Implementing the Solutions

By John Kong and David Choo

After analysing your financial situation and aspirations, take the next step by implementing your plan.

IN THIS FIFTH article in this series of Financial Planning, the subject of implementing the solutions is covered. Great care must be taken not only by the Financial Adviser but the client as well to obtain effective solutions to meet their financial objectives.

Implementing the Solutions

Having analysed your financial situation and understood your financial aspirations, the next step would be for you to agree on an acceptable plan for implementation. The plan your adviser proposes is likely to consist of financial products and professional services from complementary disciplines. In this issue, we will first consider some of the important factors or principles that will help you in evaluating the suitability of a proposed product. In the next issue, we will look at possible solutions that are suited for some of the more common financial objectives.

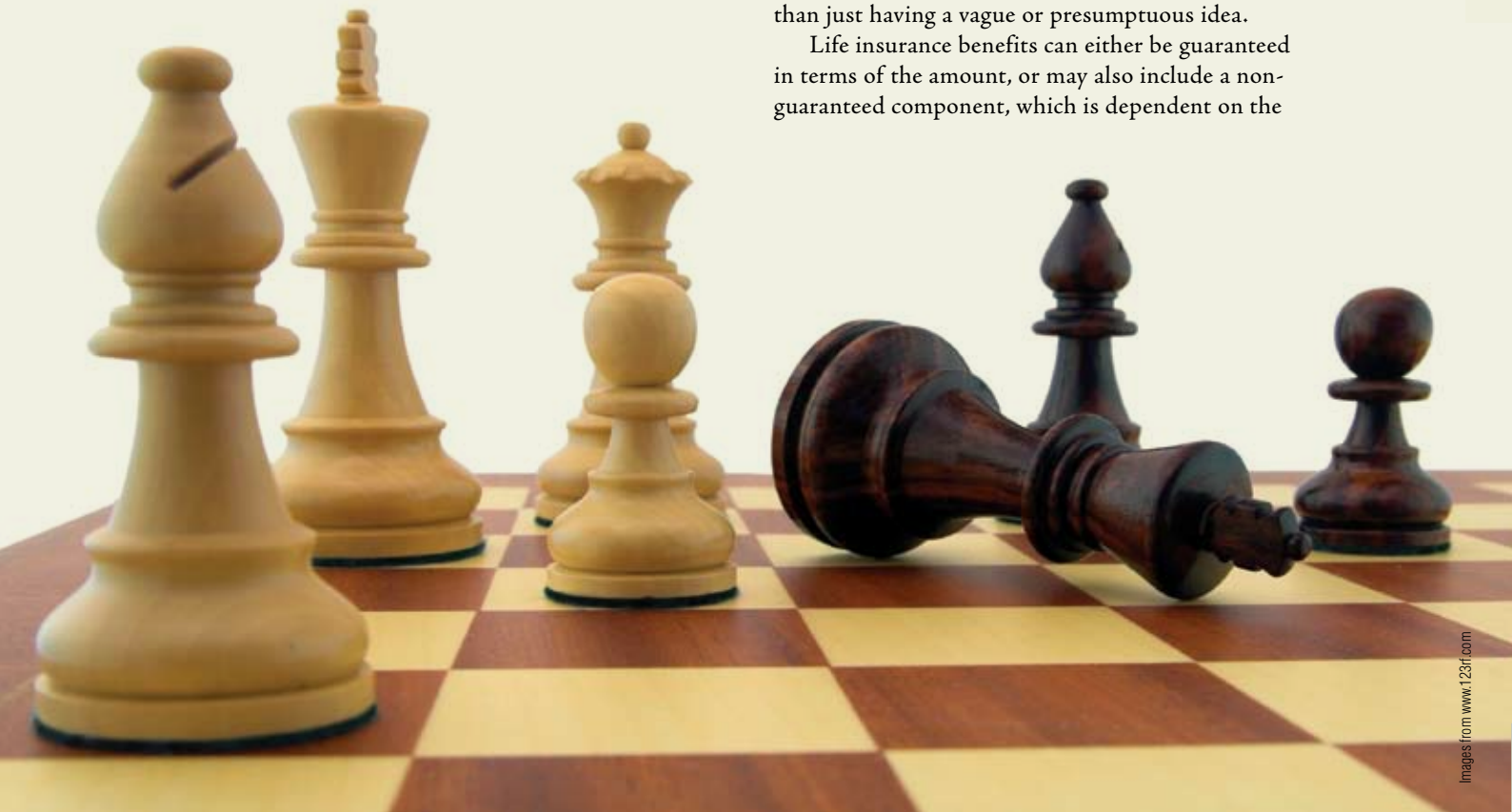
Product Features

INSURANCE PRODUCTS

Your adviser is obliged by legislation to show the product summary of the plan proposed. Read carefully the contents and ask questions to clear any doubt or uncertainty in your mind.

The definition of benefits is crucial to understanding the suitability of a product. As an insurance product, a benefit is payable only upon fulfilling the criteria specified in the policy document, and nothing less. So it is critically important to understand clearly the risks that are covered, rather than just having a vague or presumptuous idea.

Life insurance benefits can either be guaranteed in terms of the amount, or may also include a non-guaranteed component, which is dependent on the



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investment experience of the insurer. When you compare different plans with non-guaranteed benefits, ask for the basis of these projections. The Benefit Illustration will disclose the assumed investment return rates used in the illustrated projection. A higher rate will result in a higher projection, but may be deemed to be unrealistic and too optimistic if that is above what you expect the market to be capable of supporting. Conversely, a lower rate would be deemed to be more conservative, and thus more likely to be achieved.

Cash value in insurance plans is a feature some people like as it provides cash return if the insurance is no longer required in the future. While it can be argued that it may not be the most efficient means of generating future cash, it does serve to ensure that insurance cover will be maintained even when premium payments are interrupted for a period of time, and that is of paramount importance. Such cash value, comprising both guaranteed and non-guaranteed components, is a common feature in whole life plans. Guaranteed cash value may also be featured in some limited term plans. Investment-linked life insurance, however, does not guarantee any cash value apart from the sum assured in event of a claim. The illustrated 5 per cent and 9 per cent projection simply show what the investment value would become if the underlying funds do provide such level of returns. By no means are they indicative of any realistic expectation on the investments.

Limit of cover imposes a maximum to the amount assured for certain benefits in life insurance. These limits may not be apparent in the product summary as it aggregates the total amount insured, consisting of all life insurance plans and from different insurers, that has been effected on a single life. There can be exception to this, however, when an insurer applies the limit only to the accumulated sum insured with itself. Insuring yourself above these levels will be a waste of premium money, unless you harbour the hope for an increase to the limits sometime soon. Today, this capping is commonly imposed on Permanent and Total Disability Benefits and Critical Illness Benefits.

A number of hospitalisation insurance plans introduced in recent years provide benefits without limits for most medical expenses. This is in contrast to what has traditionally been available where limits are applied to all hospital expenses. Nevertheless, some limits may still apply that can restrict the amount claimable, e.g. deductible, co-insurance, annual limit and lifetime limit.

Another hospitalisation benefit worthy of notice is waiver of admission deposit. This allows you to be admitted without the need for a deposit on admission, or a top-up when the hospital stay is prolonged. This can be provided through a medical card or a letter of guarantee issued by the insurer, and is commonly a feature of group hospital plans for larger organizations. This feature is also available with one of the CPF funded shield plans.

A cash benefit is different from a reimbursement benefit. Cash benefits are paid when the prescribed criteria are met, regardless of payout from other plans or whether expenses have been incurred, This is typical of life insurance. Reimbursement benefits, on the other hand, would take into account payout from other plans and approved outlay. The basis is that you will be compensated for only what you have expended, and that you not make any gain. This is generally applicable for hospital and property insurance, though here again there are some hospital plans that pay cash benefits.

A benefit payout schedule prescribes how the insured amount will be disbursed to the claimant. Benefits can be paid lump sum upon approval of a claim, or paid over several installments of varying durations. Some may also require periodic assessment to qualify for continuing payout. This awareness will aid you in avoiding any potential cash flow issues.

Tenure of cover specifies the period of time within which the insured risks are covered for life insurance. If the time horizon for the required cover can be pre-

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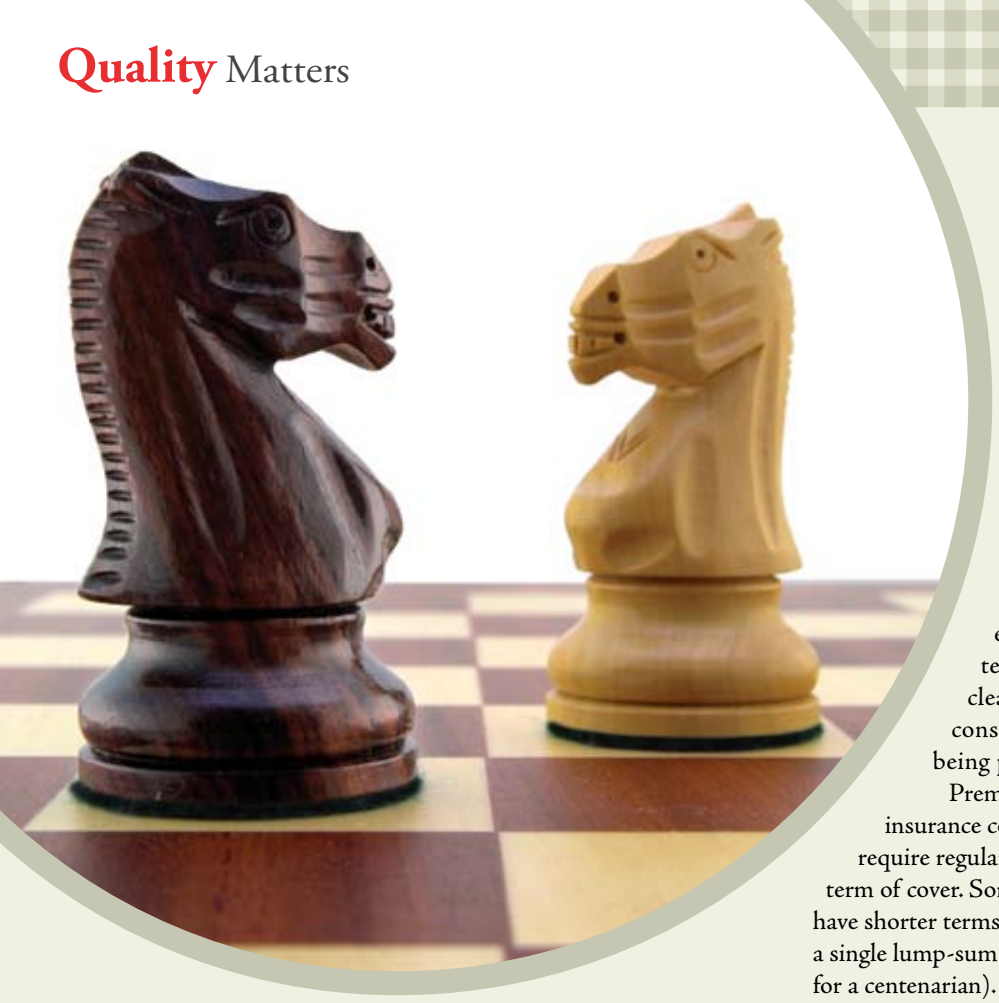

determined, a limited term plan would be appropriate. However, when that cannot be pre-determined, or when it is not prudent to impose a time limit, a whole life cover is more advisable. This is generally applicable for retirement needs, as a person's life span is not only an unknown factor, but will also potentially increase. Non-life insurance is, on the other hand, always issued on a yearly basis.

Hospital insurance is provided on an annually renewable basis. As such, it is advisable to select one which guarantees renewal so that your cover cannot be declined by the insurer no matter how adverse your claims history has been. However, you need to be aware of any lifetime cap which will be the ultimate limiting factor.

Since the introduction of investment –linked life insurance in the early 1990s, many have subscribed to its offering of combining both insurance and investment, and a host of flexible features to suit changing needs. However, besides contending with the argument that such packaging is not without demerits, it is also important that you are clear about the insurance costs and other charges that are levied from year to year. As you have to bear the full cost of insurance which increases with age, this is not considered the best means to provide cover in your old age.

Insurers design different plans for specific markets and purposes. An obvious distinction can be made between a life plan and an endowment plan. While they share some similarities such as providing benefits for death, disability or even critical illness, their focus is very different. For the same premium, life plans provide higher cover and lower cash value, if any, while endowment plans provide higher cash value and lower cover. Furthermore, endowment plans run for a limited term, unlike a whole life cover. So be clear about what your current cover consists of and what type of cover is being proposed.

Premium payment is what sustains an insurance cover. Typically, insurance plans require regular premium payment throughout the term of cover. Some life insurance plans, however, do have shorter terms for premium that can range from a single lump-sum premium to age 100 (it is limited for a centenarian). But whatever the term may be, it is important to make sufficient provision for it, particularly during your retirement years.

A further variable that you have to contend with is the rising premium over time. Hospital plans typically project a rising premium schedule for different age bands as more claims are expected to be made as one ages. Furthermore, the cost of medical care is also expected to increase in future, pushing the premium rates even higher. Premium for critical illness benefits are currently also not guaranteed, with the exception of one insurer, as insurers also foresee an increasing rate of claims of this nature. A shorter premium term, where available, will mitigate this risk of future affordability.

INVESTMENT PRODUCTS

Key consideration for selecting investment products would be to match the risk associated with the instrument to your appetite and capacity to take risk. Investment risk is a measure of the volatility, or uncertainty, of returns. Risk profiling often focuses on your appetite for risk. Your risk appetite, however, is not a stable measure as it can be influenced by a host of factors and thus tends to fluctuate in tandem with prevailing market environment. Determining your capacity for risk, on the other hand, provides a more stable basis as it takes account of your present life stage and your entire portfolio of investment assets.

New investment offerings are coming on stream at an unbelievable rate to cater for investors. Besides the

traditional stocks and equity mutual funds, they now come with specific themes or packaged with an array of instruments. Even hedge funds, once the domain of high network clients serviced by private bankers, are increasingly being rehashed for the retail market.

To evaluate the suitability of an instrument proposed by your adviser for your purpose, the following questions will help with your assessment:

- What is the investment strategy?
- Who are the fund managers and what are their expertise and track record?
- What are the underlying assets?
- How are the underlying assets diversified?
- What are the downside risks that will adversely impact performance?
- What are the upside factors that will positively boost performance?
- In what ways will this support your overall investment strategy?
- If you require regular payout, what is the basis and frequency for the payout?
- What fees are chargeable and how much?
- How easily can this investment be liquidated for cash?
- Any penalty charged for liquidation?

You need to be satisfied that the answers to the above questions, taken collectively, are consistent with your overall investment strategy.

Your Adviser

Your adviser is a vital factor to your financial future. He must be trusted to be focused on your interest, and not his. This is measured not only in terms of his integrity, honesty, reliability, and a host of other positive personal traits, but also in terms of his distribution capabilities and his professional competence. Ultimately, it is not only the best solution your adviser can offer, but also the best solution the market can offer.

No matter how your adviser is remunerated, the range of products he can offer and effectively advise on is limited by the distribution rights extended by product providers. An agent or bank officer can offer only what his company manufactures, plus whatever third party products, if any, it has been authorised to carry. Any of such third party rights are usually limited in number. An independent adviser, on the other hand, has access to a far greater number of products and providers, be they insurance companies or fund managers. Through them, you have a wider reach to solutions to provide the best match for your requirements.

Over and above the product range that can be offered, your adviser has also to demonstrate in-depth knowledge of the proposed products. Your understanding of the strengths and limitations of a product is vital for your confidence in your plan and your commitment to staying on course.

It is not uncommon for consumers to agree on purchasing a product because of a personal relationship. But ultimately, if ever you need to choose between a friendly adviser and a trusted adviser, ask yourself if he is the one to whom you can entrust your financial future for you and your loved ones. Thankfully, there are advisers around who are both friendly and trust-worthy, if you are conscientious in seeking them out.

> Your understanding of the **STRENGTHS AND LIMITATIONS** of a product is vital for your **CONFIDENCE IN YOUR PLAN** and your commitment to staying on course.

Conclusion

In the final analysis, you and your loved ones owe it to yourselves to select the plan that will put you on the journey to fulfilling your financial goals. Hopefully the pointers covered so far will be helpful for you to make the right decisions. Do not leave any doubt unanswered, but do keep asking questions till your concerns are satisfactorily addressed. Q

*By **John Kong**, Associate Director, Promiseland Independent Pte and **David Choo**, Director, Promiseland Independent Pte Ltd. Both authors can be contacted at **johnkong@promiseland.com.sg** and **davidchoo@promiseland.com.sg** respectively.*