook on life. Somewhere during the young adulthood phase, some people have begun new careers. Others have found a partner and some have had children. Toward the end of the young adult phase, people have begun to establish themselves, as they transition into the middle years of adulthood. By this time, people tend to be established in their careers. They may change jobs or employers, but typically not what they do for a living. Tenure in their field means they are moving toward the peak of their earning potential, and as they
approach the middle of the phase they begin to grow more aware of their need to prepare for retirement. Some parents experience an empty nest as their children move out and become independent. The empty nest brings an emotional adjustment as parents face the reality that they no longer have financial responsibilities for their children. For many, this is exhilarating and reintroduces parents to situations they have not experienced since the onset of parenthood. It also means having more disposable income and more time. For others, it may be a sad time that calls for reflection and a reordering of life as their children depart the home to venture out on their own. In this segment, you will find people who must begin dealing with aging parents and decisions that older people have to make. Some in the sandwich generation will begin caring for a parent or another elderly relative. For some, this phase of the life cycle means receiving inheritances in the form of gifts from living parents or estates from deceased parents.

Needs of this segment include emergency funds, mortgage cancellation, final expenses, income replacement, education planning, debt liquidation, disability, retirement planning, wills, estate planning, and long-term care planning.

4-2. Term insurance policies provide a death benefit if death occurs during the period of time that the policy is in force. The policy period is expressed as a number of years, such as 1, 5, or 30, or until a certain age of the insured, such as 65 or 70. If the insured dies during the policy period, the face amount of the policy will be paid to the beneficiary. If the insured survives to the end of the policy period the insurance company pays no benefit and the coverage ends. Term insurance is tied directly to the cost of mortality, which increases as the individual grows older. The premium is initially relatively low and increases periodically in most types of term insurance to reflect the increased mortality of the insured. The older a person is and the longer the period of coverage, the higher the premium and mortality costs will be.

The main types of term include:

- Level face amount. Most term life insurance sold today provides a level death benefit over a specific period. The premiums on these policies normally increase with age at renewal or may remain level at younger ages.

- Increasing premium contracts. Many term policies have increasing premiums with level death benefits and are renewable. The ART may be referred to as yearly renewable term (YRT) by your company. The premiums increase each year for the length of the renewal duration, which may be one, 5, 10, 20, 30 years, or to age 70. Some plans extend to age 100 and have a large number of rate bands for sums ranging from $100,000 to $1 million. Many offer different premium categories based on underwriting qualifications such as standard/preferred, tobacco user/nonuser, and various combinations of these.

- Decreasing term life policies. Some term insurance products have face amounts that decrease over time. The premium remains fixed for the length of the contract, while the face amount gradually decreases. Decreasing term premium may be significantly higher than for the same initial amount of level term. Advisors should be aware of this difference and recommend level term if appropriate for the clients.

- Term riders. Most companies allow policyowners to add term riders to either a term or permanent policy. The convenience of term insurance as a rider, and the
advantages of combining different types of protection under one contract, have earned term riders a lasting place in your portfolio. Because a policy fee is charged for the contract as a whole, the term rider will save the cost of an additional policy fee for most company plans. A level term rider can provide temporary additional term protection for a specific number of years. They may also be used to insure other family members, such as a spouse and/or children.

4-3. The different variations of whole life insurance include:

- Ordinary life provides level death benefit protection for a level premium. Premiums are paid to age 100, and the policy builds guaranteed cash values, which equal the face amount at age 100. At that time, if the insured is still alive and has paid all the premiums, the policy will mature. The cash value will equal the face value of the original policy and will be paid to the policyowner. Ordinary life offers the most permanent protection for the least premium.

- Limited-pay life policies are designed for people who need permanent protection, but who want accelerated cash accumulation or who prefer not to pay premiums to age 100. With limited pay plans, insurance protection extends to age 100 when the policy endows as it would with ordinary life, but the premium payments stop before age 100 resulting in higher premiums and cash values. Generally the shorter the premium payment period, the higher the premium and the faster the cash value accumulation.

- Modified whole life insurance is a whole-life product that offers a lower premium for a period of time (such as three to five years) and a level face amount. After a premium increase, the premium stays level for the rest of the life of the contract. This product is used for clients who may not have the money to purchase level premium whole life now, but expect to be able to afford the premiums in a few years.

4-4. Universal life combines the features of renewable term insurance with a tax-deferred cash value account that earns competitive market interest. Policyowners are able to pay premiums on a flexible, nonscheduled basis. The policyowner can increase or decrease the amount of death benefit protection of the policy at any time within company and IRS rules. Universal life policies have either a front-end or a back-end load. With a front-end load, the company’s fixed expenses are deducted before the premiums are added to the cash value account. With a back-end load, fixed expenses are recovered from surrender charges by reducing the account value if surrendered. With a Level Death Benefit Option, the amount of the term protection, or net amount at risk, decreases as the cash value account increases. With the Increasing Death Benefit Option, the net amount at risk remains level with the increasing cash value account used to increase the death benefit. Most universal life policies offer the full range of additional benefit riders available with other personal permanent policies. A monthly deduction from the cash value is made to pay for this additional protection.

4-5. Non-variable, interest-sensitive life insurance products also include:

- Current Assumption Whole Life. This is a variation of whole life that uses current mortality charges and interest earnings that are based on current yields rather than overall general account yields. It does not offer the premium flexibility of universal life.
Sometimes it is described as universal life with fixed premiums. Despite this oversimplification, as the premiums may be restructured at specified anniversary years, it describes how CAWL differs from a traditional policy. If premiums are paid on schedule, CAWL guarantees a death benefit and a minimum guaranteed interest rate to be credited on cash values.

- **Interest-Sensitive Whole Life.** Some companies guarantee the mortality charge and the expense charges in current assumption plans. When the mortality and expense charges are guaranteed, the policy is often referred to as an interest-sensitive whole life policy because interest credited to the cash value becomes the only element not guaranteed in the contract.

4-6. The key differences of variable life and variable universal life from their fixed versions are as follows:

- **Variable Life Insurance.** This was the first life insurance policy designed to shift the investment risk to policyowners. It offers a combination of permanent life insurance protection and the growth potential of variable fund investments. The policy’s cash value is invested in an account made up of one or more funds of equities, money market accounts or bonds. The policyowner decides where to invest the money and within contract limits may transfer funds from one fund account to another. The policy guarantees a minimum death benefit, but the actual death benefit paid may be higher if the investments perform well. The cash value also fluctuates with the investment performance. The cash values are not guaranteed. If the investments to which the cash values are linked perform poorly, the variable life cash values may grow at a lower rate than in traditional products or not at all. The premium is level for the duration of the policy. Each premium is reduced by an amount needed to maintain the minimum guaranteed death benefit. It offers traditional product provisions such as loan privileges and the usual variety of optional additional benefit riders. Variable life is considered to be both a life insurance and an equity product. Advisors who sell variable products must be licensed and registered with FINRA. Variable life is regulated by both state law, where applicable, and by the SEC. The company selling variable life must have a prospectus available that the advisor must mail or give to prospects prior to or during the sales interview. This fixed-premium policy offers a unique feature by guaranteeing a minimum death benefit regardless of investment performance. If all of the required premiums are paid, the insurance company guarantees that the death benefit will be paid even if the investment funds are otherwise inadequate to support the policy.

- **Variable universal life.** This is also known as flexible premium variable life and combines features of variable and universal life insurance. It offers policyowners the flexibility of universal life with the investment growth of variable while discarding the fixed-premium aspects of variable life. With variable universal life, the policyowner selects an initial insurance amount and premium level. Premium dollars can be directed to one or more investment funds and switched from one fund to another as in variable life. The same registration with NASD and licensing are required to sell variable universal life insurance as is required to sell variable life.
insurance. Because it is a registered product, it also requires delivery of a prospectus to the prospect. Policyowners decide how much premium to pay into the policy and when to pay it, just as in universal life. Likewise, the cash account must always be large enough to pay the monthly cost of the term insurance element and administrative expenses. Within certain legal limits, policyowners can adjust the combination of cash value and term insurance in the policy by making larger or smaller premium payments. It offers the same two death benefit options, the ability to change options, and other such features.

4-7. Premiums paid for individual life insurance policies are usually considered a personal expense and are not deductible for income tax purposes. There are some exceptions to this, but in these situations, life insurance premiums can be deductible because they also fit the definition of some other type of deductible expense, not because they are life insurance premiums. For example, premiums paid for life insurance in an alimony agreement may be deductible as alimony payments. Premiums paid for life insurance that is owned by and paid to a charity as beneficiary may be deductible as a charitable contribution. The premium is deductible because it is treated as a charitable contribution, not because it is a life insurance premium. Similarly, in business situations, employers are allowed to deduct premiums for life insurance protection if paid in the form of a bonus to an employee. The employer may then deduct the amount of the bonus paid to the employee as compensation and thus as a business expense. If life insurance is part of a pension plan, the premiums are deductible as part of a contribution by the employer to a tax-qualified plan. Again the deduction for the premium is based on the fact that it is a contribution to a tax-qualified retirement plan rather than a life insurance premium.

4-8. Living benefits refer to the use of cash values and dividends of a permanent insurance policy while the insured is alive. To the extent living benefits are taxable, they will be treated as ordinary income and not capital gains. In addition, the taxable amount is the amount the taxable benefit exceeds the tax basis. The tax basis is initially calculated by adding the total premiums paid into the policy and subtracting any dividends paid by the insurer. If nontaxable withdrawals have previously been made from the policy, those amounts reduce the policyowner’s basis. Living benefits include:

- **Loans.** The policyowner is given the right to borrow a percentage of the cash value in the policy. The policyowner is charged interest on the borrowed amount, and the interest is not tax deductible. If the policyowner does not pay the loan interest, it is added to the loaned amount. Unless a policy is a modified endowment contract (MEC), policy loans are non-taxable providing the policy remains in force.
- **UL and VUL partial surrenders (withdrawals).** UL and VUL policies offer the ability to withdraw cash value from the policy, known as a withdrawal, a partial withdrawal, or a partial surrender. The death benefit and cash value are reduced dollar for dollar by the amount of the partial surrender. Partial surrenders are taxable when the total amount of all withdrawals exceeds the cost basis of the policy. The exception is when the policy is a MEC; in that situation, harsher tax rules apply. In some cases, surrender charges may apply as well.
• Dividends. Mutual insurance companies pass along favorable experience in mortality, interest, and expenses through a return of premium called dividends. Policies eligible for dividends are called participating policies. In most cases, mutual insurance companies that provide participating insurance plans build a margin into their premium for contingencies. Dividends are not taxable unless the total amount of all dividends paid exceeds the total premium paid. Because policy dividends are a nontaxable return of premium, they reduce the policyowner’s basis. If total dividends paid exceed total premiums, additional dividends are taxable. Dividends may be paid as cash, applied to reduce premiums, left with the company to accumulate at interest, used to purchase paid-up additions, or used to pay for one-year term insurance equal to the current cash value.

• Cash surrenders. Income tax is payable on the surrender of all policies for cash (or the maturity of an endowment) if the amount received over the life of the contract exceeds the net premiums paid (excluding premiums for supplementary benefits). Net premiums paid determine the cost basis and equals the gross premium less any dividends received. If the amount the policyowner receives upon surrender exceeds the net premiums paid (cost basis), then the excess is fully reportable as a taxable gain in the year received. An exception to this rule would be for certain government policies or GI insurance. Any gains realized with these types of policies are tax exempt.

• Section 1035 policy exchanges. A special situation arises when a policyowner exchanges an existing policy for a new one in accordance with the Internal Revenue Code Section 1035. In a properly executed Section 1035 Exchange, no taxable gain is realized on the exchange. The adjusted cost basis of the old policy is carried over to the new one.

4-9. The modified endowment contract (MEC) came into being because some people were using life insurance primarily as a tax-deferred investment vehicle. This went against the premise that life insurance was to be used primarily to provide a death benefit. A 7-pay test was devised to determine if a policy should be classified as a MEC. This establishes limits to the amount of premiums that can be paid into a life insurance policy within a period of seven years. If the policy is overfunded, it becomes a MEC and distributions from the policy are subject to different taxation rules not applied to non-MEC policies.

If a material change occurs to a policy once it is in force, the 7-pay test period is reset. Examples of changes include an increase or decrease in coverage, or an added rider or benefit. If a policy is or becomes a MEC, it is treated the same as any other life insurance policy with one exception—some distributions from a MEC are taxed on a LIFO (last-in-first-out) basis to the extent there is gain in the policy. In addition, the taxable gain is subject to a 10 percent penalty unless the distribution is made after age 59½, or death, disability, or annuitization occurs.

4-10. The face of America continues to change. There are dramatic ethnic population shifts in many states and most large cities in this country. By 2050, Hispanics are projected to make up 24 percent of the U.S. population and minorities in general will make up 47 percent of the population. In assessing any market, you should consider what penetration your services and
products have in that market as well as how receptive the market will be. One particular opportunity you will find with emerging markets is the first-to-market strategy in which you penetrate a market where a particular product or service has little or no representation. The goal is to create loyalty and to grow with the market. Loyalty is high in these situations and that is the key to the success of this strategy.

Diverse markets qualify as target markets. They share common characteristics in their language, culture, and many times their lifestyle. They share common needs, sometimes because of their culture or simply because they are now away from the natural support system of their relatives and friends. Most importantly, they have a communication system. The latter is critical in defining a target market because it is the factor that creates a perpetual flow of prospects. Two of the biggest misconceptions are that you have to be of the same ethnicity and/or you must speak the language to sell in these markets. Undoubtedly possessing one or both of these characteristics will help you tremendously, but lacking them does not eliminate you.

Look for opportunities within your natural market. Do you currently have someone in your book of business that is a part of that market? Do you know a businessperson who is a member of that market or does business in that market? Are there businesses run by members of that particular ethnic community? In this situation, if you do not speak the language, a center of influence will be necessary. The best way to approach a new community is to find a few professional friends in the target community and ask them to help you. If you don’t know anyone, try finding a professional, such as a doctor, a non-competing insurance advisor, or a lawyer who works with members of that community. After you have done your market research, look to work with other professionals in that community. Referrals from non-competing advisors, attorneys, and other financial services professionals will build your prestige in that community.

4-11. Each divorce or separation case will present a unique set of challenges. You must deal with them in a sensitive but direct manner. Your response will be dictated largely by four factors: (1) the personal terms under which the spouses are parting, (2) the legal conditions of the separation or divorce set down by the court, (3) the number and ages of the children involved, and (4) the wishes of the couple.

You will want to express your regret and let your clients know that you are ready to help them any way you can. Tell them that there are several considerations that they should be aware of, both with their present life insurance and any new coverage that is made part of the settlement. Suggest that the three of you need to go over these points and decide the best way to proceed. Meeting with the two spouses is usually less complicated than trying to act as a go-between unless the situation is such that it is not practical for the former spouses to meet with you at one time. Determine if the divorce is amicable or otherwise. You need to be sure that no necessary coverage is inadvertently lost. Review with your clients their plans to keep their present life insurance protection in force after divorce. Discuss any change of beneficiary designations that may be necessary. Life insurance is valuable property and in recent years has begun to figure prominently in the court’s judgment. In these situations, your role should be that of a professional advisor who both facilitates the various policy arrangements and, when possible, recommends the most favorable approach to both parties.
4-12. There are many financial aspects of divorce because marriage typically involves the joining of many financial arrangements that must now be untangled. A major part of a divorce or separation is the transfer of property from one spouse to the other. Depending on how the married couple kept their financial affairs, there may be property that is commingled and other that is separate. That property may have been brought to the marriage or acquired during marriage by one party, and it is intended to stay that way. The treatment of this and other property upon divorce will vary from state to state.

When a divorce is taking place, legal instruments such as wills and trusts must be reviewed, and if necessary, modified based on the changes the divorce brings about. The federal estate tax marital deduction will no longer be available to the taxpayer. The divorced persons may need to reconsider choices for estate representatives (administrator or executor) and legal guardians for minor children. Estate planning alternatives for children may need to be reconsidered and the establishment of trusts and other legal instruments executed. Property, such as a home, retirement plans, and other assets may need to be re-titled and beneficiary designations changed. Jointly held property may need to be distributed and/or re-titled. It is also important to consider the consequences of remarriage on the family. This is particularly important where there are children from a prior marriage or prior marriages. The parent may want to consider children both from this and other marriages after his or her death.

Divorce may leave one or both parties with little or no accumulation of pension benefits or other private sources of retirement income. If the marriage lasted 10 years or longer, divorced persons are eligible for Social Security based on their former spouse’s earnings record. In addition, a spouse may be entitled to a portion of the former spouse’s retirement benefits if the divorce decree includes a qualified domestic relations order. Qualified domestic relations orders are judgments, decrees, or orders issued by state courts that allow a participant’s plan assets to be used for marital property rights, child support, or alimony payments to a former spouse. Divorce may change the family relationship, but it does not alter the basic fact that both spouses will continue to have insurance needs. The plans established to provide protection for their children may be even more important now than before. Life, health, property, and other forms of insurance will need to be continued, and possibly changed.

4-13. There are two general tax rules to keep in mind when dealing with divorce: Alimony payments are tax deductible for the payor, and child support payments are not tax deductible for the payor. Different tax rules also apply to life insurance in divorce situations. Whether premiums are deductible depends upon the premium payor, the owner, the beneficiary, and the purpose of the insurance in the divorce. Similar factors will determine whether premiums are income to an ex-spouse.

Answers to Self-test Questions

4-1. C page 4.29
4-2. B page 4.14
4-3. B page 4.3
4-4. C page 4.8
Answers to Review Questions

5-1. There are only three sources of income available to any of us at retirement: people at work, money at work, and charity. With planning before retirement, your clients will not need to work unless it is something they do to stay active and involved. Work will not be something they have to do to pay the bills. The financial need to continue working may be the result of bad luck, but it may be the result of a failure to plan and implement that plan. Money at work is the money you have working for you. This includes government-sponsored personal retirement and savings programs, and permanent cash value life insurance. Without savings or planning, only charity is available to make up the shortcomings. Charity is not an option that any of us would look forward to having to live on, either from our children or government subsidy programs.

5-2. The current retirement gap formula is determined by the following calculation:

1. Assume your prospects will retire tomorrow. Determine their current expenses, including housing, personal expenses, and recreation.
2. Calculate existing resources. Determine what current resources they have to meet expenses, including estimated Social Security and employer-sponsored retirement benefits, cash values from existing permanent life insurance, and other long-term investments intended for this use.
3. Retirement income need = percentage of current income. Determine a percentage of the current income that will meet the retirement income needs. Your prospect may not wish to discount the current income. It could be viewed as an inflation hedge. For many people 70 percent of current expenses seems realistic. Whatever figure your prospect chooses will work. It must be their goal.
4. Retirement income need – existing resources = current retirement gap. The difference between tomorrow’s needs and today’s resources is the current retirement gap. It produces a dollar figure for today, not accounting for the time value of money. Today’s calculations will change in the future as both the economy and the prospect’s needs change.

5-3. The term tax-qualified means that the plans are eligible for certain tax advantages such as deductible employer contributions or tax-deferred accumulations. To qualify for tax-qualified status, plans must conform to a number of requirements: a plan must meet minimum participation (including minimum age and service) and coverage requirements, be nondiscriminatory, meet minimum vesting requirements, have minimum and maximum...
funding standards, provide automatic survivor benefits, and satisfy distribution requirements. Tax advantages to tax-qualified plans include the following: (1) the employer can take a tax deduction for contributions made to the plan, and (2) employees do not have to pay taxes on amounts contributed, either by the employer or as salary reductions from their own pay, until they are withdrawn. This means that contributions are made on a pretax basis, earnings in the plan are made on a tax-deferred basis, and distributions from these plans can be rolled into an IRA with continued tax-deferral until the funds are withdrawn.

The various types of plans include:

- Defined-benefit (DB) plan—In a DB plan, the benefit is defined and guaranteed, based on a formula in relation to earnings, years of service, and other considerations. The employer makes the contributions on a tax-deductible basis, and assumes the investment risk.

- Defined-contribution (DC) plan—In a DC plan, the employer defines the contribution, but does not guarantee or define the retirement benefit. The employee assumes the risk of inflation, investment performance, and adequacy of the retirement income.

- 403(b) plan—The 403(b) plan has traditionally been referred to as a Tax Sheltered Annuity (TSA). It allows employees of tax-exempt employers, as described in IRS Code Sec 501(c)(3), to set aside a portion of their earned salary income for deferring compensation for retirement. Eligible organizations include public schools, nonprofit organizations, nonprofit hospitals, charitable foundations, museums, zoos, symphony orchestras, trade associations, and many private schools and colleges. Contributions are typically made by the employee, but are administered by the employer, who may also contribute to an employee plan. Each year’s taxable income is reduced by the amount of that year’s contribution to the plan, and investment growth is not currently subject to income tax. 403(b) plans are designed to be self-directed by the employee. These plans are meant to accumulate money during working years to be distributed through settlement options during retirement. Like IRAs, they have named beneficiaries and are owned by the participant.

- Individual Retirement Accounts (IRAs)—IRAs are tax-advantaged retirement plans available to many people with earned income. Under current law, eligible individuals may contribute 100 percent of earned income up to a maximum annual contribution limit. The limit applies to total contributions made to either a Traditional IRA or a Roth IRA, or a combination of the two. In 2009, a person under age 50 could contribute $2,500 to a Traditional IRA and $2,500 to a Roth IRA for a total of $5,000. The annual limit is $6,000 (in 2009) for a taxpayer aged 50 and older.

5-4. The Traditional IRA and Roth IRA have the following differences:

- Contributions can be made into a Roth IRA provided the accountholder has earned income. For a Traditional IRA, the accountholder must also be under age 70 ½.

- Traditional IRA contributions may be fully deductible, partially deductible, or nondeductible. A Roth IRA’s contributions are always nondeductible.
Withdrawal of earnings at any time results are taxable for a Traditional IRA. Earnings received through a qualified withdrawal from a Roth IRA are received tax free. Income limits restrict the deductibility of contributions into a Traditional IRA if the taxpayer/accountholder is a participant in an employer-sponsored retirement plan, whereas income limits restrict a taxpayer’s ability to fund a Roth IRA and participation in an employer-sponsored retirement plan is not a factor at all. The required minimum distributions at age 70 ½ that apply to a Traditional IRA are not applicable for a Roth IRA. 

5-5. Life insurance can provide the following benefits in retirement:

- Liquidity to pay the cost of dying. This includes funeral expenses, debts, administration costs of estate settlement, and estate taxes.
- Supplemental income through beneficiary arrangements for a surviving spouse. Proceeds can be paid through settlement options or invested in other income-producing investments to supplement income.
- Increases to retirement income. Permanent insurance can be surrendered for one of various settlement options.
- Social Security Income replacement to ensure that the beneficiary’s income level remains at a desired level.
- Bequests to family and charitable organizations. 

5-6. An annuity is a legal contract between between an insurer and the annuity owner. The annuity owner may or may not be the person entitled to receive the payments from the annuity (the annuitant).

- The annuity has two phases. The first phase is the accumulation phase in which the annuity owner builds up the value of the annuity by making investments called premiums, as with life insurance, and earning interest. The premium may consist of one payment (as with a single premium immediate annuity or single premium deferred annuity) or multiple payments (as with a flexible premium deferred annuity). The earnings grow tax-deferred. The second phase is the payout or annuity phase which occurs when the annuity contract is annuitized and the insurer makes periodic annuity payments to the annuitant. The amount of the payments depends on the value of the annuity, the age and gender of the annuitant (used to estimate the mortality experience), and the interest rate used by the insurer. Some annuities guarantee payments for a fixed period (e.g., for example, 10 years) while others guarantee payments for the life of the annuitant.
- The annuity has a death benefit, which applies only during the accumulation phase, or before the guaranteed lifetime payouts have begun. The annuity death benefit normally guarantees that a designated beneficiary will receive the greater of the accumulated value, or the premiums deposited minus any previous withdrawals. Any gains in the annuity will be taxable as ordinary income to the beneficiary upon withdrawal.
- Annuities typically include a declining surrender charge in the first 5 to 10 years. The surrender charges normally decline each year until they reach zero. To give some
access to funds, most annuities allow a “free withdrawal” amount each year of 10 to 15 percent.

- Partial withdrawals are taxed on a last in, first out (LIFO) basis. The first withdrawals from an annuity are earnings, and the owner is taxed on withdrawals until all the earnings have been distributed. The contributions are then received tax free. A 10-percent penalty tax applies to the taxable distributions made before the owner reaches 59 ½. Exceptions include those distributions made as a result of the owner’s death or disability, in substantially equal periodic payments over the life expectancy of the owner, under an annuitized contract, or attributable to investments made prior to August 14, 1982.

The various types of annuities can be categorized as follows:

- **Fixed annuities** provide a guaranteed, lifetime income at little risk to the policyowner, making them an ideal long-term investment for purposes such as retirement income planning. During the accumulation period, the interest rate fluctuates with changes in the underlying investments. However, the annuity never earns less than the guaranteed rate specified in the contract. During the payout period, the interest used to calculate payments will also be at least the minimum interest rate stated in the contract.

- **Variable annuities** pay a rate of return during both the accumulation and payout periods that may rise and fall depending on investment results. The owner of the annuity assumes the investment risk and allocates premium to a range of mutual fund type investment options called subaccounts.

- **Equity-indexed annuities** (EIAs), accumulated value is tied to a stock index of companies such as the S&P 500. Returns mirror the rate of return for the index to which it is tied. Usually there is a participation rate on the rate of return, meaning that the annuity will earn a percentage of the rate of the return of the index. For example, if XYZ Equity-Indexed Annuity were tied to the A&B Index and the A&B Index returned 10 percent, the annuity may only pass on 90 percent of that return, or 9 percent, to the annuitant. The rate of return may be capped, meaning the interest credited will not exceed the cap amount. For example, if the rate of return is 15 percent and the cap is 12 percent, the annuity would be credited with 12 percent.

5-7. Investments other than annuities include:

- **Negotiable Order of Withdrawal (NOW).** These accounts offer features of savings accounts: interest, liquidity, and withdrawal by check. Funds earn interest and are automatically transferred to the checking portion to cover checks. Restrictions on minimum balances or a limit on the number of checks may apply.

- **U.S. Government securities.** Treasury bills, notes, and bonds are U.S. Government securities that may be purchased in the over the counter securities market. Treasury bills (known as T bills) are available in amounts from $1,000 to $5,000,000 with maturity dates of 4, 13, 26, and 52 weeks from issue. Treasury notes (T notes) are available with 2 to 10-year maturities, in amounts between $100 and $1,000,000. Treasury bonds (T-bonds) are available in amounts greater than $1,000 with maturity dates of 10 to 30 years. Both T-notes and T-bonds pay interest every six months. The
interest is included in federal income taxes as it is paid. However, the interest is not subject to state or local income taxes.

- **Bonds.** These are securities issued by public or private corporations or federal, state, or local government units. They are an IOU given by the issuer to the purchaser with a promise to repay the principal, plus interest, at a specified future date. Mortgage bonds are secured by a mortgage on specific property owned by the issuer; debentures are secured only by the credit of the issuing organization. Debentures issued by large, secure organizations offer lower risk.

- **U.S. government bonds.** These are very secure and may yield just slightly less than high-quality corporate bonds. They are exempt from federal taxes, but not from state and local taxation, and are generally considered safe, reasonably attractive long-term investments.

- **Municipal bonds.** These are offered by local (municipal) governments to raise money. Interest earnings are exempt from federal taxes, and are generally exempt from state and local taxes.

- **Stocks.** Stocks represent ownership in a public or private corporation as a way to raise operating capital. The number of shares available is limited by company policy as well as by the demand from buyers. The tax advantage is the deferral of tax payments on growth until the stock is sold by the owner. Common stock provides the owner with ownership in the company that issued the shares. If the company fails, common shareholders may claim all assets that remain after all other creditors have been paid off. Preferred stock gives the owner first rights to any dividends issued by the corporation. Preferred shareholders may not have voting privileges in corporate decision-making as common shareholders do, and the preferred stock may be callable. Stock types are recognized according to investment object: blue chip, growth, defensive, cyclical, and speculative.

- **Unit investment trusts** (closed-end investment companies). These are management companies that invest in fixed portfolios of specific securities. Some hold a variety of diverse securities while others invest solely in one geographic area or industry. They neither redeem outstanding trust shares nor sell new shares on an ongoing basis. The investments are close-ended because they are fixed at the time of purchase.

- **Open-end investment companies** (mutual funds). These companies issue an unlimited number of shares on an ongoing basis and redeem these shares on demand. Shares represent ownership in the diversified securities portfolio. Types include balanced, diversified common stock, income, aggressive income, preferred stock, municipal bond, and money market funds. For the small investor there are a number of advantages to investing in mutual funds, such as diversification, professional management, liquidity, convenience, dollar-cost averaging, and economies of scale.

- **Real estate.** Ownership in real property, either directly or indirectly, is considered real estate. Advantages include appreciation, income from renting or leasing, and tax benefits. Investors can also participate in federal mortgage programs, such as Fannie Mae, Ginnie Mae and Freddie Mac, or in real estate syndicates or real estate investment trusts.
Tangible assets. This refers to property that has intrinsic value and potential for appreciation. Such property includes collectibles, precious metals and gems, commodities, and contract futures.

Limited partnerships. These are used to attract investors who do not want to be actively involved in a venture. A limited partnership is an association of two or more persons with at least one general partner and one limited partner. The limited partner has limited liability up to the limits of his or her investment as a passive participant (investor), and is not involved in management. The general partner provides everyday management duties.

Answers to Self-test Questions
5-1. D page 5.29
5-2. C pages 5.36, 5.37
5-3. D page 5.4
5-4. B page 5.15
5-5. B page 5.7
5-6. C page 5.21
5-7. B page 5.5
5-8. B pages 5.21–5.27
5-10. D page 5.11

Chapter 6

Answers to Review Questions
6-1. Common characteristics in the mature adult market segment include the following:

Attitudes about finances. The principal attitude for the mature market is safety and security. They want to preserve the fruits of their labor for their retirement years, which paradoxically requires some amount of market risk in order to combat the eroding effect that inflation can have on their assets. Early in this stage of the life cycle, many will still be concerned with accumulating assets for a future retirement. As they retire, they are apprehensive about spending down their assets. In either situation, they are worried about outliving their resources. What if they misjudge and spend all of their money before they die? Outliving resources ties in directly with their desire to remain independent. The last thing they want is to burden their children financially or otherwise. Older mature adults take great pride in their ability to remain independent and active.

Concerns about health care. Mature adults are sensitive to health care issues, especially those related to Medicare and long-term care. They understand the frailties of aging and the medical care associated with them, and they are concerned about the affordability of such care if it is needed.

Having more time. The primary goal of retirement is to have more time to do things not possible during the child-rearing and working years. Mature adults have time to
take trips to exotic places, get involved in community or non-profit organizations, pursue hobbies and interests, and learn new things. They have more time during the day to meet with you, unlike your younger clients or prospects.

- **Being deliberate.** Mature market clients tend to be more deliberate, because they have more time and are concerned about safety and reduced risk. For these reasons it may take them longer to make a decision and the buying cycle may be extended. The key is patience and to maintain a low-pressure sales approach.

- **Anticipating or entering retirement.** Retirement is something many look forward to with great anticipation. To others, it is something to dread. A major factor in this difference in attitude is the preparation made before reaching retirement. Too many people have not given any thought to the amount of money they will need.

6-2. Common needs in the mature adult segment include the following:

- **Financing health care.** Seniors are concerned about handling the costs of major illnesses, financing home healthcare, and nursing home fees. The increased cost of medical care has created a need for insurance. Medicare supplement policies offer seniors a way to fill in the gaps in the system’s benefits. Long-term care insurance policies offer seniors a method of dealing with the health care costs for chronic ailments that could easily cost $50,000 or $60,000 per year.

- **Increasing retirement income.** Most individuals are interested in increasing their spendable income; seniors are no different. Where seniors differ is in their sources of income. Prospects in the seniors market may or may not be working, but they will typically have a pool of accumulated assets representing a lifetime of work. There are a variety of privately-owned products that financial advisors can market to assist seniors in augmenting their retirement income, including annuities, mutual funds, and life insurance.

- **Reducing taxes.** Tax planning is another major financial concern of seniors. Some individuals pay less in taxes once retired, while others may actually pay more. Retirees’ paychecks are commonly replaced by generous pension checks. Mortgages may be replaced by huge amounts of equity in appreciated housing. However, with income tax deductions for mortgage interest and exemptions for children no longer available, many seniors find that they are paying taxes at higher, not lower, rates than in earlier years. Annuities and life insurance can offer substantial tax benefits. Deferred annuities can give seniors a way to shelter interest from current taxation, and can be used to lower the income taxes on Social Security benefits. Life insurance can also offer substantial tax benefits, allowing tax-free cash value accumulation, along with generous borrowing terms. The receipt of an income-tax-free sum at the death of a spouse can be used to handle unexpected living costs and replace the deceased spouse’s lost pension benefits.

- **Facilitating estate planning objectives.** Lowering estate taxes and estate settlement costs have typically been planning goals for seniors. Traditional estate planning has accomplished this by focusing on the disposition of assets at death. Unfortunately, traditional estate planning has often ignored the impact of long-term care. Too often individuals become incapacitated without having formalized plans for health care or
asset management. The unfortunate results have been smaller estates with sometimes little or nothing left for heirs. This situation has created a need for estate planning focused on today’s increased longevity, chronic care needs, and the desire to fund the dreams of future generations. Although prospects may have accepted the inevitability of death, you will find that many are still unprepared when it comes to the possibility of becoming physically disabled or mentally incapacitated. As a financial advisor, your access to life insurance, annuity, and long-term care insurance products—combined with appropriate legal tools and your senior clients’ financial assets—can make their goals a reality.

6-3. Medicare Part A Hospital Insurance helps pay for five kinds of care: inpatient hospital care, inpatient care in a skilled nursing facility following a hospital stay, home health care, hospice care, and inpatient mental health care. Benefits under Medicare Part A that cover inpatient care in a hospital or skilled nursing facility are based on a benefit period. A benefit period begins with the first day one enters a hospital and ends when the patient has been out of a hospital or skilled nursing facility for 60 days in a row (including the day of discharge). A subsequent hospitalization then begins a new benefit period.

6-4. Medicare Part B Medical Insurance helps pay for doctors’ services, outpatient hospital care, diagnostic tests, medical equipment, and other health services and supplies not covered by Medicare hospital insurance (Part A). Premiums are usually deducted from the participant’s Social Security check each month, and the amount changes from year to year. The standard annual deductible is $135 in 2009. For most services received under Part B, there is a 20 percent coinsurance amount beyond the annual deductible for all Medicare-approved charges. Medicare helps pay for covered services received from a doctor in his or her office, in a hospital, in a skilled nursing facility, at home, or any other location in the United States. Medicare medical insurance helps pay for medical and surgical services, diagnostic tests and procedures that are part of the treatment, radiology and pathology services by doctors, treatment of mental illness, and other services usually furnished in the doctor’s office, such as X-rays, services of a doctor’s nurse, drugs that cannot be self-administered, blood transfusions, medical supplies, and physical or occupational therapy.

6-5. Medicare Part C (Medicare Advantage) expands the choices available to most Medicare beneficiaries by allowing them to elect medical expense benefits through one of several alternatives to Parts A and B as long as the providers of these alternatives enter into contracts with the Centers for Medicare & Medicaid Services. However, beneficiaries must still pay any Part B premium. The Medicare Advantage plans include HMOs (most of the HMOs previously in the Medicare market became part of the Medicare Advantage program), preferred-provider organizations (PPOs), provider-sponsored organizations (PSOs), private fee-for-service plans, and private contracts with physicians. These plans must provide all benefits available under Parts A and B of Medicare.

Part D Medicare The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 added a prescription drug program to Medicare. Since spring 2004, most Medicare beneficiaries have been able to purchase a drug discount card. These cards can be sponsored by insurance companies, retail pharmacies, Medicare Advantage plans, and pharmacy benefit managers. Sponsors are required to pass any discounts they negotiate on the purchase of
drugs to cardholders, and to publish a price list of the drugs they cover. Certain low-income seniors will also be eligible for annual subsidies to help them pay the cost of prescription drugs. In 2006, Medicare Part D replaced Medicare-approved drug discount cards. Part D is a voluntary prescription drug plan that is available to all Medicare beneficiaries entitled to Part A and enrolled in Part B.

6-6. Most people need a medigap (Medicare supplement) policy to cover gaps in their coverage, or they risk consuming their retirement savings in one lengthy hospital stay. Medigap policies are designed specifically to cover deductibles and any coinsurance payments under Medicare. Most policies pay 100 percent of inpatient hospital care expenses for an additional 365 days after Medicare benefits are exhausted. These additional days are limited to 365 over the individual’s lifetime. There is a limit on the number of different medigap policy formats that can be sold. These regulations provide for standardized benefits and establish rules for selling medigap coverage. Although most companies do not offer all forms, there are 12 different approved forms for medigap policies (Plans A through L). State insurance departments determine what policies are available in that jurisdiction.

6-7. Reasons for the increasing need for long-term care and long-term care insurance include the following:

- **An aging population.** The single greatest predictor of the need for LTC is advancing age. This is due to the gradual and inevitable decline in physical and mental abilities that usually occurs as one ages.
- **Increased longevity.** People are living longer because advances in medicine have developed preventions, cures, and treatments for diseases and conditions that were once fatal. There are more people entering the time in life in which dependency on others is more prevalent. As life spans increase, the length of time people will need LTC due to such dependency will almost certainly increase as well.
- **Changes in the home.** Increased longevity is compounded by the significant change in family structure and lifestyles that have occurred over the past few decades in this country. Compared to previous generations, family members are simply less available today to meet the needs of their elderly parents and relatives because of the increased participation of women in the paid workforce, lower birth rates, and the geographic dispersion of families.
- **Cost of accelerating need.** This accelerating need will continue to drive up the future costs of long-term care because of growing numbers of patients, scarcity of facilities and staff, and continued building of new centers.
- **Few sources of money.** Some have the misconception that Medicare will cover their long-term care needs. However, Medicare does not provide custodial care for the elderly, and neither does a Medicare supplemental insurance policy. Medicaid requires an individual to have used up his or her assets before qualifying for coverage. Further, Medicaid payments are accepted by only some of the available long-term care facilities, limiting the alternatives from which an individual will be able to choose.

6-8. Six activities of daily living (ADLs) that might trigger the benefit of a long-term care policy include bathing, dressing, transferring, toileting, continence, and feeding. Other criteria may
apply for nonqualified policies, such as a physician’s certification that long-term care is medically necessary.

6-9. Benefits provided under a long-term care (LTC) insurance policy include the following:

- Facility care (nursing home care) encompasses skilled-nursing care, intermediate care, and custodial care. Care is on a continuum from acute to chronic. An emerging, more sophisticated integration of care techniques and facilities can accommodate people along the continuum and offer a wide variety of services for different levels of care. Although some people enter a nursing home for short-term rehabilitation or convalescence after a hospitalization, most people who enter a nursing home for longer stays are experiencing a chronic condition. They may need services for conditions such as dementia, Alzheimer’s disease, multiple sclerosis, or severe health conditions resulting from heart disease, stroke, diabetes, or arthritis. They may have lost their ability to perform ADLs, or become too sick or difficult for family members or others to care for them.

- Assisted-living facility care is provided in intermediate facilities for those who are no longer able to care for themselves but do not need the level of care provided in a nursing home. The number and types of these facilities are growing rapidly. Assisted-living facilities offer a more home-like atmosphere than a nursing home. Their relatively recent appearance as an LTC provider has witnessed explosive growth because they offer an effective form of care in the LTC delivery system.

- Home and community-based care provides for part-time, skilled-nursing care by registered and licensed practical nurses; for occupational, physical, and speech therapy; and for part-time services from licensed home health aides under the direction of a physician. Services typically include administering prescription medication, monitoring blood levels, wound care, diabetic care, incontinence management, and injections. Most people desire care at home because it provides an important foundation of emotional well being, control of one’s lifestyle, security, familiarity, privacy, and other comforts.

6-10. Most long-term care (LTC) insurance products today provide daily benefits on a reimbursement basis, based on the actual expenses incurred. The benefits paid are equal to the actual expenses up to the policy’s specified limit, the daily benefit amount, or maximum daily benefit. The other method of providing benefits is an indemnity policy. These pay out a specified amount of money no matter what costs are incurred for care in a nursing home or for home health care. Rather than restricting benefits to a maximum daily amount, some policies base benefits on a weekly or monthly benefit amount, such as $1,000, $2,000, or $3,000 or more. This can dramatically affect the amount of benefits paid.

As with life insurance benefits, inflation is a concern. Fortunately, most policies do offer inflation protection to help the daily benefit amount keep pace with future increases to long-term care costs. All policies have some outright exclusions such as self-inflicted injury, acts of war, and chemical or alcohol dependency. A policy will usually contain some form of pre-existing condition exclusion clause, excluding coverage for any condition for which the insured was previously treated within a certain time frame.
Although coverage and age-based premiums differ widely, typically very few companies issue new policies beyond the age of 80 or 85. Some companies do not have a minimum issue age. Other companies sell policies to persons as young as age 20. Still other companies have a minimum issue in the 40-to-50 age range.

Answers to Self-test Questions
6-1. A page 6.18
6-2. C page 6.16
6-3. D page 6.43
6-4. D page 6.3
6-5. C page 6.15
6-6. B page 6.42
6-7. C page 6.16
6-8. B pages 6.16–6.20
6-9. D page 6.43
6-10. D pages 6.2–6.4

Chapter 7

Answers to Review Questions
7-1. A well-executed product delivery can achieve three objectives:

(1) It can reinforce the sale by reemphasizing the objectives of the purchase. New clients who clearly understand how the product meets their needs will be less likely to let it lapse or move their accounts to a competitor.

(2) It can help the advisor gain the new client’s trust, and it sets expectations for future service and repeat sales. Set the expectations and schedule for future services such as periodic reviews of their insurance, investment, or financial plan. In addition, you can discuss other immediate or future needs identified during the selling/planning process. This may lead to follow-up sales or lay the groundwork for them down the road.

(3) It can offer another opportunity to obtain referred leads. A satisfied new client can be your best source of referrals. What better time is there to ask for the names of people, for whom your services and products might also be of value, than at policy delivery?

The following techniques are recommended for a successful policy delivery:

• For insurance products, there is an issuance process, namely underwriting, which results in a delay between the closing of the sale and the receipt of the product. It is critical that the advisor monitors the issuance process and takes appropriate action as needed. Communicate reasonable expectations during the closing interview, alerting applicants to any contacts, exams, and so on related to the underwriting process. The advisor should communicate with the applicant throughout the issuance process, especially if there are any delays. When the advisor receives the policy, he or she should review it to make sure that it is correct.
• Prepare for the delivery. Tie up any loose ends, making contact with any other advisors or referred leads as promised and being able to provide a report. Call to set up an appointment to deliver the product. Add a few professional touches, such as a product portfolio or policy wallet. Include any required information, such as an illustration or prospectus. Add any backup information. This includes product review checklists, summaries, company-approved information brochures, a list of suggestions, and information on claims procedures (if insurance product). Practice your presentation.

• Execute the policy or contract review. Briefly explain the policy or contract. Meet any delivery requirements, collecting any signatures or handing out required information. Review how to read annual statements. If necessary, resell the need to combat any perceived buyer’s remorse.

• Establish the expectations for an ongoing relationship.

7-2. According to the Merriam-Webster dictionary, a customer is “one that purchases a commodity or service.” A client, on the other hand, is defined as “one that is under the protection of another; a person who engages the professional advice or services of another.” It follows then that all clients are customers, but not all customers are clients. Clients are customers who follow your advice consistently, buy from you again, and refer you to others. The difference is important because a client values the relationship he or she has with the agent and will not defect simply to get a lower price. A client pays bills on time and has greater potential for repeat business and referrals. Thus a client is better for the advisor’s bottom line.

7-3. It is important to provide excellent service to clients for three main reasons:

• To facilitate customer retention. A strong client relationship can help prevent competitors from replacing your business. In this competitive climate, service is clearly a necessary defensive strategy.

• To result in repeat sales and referrals. Client building is also part of a smart offensive marketing and sales strategy as we see in the selling process. Experienced advisors report that as much as 75 percent of their new business comes from existing clients or referrals provided by these clients. Remember clients tend to refer people like themselves.

• To lower expenses. By being able to sell primarily to clients and people they refer, you can drastically lower your sales and marketing costs.

7-4. An advisor should monitor a client’s circumstances for the following:

• Insurance coverages. First, there’s a need to check that any insurance coverage is adequate to protect the needs the client desires to protect. In particular, it means evaluating whether or not the insured has the right coverages and the right amount of those coverages. Changes in insurance coverage could occur for various reasons including the following:

  a. additional needs discovered but not insured—For example, the original needs analysis uncovers that they need more life insurance or disability income protection, but they could not afford to cover these needs in full at the time of the original purchase.
b. additional needs due to life events—For example, if the client gets married or remarried, gives birth or adopts a baby, gets divorced, gets a promotion, or buys a new home, these events could trigger new life insurance or disability needs.

c. amount of current need increases—For example, if inflation spikes for several years, salary and expenses increase, or the original need was underestimated, there may be a greater need for coverage.

d. changing needs due to life events—For example, if the client’s children have left home, the life need may diminish, but a long-term care need may be felt more.

- **Life insurance values.** For permanent insurance, track cash values and policy dividends (if applicable) to ensure they are going to achieve anticipated cash goals for retirement or any other future goal. This is especially true with interest-sensitive and variable products, and participating policies where dividend values are of concern. Sometimes the amount of the need does not change but the type does. Here are two examples:
  a. term conversions—A client may have purchased a term policy to cover educational expenses and at some point realizes he or she will probably have needs beyond retirement. Perhaps his or her estate has grown or he or she would like to provide money for a charity.
  b. universal life death benefit option change—A client may find that his or her needs have diminished and now would like to focus on supplementing retirement income.

- **Automatic changes.** When automatic changes occur, communication with the client can help them adjust or perhaps take advantage of them. Some companies will provide for children insured through a children’s term rider to convert to a permanent policy without evidence of insurability. If the client or policyowner has purchased a guaranteed renewable-term policy the rates will increase at the renewal, and this presents an opportunity to communicate the increase and examine conversion possibilities. If the client has purchased the guaranteed insurability rider you can help him or her take advantage of it.

- **Investment needs.** Life events often a person’s needs for various investment products or his or her ability to fund them.

- **Investment asset allocation.** An investment portfolio rarely remains constant over the years. It is important to review the client’s asset allocation for investment products to ensure it remains within the client’s risk tolerance. In addition, a client’s risk tolerance may change over time.

- **Law changes.** Sometimes the concepts used to sell the policy may change due to law changes. This would require monitoring to be sure that the plan performance will take place as anticipated, otherwise changes may need to be made. Tax law changes often provide new sales opportunities. The most common areas impacted are income tax planning, retirement planning, and estate planning.

7-5. There are several key points to consider regarding the annual review:

- Lay the groundwork for the annual review at the first interview when you explain how you work and the services you offer. Tell the prospect that you help people
uncover their insurance and financial goals, create and implement a plan to achieve them, and then continue to monitor their plan to make adjustments as needed. This enables the prospect to understand how you expect to service their plan after it is implemented. At the policy delivery, your goal should be to leave with a date for your next review.

- Record keeping is extremely important. An updated master folder or computer record will help you prepare for the annual review. Keeping good records along the way will not only shorten your preparation time, it will also provide a more professional image. Make sure you record things like children’s names and ages, grandchildren, and so on. Record personal interests to help reestablish rapport. Also keep any policy notices that contain pertinent information on things such as cash value.

- Call to confirm the appointment. You also can let the client know in advance to bring any documentation he or she may need. Some advisors send a preapproach letter reminding the policyowner or client of the annual review service that they offer. They then follow up with a phone call to set the appointment.

- Refresh your memory by reviewing the needs analysis and any financial information that the client provided. Look at your interview notes to remember attitudes and values. Rerun policy illustrations if applicable, and compare the projected values with current values. Put together a game plan of areas where needs may exist. Review the client’s insurance plan and current progress in the plan. If appropriate, recalculate needs and note any shortfalls.

- Inquire about any changes in their current or future financial situation. Listen carefully and note any opportunities. Implement any plan changes or set any necessary follow-up appointments. An annual review is a perfect time to ask a client for referrals. There is a very high probability that they value and trust you because they agreed to have you review their insurance plan.

7-6. Two levels of service, or service packages that can be used in servicing clients based on your relationship with them, and them with you are:

- **The standard service package.** Excellent customer service is now the price of admission in financial services. It is the expected level of service and not the exception. This means you need to create a high quality standard service package for dealing with routine requests for changes and information for everyone, regardless of their value to your business. You need a system that ensures all customers and clients receive the service they need and allows you to capitalize on new marketing opportunities. Define what that package is. Communicate it to your customers. Deliver as promised. Excellent service puts you in a position to inquire about other needs. You can take care of clients and market other products and services you provide.

- **The extra frills package.** For some of your customers and clients, you will want to give a better service package that includes other services and frills. This means you will need to identify what services you will provide as frills. The purpose of the extra frills is to make every contact an opportunity to market by doing one (or all) of three things: create visibility, create awareness of the products and services you provide,
and create a sense of personal touch. Define your frills packages and deliver them. Make sure they are relevant, you can deliver them, and they are cost effective from both a monetary and time standpoint.

7-7. The purpose of monitoring and servicing is to build client relationships. Not everyone who purchases a product will want to become your client, and there will be people who buy from you that you would prefer not become your client. You will need to identify whom you want to be a client. With the ABC method, you segment your book of business into three categories or grades:

- “A” clients—These are people who believe in you and the products you sell. They are a source for repeat sales and referrals. Your long-term goal is to only deal with these clients. They merit your very best service.
- “B” clients—These are customers whom you wish to turn into clients, or customers who have purchased financial products from you in the past year, but who have not yet committed to a full client relationship. These are your “B” clients. To the “B” group you will offer a broader range of services than the “C” group. Your goal is to eventually drop them to the basic service group or to raise them to client status.
- “C” clients—These are people who have either demonstrated that they do not wish to enter into an ongoing client relationship with you, or you do not want to do more than your existing business with them. These are your “C” clients to whom you offer only basic services (for example, annual reviews, and follow up on information and service requests).

Once you have identified the three classes of clients, you can treat each accordingly in terms of the discretionary services you provide. In selecting which services to offer, distinguish between basic and discretionary services.

7-8. The marketing plan will apply target marketing concepts and will be built by answering the following questions:

1. What are my objectives? The first step of building a basic marketing plan is to identify your objectives, specifically, your income and activity objectives. There are three basic steps: (1) construct marketing funnels for your target markets and general market, (2) Determine income objectives, and (3) calculate activity objectives using applicable marketing funnels.

2. To whom am I marketing? Your basic marketing plan should include a brief profile of your target markets, defining the common characteristics and common insurance and financial needs, regardless of whether or not you can meet them.

3. What am I marketing? From the common financial needs you identified, select those needs that you are able to meet based on the products you sell and your level of training and experience.

4. How will I market to them? Your next step is to determine how you will market to your target markets. This includes the following: creating and implementing a position for your personal brand, implementing prospecting methods for identifying prospect names and contact information, implementing methods for creating awareness and interest of your products, creating and using scripts to set
appointments, anticipating objections, and outlining additional services you will offer to increase retention.

(5) How effective am I? The last part of a basic marketing plan is a plan for evaluating your results. This process will lay the groundwork for planning your next income period.

7-9. *Compliance* means following the laws and regulations, including company rules, which apply to the sale of all financial products. These are the minimum standards. *Professional ethics* is behavior according to principles of right and wrong—a code of ethics—accepted by one’s profession. By adopting, embracing, and practicing a professional code of ethics, the financial advisor will likely achieve the high standard of professionalism demanded by a career in financial services.

### Answers to Self-test Questions

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### Chapter 8

#### Answers to Review Questions

8-1. Common characteristics of the old-age market segment include the following:

- **Psychological changes.** There is a declining ability to acquire new intelligence, but a sustained ability to apply existing knowledge. Aging has little effect on the size of working memory, but it does impair the transfer of information from the short-term to long-term store. Hearing loss is very common. The loss of existing knowledge (for example, how to dress oneself) is a pathological change, not an aging one. The elderly have to come to terms with their changing role in life. Society causes the elderly to assume a dependent role through retirement and pensions.

- **Dealing with death.** Strong emotions and an increased awareness of death emerge as relatives, friends, and spouses die. There is a strong sense of nostalgia for the past, often accompanied by sadness and loneliness when the future is considered.

- **Nursing homes and assisted living.** Many in this age group face nursing home and assisted-living choices because of fragile health. Long-term care insurance and...
Medicare supplement (medigap) insurance are often issues of importance as a person begins to deal with the effects of aging.

- **Leaving a legacy.** The next generation takes on a new importance when people reach old age. A reconciliation of spiritual values and a final conclusion as to the meaning of life often provide members of this stage of life a legacy to leave to the next generation. They attempt to pass on their wisdom and knowledge about life. The liquidation and distribution of any remaining estate is considered. To many, the proper way to pass assets on to children and grandchildren is the most important objective. Many mature adults may have charitable intentions.

8-2. Common needs of the old-age segment include the following:

- **Updated will.** As with all ages, a will ensures that a person’s estate is dealt with in the manner he or she desires. By this phase in the life cycle, a will may not have been updated in a while, and relatives and friends may have predeceased your client or relationships with children have changed, thus making the will out of date. An advisor can provide good service by reminding clients to create a will, or update an existing will.

- **Lifetime income.** One of the biggest concerns for many people in the old-age market segment is the possibility of outliving their assets. The majority of old-age prospects and clients realize that Social Security is not adequate to sustain their desired standard of living. This need is even more acute for those who do not receive pension benefits from an employer. Immediate annuities are good products for this market segment.

- **Gifts to children and grandchildren.** Some members of the old-age market segment will want to leave a legacy to children and/or grandchildren. This objective may be achieved through bequests at death or gifts made during one’s life. Bequests at death may involve the distribution of assets, such as a house or investments and savings. Life insurance proceeds are another method for creating a legacy.

8-3. A seminar is an effective way to approach seniors. It is an educational and motivational meeting for people interested in your topic. The seminar’s purposes are to create awareness, motivate prospects to take action, and to set an appointment with you. They are not an attempt to make an immediate sale. The only selling that takes place in the seminar is the selling of yourself and your ideas; this will open up opportunities for one-on-one follow-up meetings in which selling of products can take place. Typically, seminars appeal to prospects who need information and have the time to seek it out—a description that fits prospects in the senior market.

8-4. When a person dies, property he or she owned will pass to heirs in one or more of the following ways:

- **By operation of law.** A typical example of this method is a home owned jointly by a husband and a wife. At the death of the first spouse, the surviving joint tenant gains full ownership of the jointly held property. Property not passing by contract, will, or operation of law passes under the laws of intestate succession.

- **By right of contract.** The prime example of this is life insurance that is paid directly to a named beneficiary.
• **By will.** If there is a will, the remaining property passes under the terms of the will once it has been admitted to probate. If there is no will, remaining property passes according to the state’s laws of intestacy, by operation of law.

• **By trust.** A trust is an arrangement in which assets are administered by a trustee for the benefit of others in a manner specified by the deceased.

8-5. When a person dies without a will (intestate), the courts take control of the estate and, in effect, write a will in accordance with the state’s intestate laws. It is unlikely that the state’s distribution would match most people’s personal wishes. For example, in most states a spouse does not automatically inherit all property when there are children. In the absence of a will, the court must also appoint an administrator of the estate and a guardian for the minor children. Normally, the courts prefer a relative as administrator, but if one is not available or willing to serve, the estate could end up in the hands of a professional administrator. This official generally takes 3 to 5 percent of the estate in fees each year. This arrangement offers little incentive to settle an estate quickly or to minimize the estate for tax purposes. The court would also select a relative as guardian if the children were orphaned, but without any guarantee of the choice the parent might have made. Because the court’s appointment does not carry the moral weight of the parent’s wishes in a will, children could become the object of a custody battle.

8-6. The will must meet technical and legal requirements. It must be in writing and properly executed according to the state’s laws. The will must be signed to indicate intent, and it must be attested to (verified) by the appropriate number of witnesses. Oral wills are generally not valid. No will takes effect until the death of the testator, the person making the will. Therefore it can be changed at any time during life. A new will can be written to revoke prior wills. Because only the original will is valid, it is important to keep it in a safe place that others know. A bank safe-deposit box is not suggested because access to it is limited. Only limited copies of the will should be made and distributed. The original should be left with the estate executor or attorney for safety.

8-7. Definitions:

• **Applicable credit amount.** The credit is an amount that can be applied directly against any gift or estate tax due, and is $1,455,800 in 2009. This means that a person with assets less than $3.5 million dying in 2009 generally will have no federal estate tax payable.

• **Marital deduction.** A deduction of 100 percent of property passing to a spouse either by gift or at death is permitted. To qualify for the deduction, the property generally must pass to the surviving spouse in such a manner that he or she has sole power of control during life or at death. In effect, the estate of one spouse can be passed to the other completely free of taxation, as long as it qualifies for the marital deduction. The marital deduction is merely a postponement of taxation at the death of the first spouse. The property that passes to a surviving spouse will be taxable at his or her subsequent death. Much estate planning is directed toward minimizing this result.

• **Three-year rule.** One strategy for decreasing the value of an estate is to transfer ownership of life insurance. However, the value of any life insurance is included in the estate if the transfer is made within three years prior to the death of the owner.
Ownership includes incidents of ownership that refer to a number of rights of the insured or the insured’s estate in the economic benefits of the policy. Examples of contractual rights that reflect incidents of ownership are the rights of surrender and the right to make policy loans, assign the contract, and change the beneficiary. One must relinquish all incidents of ownership to remove the value of life insurance from an estate.

8-8. The goal of life insurance in estate planning depends upon the client. For most people, life insurance is used to increase the size of an estate to provide for surviving family members. It could be the young family buying insurance as income replacement, to fund college educations for their children, to provide for mortgage redemption, or to build a nest egg for retirement. Life insurance provides the perfect estate enhancement to replace income if the breadwinner of the family should die prematurely.

For older clients and those who have built wealth, life insurance is used to provide estate liquidity. Their children’s support and educational expenses are usually things of the past. In addition, these older clients are nearing the end of their income-producing years, and should have less future income to replace. These people can purchase life insurance to provide death proceeds equal to the size of the anticipated shrinkage of the estate due to settlement and taxes.

Life insurance is the most effective way to supply needed dollars to meet federal estate tax obligations. First, the dollars, in the form of death proceeds, are free of federal income taxation. Second, if the life insurance is owned by someone (or some entity) other than the insured, the policy’s face amount will not be included as part of the decedent’s gross estate. Finally, a sizable death benefit may be purchased for pennies on the dollar in the form of premium payments.

8-9. Charitable gifts can produce three federal tax benefits:

- Income tax. When the donor itemizes deductions, charitable donations during the donor’s lifetime are usually deductible.
- Gift tax. With a few exceptions, qualified charitable gifts or bequests are exempt from gift taxes.
- Estate tax. Charitable gifts that become effective after the donor’s death may qualify for an estate tax deduction.

8-10. Some of the advantages your clients will realize by using life insurance as the vehicle of gifting are:

- leveraging the contribution so it will become a larger gift than otherwise possible with a straight cash contribution. It becomes a gift made on the installment plan through annual premium payments for the life insurance.
- receiving a current income tax deduction for donations made to pay premiums on a policy owned by the charity
- receiving a future estate-tax deduction for life insurance proceeds paid to a charitable organization upon the death of the donor
- creating a new asset and not depending upon other owned assets to make the gift
- avoiding the probate process for the life insurance that would create costs, delays, and publicity connected with the charitable gift to the settlement of the estate
- avoiding possible challenges by potential heirs
- avoiding creditor claims that could be attached to the other assets that pass by will
- creating, through life insurance, a self-completing gift that is fairly simple to arrange

8-11. Distribution planning is a major concern for older adults, who are concerned with maintaining their lifestyle in face of the threats of inflation and taxes. Careful projection of income and expenses, or cash flow analysis, is important in meeting future income needs in retirement. Annuities provide one source of guaranteed income in retirement. Annuities are categorized as immediate or deferred, single premium or flexible premium, or fixed or variable. Life insurance death benefits can be critical for the financial futures of surviving loved ones. The selection of the specific settlement option may be made prior to death by the policyowner or left to the beneficiary’s choice. Options include the following:

- **Lump-sum or cash proceeds.** Most payments to beneficiaries are taken as a lump sum cash payment or paid into an interest-bearing checking account. This option offers no protection against the creditors of the beneficiary. Lump-sum distributions allow the beneficiary to manage the money, either reinvesting it at a higher rate, using it to pay estate settlement costs or debts, or using it for whatever purpose they choose.

- **Interest income.** Under this settlement option, the insurance company holds the proceeds and pays interest to the beneficiary based on a rate of return guaranteed in the policy, or a higher rate based on current interest rates. This option preserves the capital for the future, and can allow the beneficiary to make cash withdrawals. This option is designed to distribute the full proceeds at a later date when the beneficiary is ready to receive them, or at the beneficiary’s death. The most flexible of all available settlement options, the interest option is also the only one in which income is fully taxable to the recipient. (With the other options, income is made up of principal and interest and only the interest portion is taxed.)

- **Fixed-period income.** Under this option, the company pays out both policy proceeds and interest earned in installments over a specified period. The income received depends on the amount of proceeds, the interest credited, and the time period selected. The fixed period payout for insurance proceeds offers no flexibility to the beneficiary and is not used unless a clearly defined purpose and time frame for need can be established.

- **Specified amount.** Under this option, policy proceeds, plus interest, are used to pay out a specified amount of income at regular intervals for as long as the proceeds last. The larger the payment, the shorter the period of income will be. This option is similar to the fixed-period settlement choice except that excess interest above the return guaranteed by the company extends the length of time for the payout.

- **Life income.** This is a settlement choice unique to the insurance industry. The promise is to pay a stated income as long as the beneficiary lives. At death, the contract ends. This describes a pure no-refund annuity. Whether the beneficiary lives to 101 or dies within the year, the annuity reverts to the company at death. For most, even though it may offer the highest return in income to the beneficiary during life, this option would prove unsatisfactory without a guarantee of return built into the...
annuity. Because of this, a more popular and commonly used life income settlement builds in a refund or period-certain guarantee.

- **Life income with refund.** The life income with refund option guarantees payments for the life of the annuitant. If the annuitant should die before all the proceeds have been distributed, the balance of payments would be paid, either in a lump sum or installments, to the annuitant’s beneficiary or even a third beneficiary, until all proceeds have been depleted. The annuitant is assured through this method that all proceeds will be paid out.

- **Life income with period certain.** Under this payout option, the annuitant receives payments for his or her entire life. In addition, he or she is given a guarantee that if he or she should die within a certain period of time (such as, 10, 15, 20, 25, or 30 years) the payment will be paid to a beneficiary for the balance of the time selected.

- **Joint and survivor life income.** Under this settlement option, income is provided for two people and is most commonly used by married couples for payment of retirement benefits. It can be set up to expire at the second death or to have the refund or period-certain guarantees built into the settlement. The joint income may be set up so that the survivor’s income continues at 100 percent of the amount paid when both annuitants were alive, or so that survivor income is reduced to a percentage of the full amount. The common arrangements are joint and two-thirds or joint and one-half. The income varies under the joint arrangements per $1,000 of proceeds depending on the difference in age of the recipients and their sex. The survivor payout percentage can be used to leverage more income during the joint payout if less is taken at the survivor payout.

**Answers to Self-test Questions**

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