Policy options in difficult times

Sometimes, some things are beyond our control, especially in times of economic uncertainty. When the economy slows down and people lose their jobs, one of the first things they cut back on is their insurance premiums. Let's take a look at some of the options available when the going gets tough

Friend for life

• What are the consequences of not paying your premiums within the grace period?

The policy contract provides for a "grace period" (usually up to 30 days), which gives you extra time after the due date for the payment of the premium.

During this period, you can still pay your premium and the life policy continues to be in force.

However, if you still do not pay after the grace period, depending on whether your policy has sufficient cash value, you will receive a notification from your insurer stating the following consequences:

1. Policy lapses — if insufficient cash value (usually within the first policy year). In this case, you will no longer enjoy any coverage and could leave you and your family exposed to financial risks.

2. The automatic premium loan (APL) has been applied in accordance with the life policy to keep your policy in force, if there's sufficient cash value.

However, you should be aware of certain terms and conditions of such an option and some of the other options available.

• What are the options available?

There's a clause inserted in your life insurance policy called the non-forfeiture option (NFO), which means you are allowed to stop paying premiums and the policy will continue to be in force but the coverage may be adjusted accordingly.

This clause is inserted to protect you as the policyholder.

In the event your policy is in danger of lapsing, the insurance company is required to provide you with the following four options:

1. Opt for automatic premium loan (APL) — by default.

2. Convert your policy to reduced paid-up (RPU) insurance.

3. Convert your policy to an extended term insurance (ETI).

4. To surrender your policy for its cash value, but leaving you with no more coverage (may not be advisable).

• What are the consequences of allowing my policy to go on APL?

This is the default option if you do not elect for any of the NFOs. An APL is when the insurance company extends a loan from your cash value to continue paying for your policy to keep it alive.

This may give you some breathing space, but you must be aware that there are interest charges on the loan extended to you.

The interest rate is decided by the insurer (typically from six to eight per cent), but may vary from year to year.

While you may continue to enjoy full coverage of all current policy benefits, these will be reduced by the amount of the outstanding loan together with all the interest charges later on.

This will reduce the benefits payable to your family members and therefore, it is advisable to repay your policy loans as soon as your finances permit.

• What are the consequences of converting your policy to RPU insurance?

This is where you give up the current face value (basic sum assured) of your policy and use the cash value to purchase a lower-face amount without having to pay for your future premiums any more.

If you elect for this option:

1. All the riders attached to your original policy, such as medical and health, critical illness, personal accident, etc. will be cancelled.

2. You will not be entitled to receive any dividend/bonus which may be declared by the insurance company.

3. You may be required to undergo a medical examination if you intend to convert the policy to its original terms and conditions and pay all outstanding premiums.

4. You may not be able to reinstate or revert to your original life insurance plan.

So, you'd better think carefully before selecting this option as in most cases, there's no turning back.

• What are the consequences of converting your policy to an extended term insurance?

This is where the basic sum assured in your policy remains the same, but you use your cash value to purchase a term policy.

The term of insurance will depend on the amount of cash value that will be used to purchase the term insurance on your attained age based on the due date on the premium in default.

The consequences of this option are the same as the RPU option and the main difference is that your coverage is maintained as the original amount, but the period of coverage is reduced accordingly.

• What are the consequences of surrendering your policy for its cash value?

This option may be taken as a last resort as it entails you losing your coverage.

In fact, you may need the coverage more so during tough times and it's not advisable to give up your policy, especially if you've paid only for a few years.

The amount that you stand to receive upon surrendering your policy prematurely will be far less than the premiums paid and it is best that you consider the three other options stated above.

Only in adverse financial circumstances where you really need this money should you go for this option.

■ Your Friend for Life article is contributed by the Life Insurance Association of Malaysia