

## SBP vs. Commercial Life

The SBP is a sound program that benefits military retirees and their families, and more military retirees should be enrolling in it! The computer files do not and cannot show why retirees decline SSBP but I am aware of the negative comments about SBP frequently made by agents and brokers representing life insurance companies.

Unlike insurance agents or those touting investments, I have no financial stake in your decision. I hope that you will read this letter and thereby give me the chance to steer you away from an unfortunate stop. It is particularly upsetting to me to know that many of you will make the wrong SBP decision because you lack information about your own retirement. Here are some of the reasons that I have heard for declining SBP and my comments on them.

**#1. I can get \$100,000 of term insurance in the first year following retirement for only \$240. SBP will cost me \$1,300 in the first year.**

Comment: What happens in the first year doesn't really mean much. The SBP decision is a life-time decision. The indexing of retired pay gives SBP a lot of value "down the road." According to my calculations, an annuity to a 42-year old male is worth 50% more if it is indexed than if it is a level, unchanging annuity.

**#2. My buddy Jack was in my unit in Vietnam. He's an insurance agent now, and he wouldn't steer me wrong.**

Comment: None needed.

**#3. SBP doesn't have cash value and my insurance policy does.**

Comment: You pay plenty for that cash value.

**#4. Under SBP, I could pay premiums for many years and then have nothing to show for it if my spouse dies before I do.**

Comment: That's all figured in our calculations, and SBP is still a good deal for most retirees. Many people pay for term insurance and never collect. You are buying protection for your spouse against the contingency of your death. If you remarry, that spouse is covered.

**#5. I'm invincible. Nobody as tough as me will ever die.**

Comment: None needed.

**#6. I am separated and about to get a divorce. Why would I want to do anything for my spouse?**

Comment: If protecting your spouse is not a consideration for you, then the whole premise of this letter, which is maximize retired pay for the two of you, is negated. There's no point in your reading any further. However, you will have to get your spouse's signature concurring with no (or reduced) coverage.

**#7. I am female, and I figure that my better mortality prospects compared to my husband's make SBP a poor buy for us.**

Comment: This argument does have some merit. Please see my comments below.

**#8. I am a brilliant stock market investor. I can take 6.5% premiums and turn that money into a fortune.**

Comment: Please help ME make some money. Actually, the disk (referred to below) allows the individual to vary the discount rate for future SBP premiums and benefits to reflect superior investment prospects. By exercising options within the disk, you can see the results with any interest rate you want.

I should point out that few insurance agents are crooks and deceivers. A lot of them are properly committed to the product they sell, but many are not knowledgeable in the true value of SBP.

**#9. I am retiring soon. How should I go about making the SBP decision?**

Comment: I would start by advising you to ignore insurance and consider your spouse and yourself as a single unit. What can you do to get the most for the two of you? Please excuse me for saying that the most valuable tool in this regard is the computer software disk your Retirement Services Officer has available for you. It was written to help you choose the most valuable option in your particular case.

The first page of output of the SBP valuation program is designed to help you choose the most valuable option. There is no mention of insurance on this page, and the reason that insurance can be ignored at first is that no commercial insurance company can give you benefits that have a greater value than the premiums you pay. If they did, they would be out of business in a short time. This reasoning applies to term, whole, and non-smoker insurance with small or large companies. After the optimal SBP is selected, the retiree should analyze the financial position of his/her spouse upon the retiree's death, as well as the amount of insurance that is affordable. The retiree can then purchase insurance to supplement SBP if it is needed.

As I say in a letter that is part of the disk, most male retirees should take the maximum basic SBP. There can be exceptions such as when the wife is substantially older than the husband or when she has health problems that are expected to shorten her life. By "maximum basic SBP" I mean all the SBP you can get without taking any of the Supplemental SBP (SSBP).

The same advice is not applicable to female retirees. Maximum basic SBP is not a good idea unless there are special circumstances. Women generally live longer than men, and the disk takes the mortality differences into account.

I have compiled some examples using the disk that may be of interest:

Example 1: Retiree is a 41-year old male E6 with 22 years of service. The spouse is 40. Take the maximum SBP.

Comments: This is a good example because it represents a lot of young couples at the point of retirement. Actually, SBP is more valuable for older couples, but these youngsters still increase the present value of their military retirement by \$6,500 by taking the maximum over taking none. The prospective SBP annuity to the spouse is worth 40% more than the 6.5% of retired pay that is given up.

Example 2: Retiree = 49-year old male O6; 26 years service; spouse, 45. Take maximum SBP.

Comments: Unless there is some unusual health situation, this example is extreme. The spouse is very young, and the retiree is not a kid. Taking no SBP would be the equivalent of flushing \$50,000 down the toilet.

Example 3: Retiree = 41-year old female E6; 22 years service; spouse, 40. Recommend forgoing maximum SBP and instead taking SBP on a small portion of retired pay (that which costs 2.5%--the "threshold").

Comments: The disk output shows that SBP for the threshold amount will maximize the total benefit for this couple.

Example 4: Retiree = 42-year old female E7; 23 years service; spouse, 55. Take no SBP.

Comments: This is an unusual example where taking SBP reduces the value of retirement no matter what amount of SBP is taken. Even the threshold amount doesn't seem to be worth the cost. The age differential and the male/female mortality disparity are the chief factors.

Example 5: Retiree = 41-year old male; 22 years of service; spouse, 46. Take maximum SBP.

Comments: The fact that wife is older makes this a close call, but does not necessarily disqualify SBP. I would take the maximum because I would be protecting my wife at least as well as I could by buying insurance, but without having to do any shopping around for insurance. I eliminate any worries about the insurance company having financial difficulties. If my wife should die and I remarry, having taken SBP initially could prove advantageous.

### **FREQUENTLY ASKED QUESTIONS**

**Q:** What about the Supplemental SBP (SSBP)? Do the actuaries have any advice?

**A:** I wish I could say we do, but we don't. Unlike the basic SBP, the retiree and spouse are not benefiting from any government subsidy with SSBP. There is a SSBP disk to help with this decision. Of course, the decision only comes up when maximum SBP is selected. For a retiree whose health is poor or whose spouse is much younger, SSBP can be a good buy.

**Q:** What about Veterans' Group Life Insurance (VGLI)? Is that superior to SBP?

**A:** You should treat VGLI just like any other type of life insurance. First, decide about SBP. Second, buy supplemental life insurance as needed, paying the fewest cents per thousand as you can from a reliable company. I would look at prospective costs as you age as well as the cost during your first year of retirement. Needless to say, VGLI is run by a reliable insurer.

**Q:** How does SBP operate as far as my taxes are concerned?

**A:** Every penny that you ever receive from the Military Retirement System is taxable income. When you choose SBP, you are electing to receive reduced retired pay (6.5% for spouse coverage) to provide your spouse a benefit payable if you die first. In many, but not all cases, a higher marginal and overall tax rate will apply while both are living, and a lower one after the retiree's death, because income drops. In those cases, the benefit of taking SBP will be enhanced. This tax benefit is worked into the valuation program.

The previous part of this letter is addressed to the potential retirees who apply the SBP disk to their own situation. I would be foolish to think that all of you who retire this year will use the disk. Facing that harsh reality, I wish to say a few words to those who cannot or will not.

Male retirees can't go far wrong taking the maximum SBP. The situations for them where the threshold amount of SBP is not worth it are rare.

- The older you are, the more you want SBP.
- The younger your spouse is, the more you want SBP.
- The worse impairments you have to your health, the more you want SBP.

I cannot, in good conscience, advise all female retirees that it is always a good financial decision to take the maximum SBP. If you are approximately the same age as your husband, SBP is relatively better than if you are 6 or 8 years younger. I think female retirees would be very foolish, however, not to take the time and effort to find out what the disk output advises in their particular case.

One word of caution about the advice above: it is based on expected values and large amounts of statistics. In Example 4 above, the young female retiree could get hit by a truck a month after her retirement, and her husband could live to age 90. Every outcome is different and unknown at the time the decision must be made. The actuaries have compiled massive amounts of experience and reflected that experience in the valuation program that I want you to use.

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