

# [Amount of life insurance to purchase](https://assignbuster.com/amount-of-life-insurance-to-purchase/)

Correct Life Insurance Amount and section Correct Life Insurance Amount Life insurance trades a known value, the premium on a due date, for an unknown time of death and a known value of economic life. The economic value of life determines the benefit or face value of the policy. Arriving at this value requires a financial accounting of current conditions and future needs. The process proceeds as follows: 1. Assessment of current financial position. 2. Survey of current life insurance in force. 3. Estimate funds to clear the estate. 4. Estimate future income needs. 5. Anticipate special needs. This review follows these steps to a life insurance value. I am a 30-year-old man with a wife, same age, and two children, ages 2 and 4. I enjoy a good job paying $50, 000 per year, and my wife earns $30, 000. Our net take home pay is about $40, 000 after all deductions. If I should die early, I want my wife to be able to stay at home and parent the children full time. We have managed to save $25, 000 cash in checking and savings accounts. We have a portfolio of mutual funds, $48, 000, securities, $10, 000, IRAs, $6, 000, and a 401K with $6, 000. Our total liquid assets are $95, 000. Currently, I have three times earnings as a life insurance benefit at work and a $10, 000 pension death benefit for a total in force life insurance of $160, 000. Upon my death, my wife would have liquid assets of $255, 000. My death would cost $7, 500 in funeral expenses, $5, 000 deductible for medical insurance, $22, 000 to clear our installment debts and about $3, 000 in probate costs. These costs total $37, 500; so the liquid assets decrease to $217, 500. Insurance must replace all of our income for my wife to stay home. An after death adjustment period of two years costs about 150% of normal earnings for a total of $120, 000. The children will be dependent for another 20 years. Twenty years at $40, 000 is $800, 000 to replace that income assuming earnings on the money equals inflation. The kids will leave, but she won’t be able to collect social security or pension for another 15 years. A reduced income is necessary, perhaps $30, 000 per year, for a total of $450, 000. In her retirement, an additional $12, 000 per year will be paid by pensions. She will require an additional $18, 000 per year for 30 years. That is an additional $540, 000. The total income replacement is $1, 910, 000. I am now short $1, 692, 500. In addition to these needs, the mortgage, college educations and emergency money should be funded. The mortgage is $180, 000, college should cost about $80, 000 and a $50, 000 emergency funs is adequate. These sums add $310, 000 to the deficit for a total shortfall of $2, 002, 500. I will need to fund this shortfall with life insurance in the amount of $2, 000, 000. References Wiening, Eric A.; Rejda, George E.; Luthardt, Constance M.; & Ferguson, Cheryl L. (2007) Personal Insurance. Canada: Insurance Institute of America. Appendix A ESTATE CLEARANCE FUNDS       FUNERAL COSTS   $7, 500   FINAL MEDICAL BILLS   $5, 000   INSTALLMENT DEBTS   $22, 000   PROBATE COSTS   $3, 000   FEDERAL AND STATE TAX   $0 $37, 500         INCOME NEEDS years     READJUSTMENT PERIOD 2 $60, 000 $120, 000 DEPENDENCY PERIOD 20 $40, 000 $800, 000 NO KIDS AT HOME 15 $30, 000 $450, 000 RETIREMENT PERIOD 30 $18, 000 $540, 000         SPECIAL NEEDS       PAY OFF MORTGAGE $180, 000     COLLEGE EDUCATION FUND $80, 000     EMERGENCY FUND $50, 000   $310, 000 gross amount needed     $2, 257, 500         CURRENT BALANCE SHEET       CHECKING AND SAVINGS $25, 000     MUTUAL FUNDS $48, 000     SECURITIES $10, 000     IRAS AND KEOGH $6, 000     401K $6, 000   $95, 000                 CURRENT LIFE INSURANCE       GROUP LIFE $150, 000     PENSION DEATH BENEFIT $10, 000   $160, 000       $255, 000               $2, 002, 500 current income $50, 000     wife's income $30, 000     net $40, 000