

Extended Term Insurance

Life insurance is a safety net that serves the purpose of protecting your loved ones from monetary hardships after your death. Some states of the US have made it compulsory for people to buy the mandatory types of life insurance for protection of their dependents.

[Life insurance is mainly of two broader categories:](#)

1. Term Life Insurance Policy
2. Permanent Life Insurance Policy

What is the difference between Term Life and Permanent policies?

It is important to understand the difference between the two if you're planning on going a life insurance shopping spree. Term life as the name shows, is for a specific time span ranging from 10-30 years. Whereas permanent life policies last for a lifetime.

Major differences between the two include:

1. [Term life](#) has cheap premiums, [permanent life](#) policies are 15 times costlier.
2. It does not offer cash value while permanent life offers a cash value component.
3. Term life pays nothing if you outlive the term, permanent have 100% guaranteed death benefit payout to dependents.
4. This is more popular due to affordability; permanent life policies are quite reliable but expensive.

Contents of this comprehensive blog for explaining the extended term insurance are:

1. [What is the cash value component of any policy?](#)
2. [What is extended term insurance?](#)
3. [How is extended term insurance calculated?](#)
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What is the cash value component of any policy?

Only permanent life policies have the cash value account. The heavy premiums for any life insurance policy every month go three ways:

1. Funds the death benefit payout for dependents, can only be used after the death of the policyholder.
2. Funds the cash value, it can be used by the policyholder when he is alive for emergencies, and has an interest accumulated on the cash too.
3. It funds the insurance firm overhead and monthly costs.

Cash value is a distinctive selling point of the permanent life insurance policies. Moreover, it offers comfort during the life of the policyholder and he borrows loans or money from it, for major lifestyle improvements or medical emergencies. Lastly, the money in death benefit and cash value is 100% tax-free.

What is extended term insurance?

Now that we have a clear picture of cash value, it is easy to understand an extended term insurance concept. It is the simple fact that if and when, any policyholder of a permanent life insurance policy becomes unable to keep up the heavy monthly premiums, any more; he switches his permanent policy into a cheaper term life.

This can be due to various reasons: he might have lost his job, he might have run out of assets from which he paid the premiums, he might have some major cash flow breakdown. Nevertheless, what the reason might be, once he knows he cannot continue the premiums, he understands that the policy can lapse.

Usually there is a 24 hours to 30 days' grace period, if he acts sensibly, he can call up his agency and inform them about the cash flow sabotage. So, he can inform them that he wants to convert his permanent policy into a term life. It is a very practical move chosen by the majority of the population.

Now the life insurance agency considers how much money he has accumulated in his cash value, based on this and many other factors, he can switch for a term life. Obviously, the best part is he can keep the coverage and he does not have to pay premiums any longer, premiums are withdrawn from his cash value onwards.

How is extended term insurance calculated?

Let's elaborate this with a simple example, suppose a person bought a whole life insurance policy for \$200,000 coverage. And he has been paying his premiums for a decade and his cash value has reached \$35,000 by now. Now, he lost his job and is unable to keep up the premiums any longer.

So, he calls up the life insurance agency and informs them and asks them to let him convert his whole life to a cheaper term life, and tells them that he cannot pay premiums for term life either.

Consequently, the life insurance agency will set up a meeting with him, together they will evaluate these:

The total cash amount in his cash value is \$35,000.

They will ask him what term he is looking for, if he says 20 years, he gets a smaller coverage term life since he has to pay premiums for a longer time through his cash value \$35,000. It might be \$25,000 coverage he might be able to buy for 20 years.

If he says he is 80 years old now and wants to extend for only 10 more years, they'd give him \$75,000 coverage for next ten years and his premiums would be paid from his cash value \$35,000.

The new term life coverage is decided with the mutual consent of the policyholder and the agency. **It depends on cash in cash value, and the term time you choose.**

What are the advantages and drawbacks of extended term insurance?

The advantages are obvious; you do not make more premium payments, your last permanent policy cash value becomes your savings to pay for future term life premiums, your coverage is not lost but converted, you never went uninsured by selling the policy or surrendering it. Your dependents will get full death benefit payout of new term life after you pass away.

Only small drawbacks such as if you outlive this term life, you go uninsured and your dependents get no death benefit payout. It is highly unlikely though! You lose your cash value for good, if you have any cash emergency now; you cannot draw a loan or money against the previous permanent policy's cash value. Now it is dedicated to making your monthly term life premiums.

What is a non-forfeiture clause and why does it exist?

For permanent policies, this non-forfeiture clause exists, to facilitate the policyholders if they cannot keep up premiums. Since it happens a lot; the law has been forged to manage the transition period.

There are following ways to manage a life insurance policy during **grace period**, when you become unable to continue premiums:

1. Let the life insurance **policy lapse!**
2. **Surrender** the life insurance policy.
3. Go for selling the life insurance policy, aka **life settlement**.
4. **Convert your permanent policy into a term life policy** by giving up your cash value account to make future premiums.

Last option is the most practical one since it keeps your dependents insured and you no longer have to pay the monthly premiums.

However, selling or surrendering will not give this much benefit. When you sell your permanent life insurance policy, it has probability of getting sold in the secondary market based on:

1. You are older than 65 years.
2. Policy coverage should be more than \$100,000.
3. You have some chronic or fatal illness diagnosis.

Even then, what you get in exchange for selling the policy is way less than the policy's actual coverage. Similarly, when you surrender it in grace period, you will receive the full refund of the premiums you've made so far, your dependents go uninsured and it is not a fruitful trade off.

No matter if your [life insurance policy](#) is term life or permanent life; make sure you add the rider for long-term insurance care for taking care of your spouse or yourself from your policy in old age. For a permanent life insurance, you must have a long term care insurance at hand, for paying the medical bills in old age.

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