The ins and outs of endowment policy benefits

Endowment policies have been dispensed by some of our readers. Here are some things you should know about them.

By Genevieve Cus
genevi@php.com

All insurance endowment plans are likely to be one of the first things that come to mind when one studies to embark on a medium-term investment strategy. Endowments are clearly seen as an efficient form of savings. How many of us have put money into our endowment plans and you don’t know the risk of any lapse payment? You need not have to look too far about what sort of risks and potential returns you may have little volatility.

Yet for some policyholders, endowment plans have disappointed in terms of their maturity values, causing a stir in the industry. What can you do to manage risks and what should you watch out for?

Endowment policies carry lower underwriting costs and offer savings plan products. It’s a staple in Singapore’s insurance market. They are typically marketed to parents with young children as a form of savings for future education costs.

There are two broad types of endowments: “participating” and “non-participating”. The former is a “with-profits” type of insurance plan where premiums are pooled together by the insurer and collectively invested to achieve a rate of return. The latter offers a guaranteed rate of return, which is paid back to you from your policy fund. Non-participating rates are typically lower than those of par endowments.

Non-participating returns are typically lower than those of par endowments. The bulk is invested in a very diversified manner. The bulk is invested in bonds whose maturity profile matches that required by the policy. Some policyholders have been disappointed by their maturity values. Here are some things you should watch out for.

Some policyholders have been disappointed by their maturity values. Here are some things you should watch out for.

**Understanding bonuses**

With endowment plans, there are two components to the policy return: guaranteed and non-guaranteed. The non-guaranteed portion of returns is expressed in terms of bonuses. Sometimes a plan can also include cash dividends, although a bonus structure is more common. A policy can have an annual or a “terminal” bonus. As the name implies, an annual bonus reflects cash paid out in a given year of the policy. On the other hand, a terminal or one-off bonus is a payout of the accumulated annual bonus to date.

Some plans may also offer a one-off “bonus performance” which paid when the policy matures or is surrendered. This is typically very low compared to the bonus from the policy.

Once a bonus is paid, the amount becomes part of the guaranteed value. You will find details on the annual bonuses of the types of bonuses in the product summary that should accompany the policy document.

In par polices, returns are “smoothed”. This means that if you invest in an endowment plan, you benefit from an annual bonus and retain more surplus. In a poor year, the value of the annuity contract or the insurer may be lower, but the policyholder is not penalised. The policy is designed so that the payout of the policy is greater than the total premiums paid.

**Projected investment rate of return**

All with-profit plans have a projected investment rate of return (PIR) of 3.75% to 5.25% per annum. The projected investment return rate (PIR) is a long-term rate of return used to calculate the maturity value of a policy. It is typically expressed as a percentage. The PIR does not guarantee any rate of return, it is merely used to determine the expected rate of return on the policy. It is used to calculate the bonus rate that the policyholder will receive.

The PIR is calculated as the sum of the following:

1. The guaranteed rate of return on the policy
2. The non-guaranteed rate of return on the policy
3. The dividend rate on the policy
4. The policyholder’s rate of return

**Deductions**

In Singapore, endowment plans are subject to income tax. Taxation is calculated on the net profit that is generated from the policy. The net profit is calculated by deducting the policyholder’s premiums paid from the policy’s maturity value.

In Singapore, the tax rate is 16%, which means that 16% of the net profit will be taxed. This means that the policyholder will receive 84% of the net profit as a dividend, which can be reinvested in the policy or withdrawn from the policy.

**Understanding the benefit illustration**

When you purchase an endowment policy, you receive a benefit illustration that shows the guaranteed and non-guaranteed portions of the policy. The benefit illustration provides an estimate of the future value of the policy at maturity. The benefit illustration is a useful tool for assessing the performance of the policy over time.

The benefit illustration typically includes the following information:

1. The guaranteed portion of the policy
2. The non-guaranteed portion of the policy
3. The dividend rate on the policy
4. The policyholder’s rate of return

The benefit illustration is a useful tool for assessing the performance of the policy over time. It provides an estimate of the future value of the policy at maturity. The benefit illustration is a useful tool for assessing the performance of the policy over time.