Is it worth it?

Read the fine print when considering mortgage life insurance

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YOU'VE searched hundreds of classified ads and scoured countless neighbourhoods for that perfect home, scrimped and saved for the down payment, and now you're ready to take out a loan on the biggest purchase of your life.

Chances are, your bank representative will ask whether you want to take out mortgage life insurance.

In exchange for paying a monthly premium, the bank promises to take care of your mortgage should you get carried off to the pearly gates before your loan is paid off. No need to worry about your family being saddled with burdensome mortgage payments. With the application process taking mere minutes, you'll be approved for the insurance before you can yank the "for sale" sign off the property and become a proud Manitoba house owner.

It seems to make sense, even though you have to confront the daunting prospect that sometimes a mortgage can outlive you.

But hold it right there. You may want to think twice before you sign those papers. Many financial planners warn that mortgage life insurance has some significant pitfalls that could have you overpaying for peace of mind -- or, in the most unfortunate circumstances, paying for a policy your family won't be able to collect on.

"The banks have a captive audience and they're going to sell their products during a very emotional situation when people are going to answer yes, not knowing whether they're going to be the best or not," cautions Mark Halpern, a Certified Financial Planner and founder of illnessPROTECTION.com Inc. in Toronto. "People need to sit down with a competent professional to see how this fits in with overall financial planning."

"This is not an area where you want to be an impulse buyer, and the results of making the wrong decision can be catastrophic," Halpern adds.

Mortgage life insurance is not to be confused with mortgage loan insurance, which is typically required by lenders when homebuyers make a down payment of less than 20 per cent of the purchase price.

Life insurance sold by mortgage lenders is a form of creditor insurance and differs from personally owned insurance policies sold by insurance agents and brokers.

It has come under increasing criticism because it uses "post-claim underwriting." That means a detailed analysis of whether a person can collect is done only after a claim is filed. Sometimes, an unknown health problem at the time of signing can make certain claimants ineligible.

The banks may ask you a short list of 10 or fewer medical questions when they're getting your signature on the dotted line, but they won't thoroughly delve into your health records until a claim is made, notes Valerie Chatain White, a Certified Financial Planner in Winnipeg. "During post-claim underwriting they will look at everything and question it to death."

A routine test at the doctor could be used as justification by an insurer to have your claim denied, if it wasn't mentioned in your initial application.

Mortgage life insurance is also not portable should you sell and purchase another home. You'll have to reapply, and could be hit with higher premiums if your health has deteriorated or if you're deemed a higher risk -- say, if you started smoking.

MaryAnn Kokan-Nyhof, a Certified Financial Planner in Winnipeg, tells the story of an elderly Winnipeg couple that had moved their mortgage to another bank that offered a better interest rate. Just as they were switching, the unforeseen happened, and the husband suffered a heart attack. Just like that, they became ineligible for a mortgage life insurance policy with the new bank.

"She was just floored because she was sure she had it from the first place," says Kokan-Nyhof. "Fortunately, he didn't pass away but he can't get insurance any more."

Mortgage life insurance is also criticized for maintaining the same premiums even as you pay off your home. In effect, the more the outstanding balance drops, the less your family can collect should you pass away, and the more expensive each dollar of coverage will be.

Halpern contends that, when examining comparable products, term life insurance is often priced the same or better than mortgage insurance.

While mortgage life insurance ultimately protects the bank by making sure the mortgage gets paid off, personally owned insurance gives you the flexibility to decide where the money goes.

Kokan-Nyhof says she almost always recommends individual life insurance over mortgage insurance. "One of the main reasons is individual life insurance belongs to you. You own it. The beneficiary is whoever you name it to be. It isn't the bank first in line for the money."

Adds White: "A person is actually better off to own their own insurance and work out their own financial plan so you know how much you need to pay off your debt, including your mortgage and car, but over and above that, how much does your family actually need to live on."

Mortgage life insurance can be bought and cancelled at any time while carrying the mortgage loan, notes Halpern. But if you do decide to switch to term insurance, make sure you don't cancel an existing policy before being approved. You could be in for a nasty surprise if a bank turns you down for a new policy.

"Do the application, do the medicals, pay for the first premium, and then go ahead and leave the mortgage insurance," Halpern advises.

White recommends sitting down with a licensed broker or financial planner before purchasing insurance. "There are so many nuances out there right now, it is difficult for the consumers to really know, 'am I comparing apples with apples?' And until you drill down and get to the pure cost of insurance you may not really know."

Matthew Cram, a spokesman for TD Bank in Toronto, defends mortgage life insurance as a product that is easily accessible at bank branches everywhere.

"Many Canadians find it difficult gaining access to an insurance broker whose main priority is to focus on higher amount policies and sophisticated solutions for high net worth individuals," Cram contends.

He says the "vast majority" of mortgage life insurance claims get paid, and advises consumers to read through the questions on the application process carefully. "Then, as long as they answer appropriately, then they should feel confident that they are protected."

He says while term insurance may make more sense for some people, for others the two products can work together. For instance, if you're starting a family, you might want extra insurance to cover a mortgage liability for a particular time period, like when your children are still living at home. Mortgage life insurance can also protect a family's largest asset when their total insurance needs haven't been mapped out yet.

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Apples to apples

There are so many competing insurance products on the market it can be difficult to get a true comparison of their costs.

Banks also now often throw in disability and critical illness insurance as part of mortgage life insurance packages, which could make them worth considering based on the extent of your coverage needs. In many instances, though, mortgage life insurance alone can be more expensive than personally owned term insurance, according to several financial planners.

To get an idea of what term life insurance will cost, check out www.getterm.cc, a website run by Compulife Software Inc. that life insurance brokers often use.

Suppose you're 40 years old, in excellent health, a non-smoker and taking out a $200,000 mortgage. RBC's Insurance HomeProtector plan would cost $40 a month for single coverage. By comparison, term life insurance premiums, according to that website, range from $21.51 to $40.80 based on a 10-year term, and $31.14 to $67.27 for a 20-year term. That's just a rough comparison, but it does illustrate term insurance can offer the lower premium.