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HEG79-101 Insurance – What Kind Do You Need?

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Insurance -- What Kind Do You Need?

This NebGuide examines various types of risks and the need for insurance.

Kathy Prochaska-Cue Extension Family Economics and Management Specialist

Have you spent time recently with an insurance agent who was trying to explain an old policy or to sell you a new one? Perhaps you felt you didn't know which questions to ask about what you were signing, or how the policy would pay in an emergency.

Most people would like to better understand insurance terms and the reasons for buying insurance. Before you visit with an agent, you will want to answer some basic questions about an insurance purchase that is adequate for your situation.

Major Risks

What risks and hazards threaten the average individual or household? Here is a list of the more important ones:

- Death of a household member -- husband, wife, child, and especially a wage earner.
- Total or partial disability of a household member -- wage earner, husband or wife, child.
- Loss of job by a wage earner.
- Illness or accidents in family.
- Fire or windstorm damage to home.
- Liability for damages done by your car.
- Liability for damages suffered by someone on your property.

This list could go on and on, but the point is that each risk or loss has a special meaning to each individual and household. There are risks no one can avoid.

Why Insurance?

Insurance is one means of providing financial protection against the risk of unexpected losses. It does not remove the risk of death, injury, or fire; it compensates you, at least in part, for actual losses incurred. You trade a series of annual payments for the assurance that you won't have to take a major loss at some unknown time.

Insurance -- whatever kind it may be -- operates on the principle of spreading or sharing the risk. One person alone would find it difficult if not impossible to provide this protection because the possibility of a loss cannot be predicted as well for one person as for a group. Large groups of people can pool or transfer their risks to an insurance company. The individual pays the company a specified amount called the premium. The size of the premium is based on the frequency of losses by the group in past years, and the costs of company administration and selling divided by the number of people in the group.

What Risks Should Be Insured?

Losses are many and varied. Some are in the nature of disasters, such as the loss of your home by fire. Others are minor; for instance, a traffic accident in which the fenders of your car are smashed. Some are remote, one-in-a-million possibilities; others are fairly likely to happen to you at least once in a lifetime.

The risks you face are not exactly the same as those other people face. Risks grow out of your particular situation: your job, the size of your household, savings, and income. Neither will your risks remain the same year after year. Your circumstances will keep changing.

Four Steps in Insurance Decision-Making

1. Determine what risks you face.
2. Determine what causes these risks.
3. Determine how you should handle each risk. There are *three ways* to handle risk:
 - o Take care to *prevent* the feared occurrence from happening to you.
 - o *Keep* the risk; set aside savings to help cover it if it occurs.
 - o *Transfer* the risk through the use of insurance.
4. Make a plan. Shop around for needed protection and a good agent.

What Risks Should Be Kept and What Risks Should be Transferred?

		Probability of Occurrence	
		Low	High
\$ Cost of Occurrence	High	3. Transfer risk.	4. Insurance not available or too costly.
	Low	1. Keep risk.	2. Probably keep risk.

A guideline for deciding on the need for insurance is shown in the chart above.

In *block #1*, the probability of the event occurring is low, and the cost of each occurrence is low. Keep the risk; don't buy insurance.

In *block #2*, the probability of the event happening is high, but the cost is low. Consider keeping the risk; set aside money for this loss in your emergency fund. Don't buy insurance.

In *block #3*, the probability of the event is low, but the cost is high. Transfer the risk; buy insurance.

In *block #4*, the probability of the event is high, and the cost of each occurrence is also high. No one will sell you insurance or the cost of such insurance would be prohibitive, so you are forced to keep the risk.

Some Clues To Solving The Puzzle

There is no easy way to find the answers, but there are ways to assure yourself of a sensible program for you and your situation. A formula for working out a sound insurance program is simple to state, but not so simple to carry out.

1. Get all your policies together. Look them over.
2. Carefully assess your resources: your economic resources--savings, social security, property, etc. - and human resources, such as state of health of household members, special skills and abilities, and earning capacity.

Consider which kinds of losses would be most serious for you and which you can best afford to pay out of your pocket. Ask yourself these questions:

... What are the chances of any particular loss occurring to me or to someone in my household?

... Which would be more serious -- damage to my car or liability for injury or death of someone else in that accident?

... Or, as a young person with several small children, which is the most pressing concern -- insurance to provide income in case of an early death of the wage earner or to build up savings for college?

... How can insurance be used for protection from these possible losses, and what will it cost?

At this point you are ready to learn as much as you can about the kinds of insurance protection that are available.

A study of insurance will lead you to an important step: *finding a good agent*. Take time for this. A "good" agent is someone you can talk to and whose judgments you can trust.

When you talk to an agent, make sure that you understand the insurance language he or she uses. You will learn some of the basic insurance terms in other [NebGuides](#) available in this series.

In the final step -- working out a total plan -- the services of your agent can be invaluable to you. Your agent shouldn't decide which policies and how much you should buy, but can help you make decisions more wisely.

Pointers for Policyholders

- Know what you have in insurance. Be adequately covered, but avoid double coverage.
- Try to buy insurance through group policies whenever possible. This coverage will cost less than an individual policy.
- Increase deductibles.
- Check for special rates.
- Pay premiums annually instead of monthly or quarterly. When you pay more than once a year, it usually costs you more because it costs the company more to keep your records. Avoid the added service charge you pay when you pay premiums more than once a year.
- Review policies at least annually to be sure you have the insurance you need.

For more information and answers to specific questions about your insurance policies, contact your

agent or the representative for your group insurance plan.

Need Help With Your Insurance?

If you have problems with, or questions about, an insurance company licensed to do business in Nebraska, you can get help by writing to the State Insurance Commissioner. Be sure to include your name and address, the name of the company and the agent, the policy type and number, and the details of your problem. Address your letter to:

Commissioner of Insurance
Terminal Building
941 "O" Street, Suite 400
Lincoln, NE 68508-3690
Telephone: 402-471-2201

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