



THE TERM VS. PERM ANALYSIS

INTRODUCTION

An individual may often need life insurance coverage to replace income for the family, repay debt obligations, or plan for a business succession or estate plan in the event of premature death. Although term insurance provides low cost death benefit protection when purchased at younger ages, the policy becomes increasingly expensive to maintain at older ages. Moreover, unlike permanent insurance, term insurance does not provide cash value accumulation that can be tapped to supplement income or to fund an emergency need. Essentially, term insurance can provide only temporary protection with limited opportunity for the continuation of coverage at older ages.¹

THE BENEFITS OF PERMANENT INSURANCE

Permanent insurance can be designed to provide both death benefit protection for lifetime and cash value accumulation potential based on a client's particular needs. In fact, permanent insurance may help an individual to recover the cumulative premiums paid into the policy and potentially more. The cash values of a permanent policy also grow

tax-deferred and may be available to supplement income or to fund an emergency need on a tax-favored basis.² And, unlike term insurance, certain permanent insurance policies may provide death benefit guarantees to age 100. In some cases, the death benefit of a permanent policy can even be accelerated during lifetime on a tax-free basis to cover qualified long term care expenses of the insured.

Although the John Hancock term products may include a provision to accelerate the death benefit³ in the event the insured becomes permanently and totally disabled and is expected to survive for one year or less, the provision does not allow for the acceleration of the death benefit to cover long term care costs. Depending on the type of permanent product chosen and the client's changing needs, the policy may be adjusted over time to accommodate cash flow needs, to switch the focus of the policy to maintain death benefit coverage, accumulate cash values, or to use the policy as an emergency fund to cover long term care costs if and when needed.

	Death Benefit Protection	Cash Value Accumulation	Acceleration of Death Benefit during lifetime to cover long term care expenses	Potential Death Benefit Guarantee to age 100	Flexibility based on changing needs
Term	Yes	No	No	No	No
Permanent	Yes	Yes	Yes	Yes*	Yes

* Guaranteed products and features are based on the policy's premium requirements and the claims-paying ability of the insurer.

THE LIFECARE BENEFIT RIDER⁴

The LifeCare Benefit rider, when available and included in a John Hancock permanent life insurance policy, accelerates the death benefit in monthly installments to cover qualified long term care expenses during the lifetime of the insured. The rider covers up to a maximum monthly percentage of the death benefit, chosen when the policy is issued. The maximum percentage is 1%, 2% or 4% of the net death benefit available when long term care costs are first needed. However, before the death benefit can be accelerated the insured must satisfy a waiting period which varies by state.⁵

The LifeCare benefit payments will be made until the insured no longer has long term care expenses, the net death benefit is exhausted or the insured is deceased, whichever comes first. The amount of the death benefit remaining at death, if any, will be paid as a death claim.

AFFECTS OF LIFECARE BENEFIT PAYMENT

Note that when the policy death benefit is accelerated to cover qualified long term care expenses, the death benefit is reduced dollar for dollar and the cash value and account value are reduced proportionately. In addition, a portion of each approved monthly LifeCare Benefit payment will be used to repay a portion of any indebtedness under the policy and will reduce the monthly payment amount for that period. There is also a monthly charge taken from policy cash values when the LifeCare Benefit rider is included in the life insurance policy.

QUALIFIED LONG TERM CARE SERVICES

The LifeCare Benefit rider covers qualified long term care services which include services needed when the insured is confined to a nursing home, an assisted care living facility or a residential care facility, and is receiving nursing, custodial, hospice or respite care; or the insured is receiving home health care, hospice care or respite care in his or her home, or in an adult daycare center.

THE TERM VS. PERM DEBATE

To determine which type of policy is appropriate for a client, a cost/benefit analysis is necessary. A comparison of the benefits of each type of policy can help the client to make an informed decision about which type of policy is appropriate. Clients should consider all of the following:

1. Determine the amount of life insurance required. A client's net worth, annual income, existing life insurance coverage and current and projected liabilities need to be assessed to determine the amount of life insurance protection needed and the cash flow available to fund the need. It is also important to ascertain whether a client's existing term policy has a conversion privilege to determine whether or not the term coverage can be converted to a permanent policy without further evidence of insurability.
2. Compare the long term benefits of permanent insurance. Although the annual cost of a term insurance policy may be less than the cost of a permanent one at younger ages, the cost of term rises significantly over time. It is important to consider the time period that insurance protection is needed and assess the long term total costs of each type of policy. These costs should be compared to the net annual benefits that each type of policy provides over the client's lifetime, including the net death benefit, net cash value accumulation, net supplemental income, and the amount of death benefit acceleration available to cover long term care costs.
3. Consider the types of permanent insurance policies available. The type of policy chosen should be based on a client's risk tolerance, the client's requirement for premium and death benefit guarantees, available policy features and riders desired, supplemental income desired, the client's cash flow constraints and need for flexibility to accommodate changing needs over the lifespan.

HOW IT WORKS

A permanent policy can be designed to take into account a client's death benefit needs and any income or lump sum cash required in the future. The premiums, net of life insurance and administrative charges, are invested in an underlying fixed account or one or more investment funds. The design of a permanent policy takes into account the client's risk tolerance for specific types of investment funds, including stock and bond funds, as well as the client's preference for fixed accounts.

BENEFITS OF PERMANENT LIFE INSURANCE

- **Permanent Death Benefit Protection** – The death benefit provides protection against economic loss.
- **Cash value accumulation** – A permanent policy has the potential to accumulate cash values on a tax-deferred basis and may help the insured to recover premiums.
- **Tax-favored income** – Distributions from cash values may be taken on a tax-free basis as long as cumulative withdrawals do not exceed cost basis and policy loans are taken thereafter.
- **Death benefit acceleration to cover long term care costs** – When the LifeCare Benefit rider is included in the permanent policy, the policy's death benefit may be accelerated to cover qualified long term care costs.
- **Flexibility** – The permanent policy may be designed to provide the insured with the flexibility to address changing needs, such as a need or ability to adjust premium payments and or to switch the focus of the insurance protection from death benefit protection to cash value accumulation or vice versa, or from death benefit protection to long term care protection.

CONSIDERATIONS

- **Cash flow** – In the short term, a permanent policy requires a higher cash flow commitment.
- **Death benefit reduction** – Loans and withdrawals taken from the policy will decrease the amount of the death benefit and may potentially cause the policy to lapse if additional premiums are not paid. If LifeCare Benefit rider payments are made, the death benefit will be reduced proportionately as well.
- **The low cost of term insurance** – The cost of term insurance at younger ages can be significantly less than the cost of permanent insurance. It is important to consider the client's short-term and long-term goals of owning the life insurance as well as cash flow constraints.
- **Additional Premiums may be required** – Depending on the performance of the underlying investment accounts of a variable life insurance policy, the cash values available for loans and withdrawals may be worth more or less than the original investment amount. Additional premiums may be required to sustain the policy.
- **Limitations** – The life insurance policy can provide death benefit protection, cash value accumulation, or funds to reimburse long term care expenses. Although the policy may provide some of each of these benefits or a combination of them, the policy cannot provide all these benefits in full.
- **Additional tax, risk and expenses** – The purchase of life insurance has costs and risks associated with it, including the cost of insurance. Purchasing variable life insurance also involves investing in underlying investment accounts that correspond to a client's investment objectives and level of risk tolerance. The types of risks associated with investing in these accounts include potential market, portfolio, inflation and international risk. For more information, please refer to the product prospectus.

CASE EXAMPLE

Timothy Walker, age 45, is busy building a successful business. Tim is concerned about his family's financial well being in the event of his premature death. He wants the security of knowing that the current level of income available to his family will continue and that his business debt and mortgage will be repaid upon his death. He has determined that his family will need \$250,000 of cash assets should he die. He is now assessing the costs and benefits of a term and permanent life insurance policy.

The chart below compares a 20-year John Hancock term policy with a death benefit of \$250,000 to a John Hancock Accumulation VUL policy. The annual term premium is \$488 while the annual Accumulation VUL premium is \$2,594, both based on a male, non-smoker, preferred underwriting risk. Each chart illustrates, in specified years, the amount that will be available during lifetime and at death in each type of policy. In the term insurance scenario, it is assumed that the difference between the term and permanent premium is invested annually in a hypothetical "side fund" that is illustrated to grow at a pre-tax growth rate of 7.28%, net of management fees.⁶ The side fund is assumed to be taxed annually at a blended rate of 5.33% based on 35% ordinary income tax and 15% capital gain.

Note that in order for distributions from the cash values of a life insurance policy to be tax-free, withdrawals up to basis in the policy can be taken first. Thereafter, policy loans can be taken on a tax-free basis. However, policy withdrawals and loans will reduce the policy death benefit and cash values available. Loans from the policy will also be subject to loan interest charges, further reducing the policy's death benefit and cash value.

TERM VS. PERMANENT COMPARISON – DROP TERM COVERAGE								
		John Hancock 20-Year Term and Invest The Difference*			Permanent Insurance: Accumulation VUL			Difference
Yr	Age	Total Outlay	Death Benefit Plus Side Fund	IRR on Death Benefit**	Total Outlay	Death Benefit	IRR on Death Benefit	Additional Amount with Permanent Insurance
25	69	\$51,880	\$98,502	4%	\$51,880	\$250,000	10%	\$151,498
30	74	\$51,880	\$127,704	4%	\$51,880	\$250,000	8%	\$122,296
38*	82	\$51,880	\$193,474	5%	\$51,880	\$250,000	5%	\$56,526

* Assumed life expectancy

** Internal Rate of Return on death benefit. The IRR on death benefit is equivalent to an interest rate at which the amount equal to the illustrated premiums could have been invested outside the policy to arrive at the net death benefit that the life insurance policy provides. The data shown is taken from an illustration. It assumes a hypothetical rate of return and is not a representation of expected future results. Unless indicated otherwise, these values are not guaranteed. We urge you to request a basic illustration showing the impact of 0% and maximum sales charges and the impact it will have on policy cash value and death benefit.

The Accumulation VUL includes the LifeCare Benefit rider. Unlike the taxation of the Side Fund, the cash values of the permanent policy are assumed to grow tax-deferred. The data shown is taken from an illustration. It assumes a hypothetical rate of return and is not a representation of expected future results. Unless indicated otherwise, these values are not guaranteed.

The LifeCare Benefit rider can be exercised during the insured's lifetime. However, any policy withdrawals or loans taken prior to the exercise of the rider will reduce the amount of the death benefit that can be accelerated. If no withdrawals or loans are taken from the policy during lifetime, the LifeCare Benefit payments would be calculated as follows:

MECHANICS OF THE LIFECARE BENEFIT RIDER INCLUDED IN PERMANENT POLICY				
Premium	Initial Death Benefit	LifeCare Maximum Monthly Benefit %	Amount of Monthly LifeCare Benefit	Potential Months of LifeCare Benefit Payments
\$2,594	\$250,000	4%	\$10,000	25 months

- 1 A conversion privilege may be available on some term insurance policies in which the insured may convert the policy to a permanent policy within a period of time and without evidence of insurability. This privilege can be valuable if the insured's health has deteriorated and permanent insurance coverage is needed.
- 2 Withdrawals and loans from a life insurance policy classified as a Modified Endowment Contract (MEC) may be subject to income tax, and a federal tax penalty if the withdrawal or loan is taken prior to age 59^{1/2}.
- 3 Benefits may be taxable under current tax laws. Policy must be owned by the insured for the term policy's accelerated death benefit provision to apply. Clients should consult their personal tax advisors regarding the tax implications of benefits received under the Accelerated Benefit. This provision allows the insured to receive up to 50% of the death benefit of the contract, reduced by one year's interest at current rates, to a maximum of \$1 million.
- 4 The LifeCare Benefit rider may not be available in all states.
- 5 The waiting period is typically 100 days but varies by state.
- 6 In order for distributions from the cash values of a life insurance policy to be tax-free, withdrawals up to basis in the policy can be taken first. Thereafter, policy loans can be taken on a tax-free basis. However, policy withdrawals and loans will reduce the policy death benefit and cash values available. Loans from the policy will also be subject to loan interest charges, further reducing the policy's death benefit and cash value.



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