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Planning to Buy an Endowment Plan? It May Pay to Wait a Few more Days

You may be able to buy a policy at a lower cost with higher life cover as well as surrender value after the insurance regulator announces the final guidelines for traditional endowment plans, says **Preeti Kulkarni**

You should wait for a few more days if you are planning to buy a traditional endowment plan this tax-saving season. The Insurance Regulatory and Development Authority (Irda) on Monday has hinted that the final guidelines for traditional plans will be released after the Insurance Advisory Committee's meeting this Friday. Last year, the draft guidelines on traditional plans had made a case for lower charges and higher life cover as well as the surrender value, among other proposals. As things stand today, life insurers may have to refile a large chunk of their endowment portfolio by June 30.

TO BUY OR NOT TO BUY

Insurance companies and their sales forces are heavily promoting these products now. In fact, traditional insurance products regained their top spot after the insurance regulator clamped down on unit-linked insurance plans, or Ulips, two years ago. After the new guidelines on Ulips, insurance agents also switched loyalties to traditional products due to the higher commissions attached to them.

Moreover, investors, too, are keen on endowment plans for their assured return promise, as very few have regained confidence in the stock market. If you are going to take the endowment plan to save on taxes, you should wait for a week for clarity.

"It may make sense to find out if the new norms would be more investor-friendly, and then invest. In their current form, it is not such a great proposition," says Suresh Sadagopan, certified financial planner at Ladder7 Financial Advisories. The new products are likely to have lower charges and possibly higher cover and surrender value.

The draft guidelines give some indications on this front. For example, commissions could be capped to three times the premium payment term. That is, if you have chosen a premium paying term of 10 years, the commission charged will not be more than 30%. Also, Irda has recommended offering a minimum surrender value calculated on the basis of the year of surrender.

"Policyholders will see a benefit in terms of increased minimum surrender value. At the moment, the guaranteed surrender value (GSV) is around 30% of the premiums paid minus first year premium, irrespective of the number of policy years gone by. Those staying with the policy for a longer term will see direct guaranteed benefit from the new guidelines, assuming they are finalised in their current form.

However in the current scenario, the special surrender value (for participating products) was anyway much higher than GSV and close to what is being proposed as GSV," says Gopesh Modi, head, products, Edelweiss Tokio Life Insurance.

The minimum life cover, too, is expected to be enhanced to 10 times the annual premium for those under 45. "As such, Irda norms are expected to be beneficial to the policy holders and may result in reduction of charges, among other things. However, the nature of the product and other broad features are likely to remain similar and any improvements may only be marginal," says Arvind Laddha, CEO, Vantage Insurance Brokers.

STUDY THE NEW FEATURES CLOSELY

While certain benefits are clear, insurance-seekers need to be aware of the flipside, too. "Policyholders – especially those who are over 50 – need to bear a key point in mind with respect to death benefit. It is likely to go up in the newer traditional plans. So, you may see insurers introducing caps on maximum age at entry or exit. Therefore, people in the age group of 50 and above may consider buying the current plans, as they may find it difficult to buy one later," says Modi. Even the recommendations on surrender value may not have a significant impact, feel some.

"I think the changes are substantial from the insurers' point of view. However, I don't think it will make a material difference in terms of benefits for the policyholders. If they are planning to surrender the policy mid term, they could fetch a better surrender value. But such policies should never be

Should you Wait for the New Guidelines?

1. **With Irda hinting** at the announcement of final guidelines soon, new versions of traditional policies will hit the market in a few months time

2. **For insurance-seekers** looking to buy endowment policies to save on taxes before March 31, this creates a dilemma - whether to choose from the current lot or wait for the newer ones

3. **The new regime** could bring in a lower charge structure, along with higher cover and surrender value

4. **On the other** hand, mortality charges are likely to go up, resulting in lower proportion of premium being directed to investments

5. **Investors should** take into account other features, too. Compared to other tax-saving avenues like ELSS and PPF, endowment plans' charges are higher and they require long-term commitment

6. If you are convinced of endowment plans' proposition - capital protection and secure returns along with insurance cover - you can wait for a few more days for the new guidelines

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bought with a short-term horizon in mind," says Chandan Khasnobis, appointed actuary, IndiaFirst Life Insurance.

Also, remember, higher sum assured means higher mortality charges. "People buy endowment policies with the savings objective in mind. Such policyholders may find the new version unattractive as the mortality charges will eat into the premium amount directed towards investment," adds Modi.

INSURANCE AS A TAX-SAVING TOOL?

However, this doesn't mean that you should forget the fact that insurance is a smart way to save taxes. Sure, traditional plans, as mentioned earlier, offer capital protection along with secure returns. If you have chosen a participating - or with profits - endowment plan, you could also earn annual bonuses. However, the list of negatives is also equally long.

"The charges in an endowment policy could be higher than in most other tax-savings options and one needs to understand them well. Another aspect to keep in mind is that the savings through endowment premiums should not be more than 50% of the overall savings potential, as this is a fixed commitment and any break in the premium payment could result in the insured losing a significant portion of the contribution already made," explains Laddha of Vantage Insurance Brokers. Endowment plans invest primarily in debt-oriented instruments, offering returns in the region of 5-7%.

"Low returns, low insurance cover and commitment to pay premiums for a long time count among its drawbacks. It also sucks out cash flows which could have been deployed for better yields," points out Sadagopan.

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