Buying child life insurance

By Michelle Warren • Bankrate.com

Eileen McGeough bought life insurance for her two children after her neighbour's teenage son was killed in a car accident almost 20 years ago. The sudden death and watching the family struggle in the aftermath left McGeough feeling vulnerable. At the time, the young mother knew she wouldn't have the money on hand to bury one of her own children. For $15 a month per child, life insurance gave her some peace of mind.

"You don't think about these things until something happens," says Caledon, Ont.-based McGeough. "I just got scared and thought, God forbid, should anything happen it would be one less thing you'd have to deal with."

The average cost of a funeral is $5,500, according to the Board of Funeral Services, but flowers, a reception and casket push it to $9,000 or $10,000. McGeough's admits her $13,000 payout would ease the financial burden, although it would do nothing for the emotional pain.

It's that stark reality, an uncomfortable juxtaposition, which often makes child life insurance a bit of a taboo subject: People don't want to think about their child dying. But products and the way people view insurance has evolved since McGeough bought her policy. Back then it was marketed two ways: cover funeral costs and save for university.

"People used to use it as an education fund, but it's less likely these days," says Lorne S. Marr, founder of LSM Insurance in Markham, Ont. With the introduction of the Canadian Education Savings Grant in 1998, which matched 20 per cent of a family's contribution to a Registered Education Savings Plan (RESP), the popularity of child life insurance waned.

Insurance is a viable investment tool

But attitudes are shifting and people are looking at child life insurance in a new light, says certified financial planner Mark Halpern, president of illnessPROTECTION.com. "It really has to be viewed in the perspective of overall financial planning ... Think investment."

In other words, get out of the mindset of something bad happening to your child and instead view it as a tool to help plan for your child's future.

A life insurance policy is a useful tool that allows you to grow money on a tax-free basis (with relatively consistent and decent returns when compared to the performance in recent years of traditional investment tools). Parents can choose a plan that allows them to transfer ownership of the policy, including investments, tax free to a child once the child reaches 18. These plans then allow the child to make withdrawals for any purpose -- education, travel, buying a home -- and although the withdrawals are taxed, it's not likely to be much if the child has little or no other income.

Insure parents first

Experts agree, however, that when it comes to life insurance the first order to business is making sure parents have coverage. The primary reason for life insurance is to offer financial protection should a family's primary-income earner become incapacitated.

In most cases, the death of a child "has an emotional impact, but not a financial impact because the child doesn't have an income," says Marr. "Any time you're considering a child policy keep in mind that it's usually much less important than adequate insurance for parents. You should be looking at the insurance dollars on yourself before your child."

Family history an importance consideration

There are, however, poignant arguments for insuring children. One of which is insuring a child at a young age guarantees the ability to get insurance in the future. This could come in handy if your child were to develop health problems, such as asthma or cancer, which could make it difficult for them to get insurance when they are older.

"The one good thing is they are still going to be able to maintain that coverage," says Marr. Certain policies allow a child to upgrade their insurance in adulthood. This is an important consideration for those with family history of disease, such as heart or diabetes. It also comes in handy should your child opt for what's considered a more dangerous profession, such as a firefighter, which usually involves higher premiums.

"The best time to buy insurance is when someone is young and healthy," says Halpern. Permanent policies also allow children to lock in at favourable rates; they will pay a fraction of the cost as compared to waiting until adulthood to start.

Most people have the wrong insurance

The thing to keep in mind when shopping for insurance is that not all policies are created equal. There are many different types of insurance -- term, universal life or whole life -- and you need to find the one that works for your family, whether you're looking at it as a legacy planning tool, savings mechanism or to cover funeral costs. Term, for instance, is temporary protection with no investment or cash value that is basically used to cover burial expenses, while whole and universal cost a little more, but offer different kinds of investment opportunities.

"Most people don't have the right type of insurance," says Halpern. "It comes down to making sure people have the right advisor -- a problem solver as opposed to a policy pusher."

In most cases parents can expect to pay $20 to $50 a month (depending on extent of coverage and existing health circumstances) for a stand-alone policy (one they can parlay into adulthood), or do what's known as a ‘child rider' where essentially they tack it on to a parent's existing policy for $3 to $10 a month.

For parents like McGeough, it's an investment that continues to pay off in peace of mind. Although her children are both grown, she maintains the policy. "I feel security having it there," says McGeough, adding "There's also a part of you that thinks, way down deep inside, that if you have it nothing (bad) will happen."

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