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How to Use Life Insurance to Pay for Retirement

Rebecca Lake | FEB 11, 2019

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Most people think of life insurance in terms of the financial benefits it provides to relatives when you die. But many don't realize that you can often use it to your advantage even sooner. Certain types of life insurance policies can be used to generate additional streams of income for the person who takes them out. This can come in handy in retirement. Here's a look at how permanent insurance products can act as supplemental income.

Compare life insurance quotes now.

Building Cash Value With Whole Life

A term life insurance policy stays in effect for a specific number of years, usually anywhere from five to 30 years. On the other hand, a whole life policy (a type of permanent life insurance) only expires when you cancel it. Otherwise, whole life insurance covers you for a lifetime.

Whole life insurance tends to be more expensive than term life due to higher premiums. But the trade-off is that you're accumulating cash value in the whole life policy. You can then borrow against or withdraw from that cash value later on. Depending the policy, you may also earn interest or dividends on a tax-deferred basis. Generally, you can borrow against the policy up to the amount of cash value you've accrued without taking a tax hit. If you're receiving dividends, you won't owe any taxes on them unless they exceed the total amount of premiums you've paid.

It's always important to be careful about how much you borrow. That way in this case, you can use a whole life policy as a steady source of income in retirement. Technically you don't have to repay loans against cash value. However, you should keep in mind that any outstanding loan balance reduces any death benefit payable to your beneficiaries when you die.

Investing With Universal Life

Universal life insurance is another type of permanent coverage. However, it works a little differently than a whole life policy. You still earn cash value based on the amount of interest earned as you pay your premiums. One difference is that your premium amount can be adjusted based on your situation. You also have the ability to raise or lower your death benefit as needed. Plus, you can use the accrued interest to cover your premiums.

Universal life insurance can be attractive to retirees. In addition to building cash value, there's also an investment component involved. Part of what you pay in premiums goes towards the policy cost. Then the rest is invested in a vehicle of your choice. Those investments' performances determine your individual returns. You can borrow against the cash value tax-free up to the point that withdrawals exceed what you've paid.

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The only downside to universal life is that returns aren't always guaranteed. You may want to review the prospectus carefully before choosing this type of coverage.

Converting Permanent Insurance to an Annuity

So you've successfully built up a substantial amount of cash value in a whole life or universal life policy. From there you can convert that to an annuity, creating a regular source of income.

An annuity is a type of contract that you purchase from a life insurance company. Typically, you fund an annuity with a lump sum. The insurer then pays you a fixed amount for the duration of its lifetime. A lifetime annuity allows you to receive payments until you die. They may even continue providing benefits, albeit reduced, to your spouse.

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policy. But having other assets to leave for your heirs can negate this factor. In that case, making the switch can provide some much-needed cash flow for your golden years. When you're shopping around for an annuity, you may want to compare the payouts from different companies. That way you can make sure you land with the biggest benefits.

Bottom Line

Developing a solid retirement strategy begins with knowing what your different savings and investment options are. If you haven't thought about how life insurance fits into the picture, you may be overlooking a potentially valuable source of income.

A financial advisor can help you explore all of your options and determine which retirement strategy is right for you. A matching tool like SmartAsset's SmartAdvisor can make it easier to find a person to work with to meet your needs. First you'll answer a series of questions about your situation and goals. Then the program will narrow down your options from thousands of advisors to three fiduciaries who suit your needs. You can then read their profiles to learn more about them, interview them on the phone or in person and choose

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Rebecca Lake is a retirement, investing and estate planning expert who has been writing about personal finance for a decade. Her expertise in the finance niche also extends to home buying, credit cards, banking and small business. She's worked directly with several major financial and insurance brands, including Citibank, Discover and AIG and her writing has appeared online at U.S. News and World Report, CreditCards.com and Investopedia. Rebecca is a graduate of the University of South Carolina and she also attended Charleston Southern University as a graduate student. Originally from central Virginia, she now lives on the North Carolina coast along with her two children.

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Retirement Income Calculator

Annual Income

$ 54,037

Current Savings

$ 25,000

Monthly Savings

$ 270

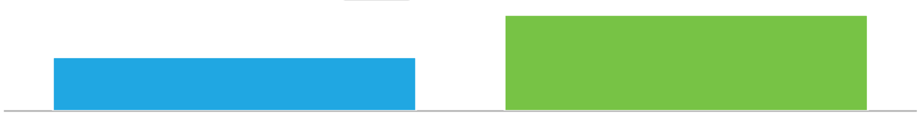
6% of income

Birth Year

1984

We recommend saving **$574,747** at retirement. This will cover **$72,366** per year in retirement income. *Follow this link to see your 3 financial advisor matches*

Retirement Age 66



Savings at Retirement
$331,636

Recommended Savings
$574,747

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