

*Standard 11:* The student will describe and explain how various types of insurance can be used to manage risk.

## Different Types of Insurance



### Lesson Objectives

- ⇒ Examine the different types of insurance available.
- ⇒ Identify key terms associated with insurance and risks: natural disaster, liability, disability, deductibles, and risk management.
- ⇒ Explain the purpose and importance of different types of insurance protection as a risk management strategy (e.g., life, health, property, liability, disability, and automobile).

*The ambulance pulled up while people were looking at the smashed cars. At least no one was badly injured.*

*Jermaine had gotten his car last week. His mom said he needed to get insurance, but he had been so busy with school and work that he forgot.*

*His arm hurt. He could get health insurance at work, but he needed the money to make his car payments. Now his arm was broken, and he had no health insurance. The ambulance could take him to City Hospital, but he would have to pay the bill. How would he work with a broken arm?*

*He did not mean to hit the car in front of him. He was in a hurry and just did not see it was stopped. And, he was talking to Dominique on the phone because he did not have time to call her earlier.*

*Can you find anything that Jermaine could have done differently to reduce his risk and his losses?*

## Personal Financial Literacy Vocabulary

**Claim:** A written request submitted to your insurance carrier to cover a loss.

**Deductible:** The dollar amount or percentage of a loss that is not insured, as specified in an insurance policy.

**Premium:** The fee paid for insurance protection.

### Introduction



Insurance is one of the most important parts of your risk management plan. By purchasing insurance, individuals can transfer their personal risk to a third party—the insurance company. Today, it is possible to insure almost *anything*. Understanding the different kinds of insurance available and evaluating potential losses helps consumers make more informed

### Lesson

Lloyd's of London is one of the most famous insurance groups in the world. It has been known to issue insurance policies on several very interesting and unique items, including Brooke Shields' and Tina Turner's legs, Jimmy Durante's nose, Celine Dion's vocal chords, and America Ferrera's smile.

Most insurance companies are not quite as exotic with their policies. They tend to sell insurance for things such as cars, houses, and boats. People like you pay **premiums** to insurance companies to cover potential losses associated with their belongings. The insurance company takes those premiums and pulls them together in one pool of money. Those funds are available to pay for the losses suffered by members of the pool. By using this process, insurance companies can charge lower premiums and provide more services for their customers.

Insurance premiums are based on the potential risk and potential losses they will have to pay to the group members. While insurance premiums sometimes seem rather high, the rates vary from person to person—depending upon personal risk factors such as age, health, personal behaviors, employment, and, yes, credit ratings. In return for paying the premium, you receive an insurance policy from the company explaining your rights and responsibilities when using the insurance. An insurance policy is simply a contract between you and the insurance company outlining what is covered, the

limits of your coverage, and whatever procedures you must follow to maintain the policy and collect any payments for your losses.

While the insurance company will pay the greatest part of your loss, generally you will also pay a small part as well—in addition to your premium. The additional amount you pay when filing a **claim** with the insurance company is called the deductible. The **deductible** is the term used for the amount you, the insured, are willing to pay before your insurance policy picks up the risk. It represents the portion of the risk you are prepared to cover from your personal savings. You will often hear the phrase “after you meet your deductible” to indicate the amount you must pay before the insurance policy takes effect.

When making insurance choices, you should consider the following.

- Is this insurance necessary? If the potential loss is large, it could be financially devastating to you and your family. If the potential loss is small, you may have savings or other financial resources to cover it without insurance.
- How much insurance is needed? Do you want to cover the minimum loss, or do you need to cover the cost to replace whatever you may lose?
- How much will it cost? Do the benefits of purchasing the insurance outweigh the costs?

### *INSURANCE WEB SITE*

Go to the following Web site for more information on insurance for young people: <http://www.insureuonline.org/>.

## Types of Insurance

There are many types of insurance, almost more than you can list. Whether it is health, disability, life, homeowners, renters, or auto insurance, understanding how insurance companies calculate risk and the standard features of insurance policies will help you make the best choices for your personal needs.

### Health Insurance

What happens when you go to the doctor? Perhaps one of your family members has medical insurance that covers your medical expenses. While you may be covered by someone else’s insurance now, you will soon be in a position to make your own choices about health insurance.

Health insurance, also called medical insurance, helps protect you and your family from expensive or unexpected health care-related expenses. It is designed to estimate your overall risk of health-related expenses and supplement your cost for care, including doctor's appointments, hospitalization, prescriptions, and other similar costs. Originally, health insurance was designed to cover "catastrophic" health-related expenses, but has been gradually expanded to include more preventative care.



You make monthly payments called **premiums** to pay for your insurance coverage, and those premiums are based on a variety of factors. Some employers will pay your premiums as part of your benefit package with the company. Having insurance through an employer is generally much less expensive than buying it on your own because employers can pool those who are healthy and spend minimal amounts on health care with those who have numerous health problems and frequently use their health

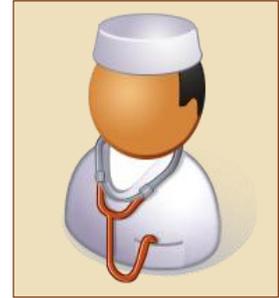
care benefits. If purchased individually, the insurance company will base the premiums on your personal risk factors such as age, overall health, and previous health problems.

Most insurance policies do not cover all health care costs. You are still responsible for certain out-of-pocket costs and the deductible. Other costs can really add up and often include.

- **Copayment:** The amount you will have to pay each time you visit a health care provider. A "copay" is generally \$25 to \$35 and is collected when you sign in for your doctor appointment.
- **Coinsurance:** The percentage of your medical costs you will need to pay after meeting your deductible. Traditionally, your insurance company would pay about 80% of your medical costs, and you would pay the other 20%. However, coinsurance amounts today vary greatly, making it an important feature to check out before making a decision.

Most major medical insurance policies have a limit on coverage. For example, if your policy has a \$1 million maximum lifetime coverage, your insurance company will pay up to that amount for your health care. Once you reach that amount, you will no longer be covered by that specific policy.

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Health insurance costs increase as you age. Buy health insurance while you are healthy instead of waiting until you need it.

Copayments, premiums and out-of-pocket expenses depend upon the type of health insurance you have. A plan called a PPO tends to have more out-of-pocket costs than an HMO—but PPOs offer more flexibility when choosing a doctor and other services. A PPO is a “preferred provider organization,” and an HMO is a “health maintenance organization.” Be sure you are familiar with the options both offer before you agree to the coverage.

The best health insurance plan for you is the one that gives you the greatest flexibility and the most benefits for the lowest cost. There is no standard health insurance plan or a “one-size-fits-all” policy. You will need to compare costs and benefits before choosing a plan.

### Disability Insurance

Disability insurance, also known as disability income insurance, is another type of medical coverage. It pays part of your income if you become ill or injured and need an extended period of time to recover or if you can no longer work.

### Medicare

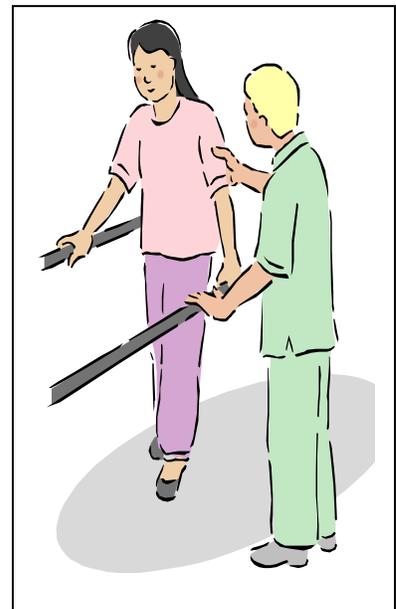
Medicare is a health insurance program provided by the federal government to people over the age of 65 or with certain health conditions.

### Medicaid

Medicaid is another type of federal health insurance, and it pays health care costs for low-income citizens of all ages. It is administered by state and local governments, which also provide matching funds to offset the costs.

### Long-Term Care Insurance

Long-term care insurance helps cover costs associated with care in a nursing home or other similar facilities if you become unable to take care of yourself. Generally, people who need long-term care require assistance with daily activities such as dressing, bathing, walking, etc.



Because many people require long-term care as a result of an accident, age is not a determining factor for purchasing long-term care insurance. In fact, about 40% of those receiving long-term care are between 18 and 64. The late actor Christopher Reeve became paralyzed following an equestrian accident in 1995 at the age of 42

and required nine years of long-term care, costing millions of dollars. Most people do not want to think about being severely injured and postpone the decision to buy long-term care insurance. However, it may be too expensive or too late to get coverage once the insurance is needed.

## Life Insurance

The main purpose of life insurance is to insure against loss of income due to death and can also be used for retirement planning and investing. It is the one kind of insurance you pay for, but only others benefit from it. Except in rare cases, the purpose of life insurance is to provide for others at the time of your death.

Life insurance companies offer a wide array of policies to meet your needs as your personal circumstances change and evolve. Following is a brief description of the three basic kinds of life insurance.

- **Term life** or “temporary” insurance: Provides coverage for a defined time period, generally five, 10, or 20 years; pays cash benefits to a named beneficiary *if* the insured dies during the term of the policy.
- **Whole life** insurance: Covers the insured for their whole life; benefits are paid to the beneficiaries when the policyholder dies.
- **Universal life** insurance: Whole life insurance with more flexibility; allows the policyholder to maintain their policy and still make changes, such as decreasing the death benefit or changing the premiums.



Like health insurance, life insurance is often provided by your employer as part of your benefit package. If you purchase life insurance on your own, the premiums tend to increase as you age. Therefore, it is generally less expensive to purchase life insurance while you are young instead of waiting until you are older.

## Liability Insurance

Liability insurance protects you when others claim to be hurt or injured as a result of something you did or did not do. Generally, it pays medical bills or provides compensation to anyone who can prove you were negligent or acted improperly. Most states, including Oklahoma, require you to have liability insurance on your automobile in case you are involved in an accident. Damage or injuries caused intentionally are not covered by liability insurance policies.

## Homeowner's Insurance

For most people, their home is their largest single investment. Having homeowner's insurance protects your investment against disasters such as fire, tornadoes, busted pipes, robbery, and other similar problems.

Most standard homeowner insurance policies cover your house (the structure itself) and the contents (any personal property you have in the house). In addition, the majority of homeowner insurance policies provide liability coverage in case someone visiting your home is injured.

You have the option to purchase homeowner's insurance that covers either actual cash value or replacement costs. Actual cash value is the amount it would take to repair or replace damage to your home after normal wear and tear, commonly called depreciation. Replacement cost is the amount needed to replace or rebuild your home or repair damages with materials of similar kind and quality, *without deducting for depreciation*.

A good rule of thumb is to insure your home for at least 80% of its replacement value; the other 20% would include the value of your land which probably does not need to be replaced following a disaster.

Few, if any, homeowner's insurance policies cover flood damage. Beware! If you live in an area prone to flooding from any cause—hurricanes, rivers, or streams—be sure to ask about purchasing flood insurance, which is available through the federal government's National Flood Insurance Program (NFIP). In some areas, flood insurance may be required. Consult your insurance or real estate agent for more information.

Take an inventory of all of your personal property, along with a photograph or video of each room.

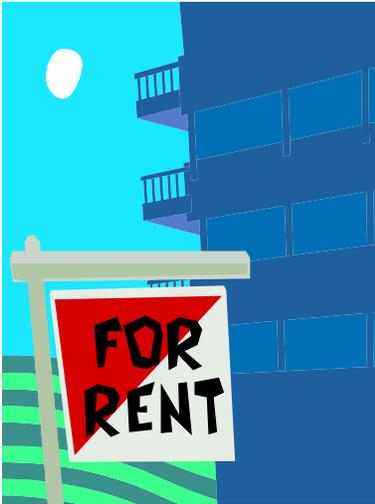
Also, save your receipts for major items and keep them in a safe place away from your house or apartment.

Having this information will make it easier if you ever need to file a claim.

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## Renter's Insurance

As a young person starting out, you are probably more likely to be a renter than a homeowner. To protect your personal property, you should consider renter's insurance which provides some of the same coverage as a homeowner's policy. Renter's insurance protects renters from theft or damage of personal items—furniture, TV, computer, clothing, etc.—in their apartments or their cars.



The landlord should carry insurance to cover the building itself; all you need to insure is your personal property. Except for a very few circumstances, your items will not be covered by your parent's policy or by the landlord's policy.

A good renter's insurance policy will also include liability insurance. You can be held responsible if someone is hurt or injured while visiting your apartment; liability insurance is your best protection.

Generally, renter's insurance can be transferred from one location to another when you decide to move.

Before purchasing renter's insurance, make sure you understand exactly what is covered and what is not covered. If your insurance agent is not willing to explain it to you, perhaps you need to find another agent. Prices on renter's insurance will differ from company to company. It is always advisable to get more than one estimate before making a final decision.

## Automobile Insurance

Buying a car is an important goal for most young people. With the payments, gasoline, and insurance, it can be an expensive purchase. However, failing to purchase automobile insurance can be an even more expensive decision. Everything is fine, until something happens. Before stopping to ask why insurance is necessary, remember this: It is the law!

So, why would almost every state in the country require you to have automobile insurance if you own a car? Automobile insurance limits financial loss due to damage or a car accident. If a tree falls on your car or it is damaged by a hail storm, your

### **CAR CRASH STATISTICS:**

- ❖ There were about 6,420,000 auto accidents in the United States in 2005.
- ❖ The financial cost of these crashes was over \$230 billion.
- ❖ 2.9 million people were injured and 42,636 people were killed.
- ❖ About 115 people die every day in vehicle crashes in the United States—one death every 13 minutes.

comprehensive insurance policy covers your claim and helps offset the cost of repairs.

More importantly, auto liability insurance pays for someone else's property or injuries, if you are at fault, in an accident. It is called "bodily injury and property damage coverage" on your policy. In addition, your insurance will pay if the other person is uninsured. Your policy is required to have uninsured motorist coverage for your injuries.

You can also purchase comprehensive insurance to cover your vehicle if it is damaged by an act of nature or if it is stolen. As an added protection, you can purchase collision insurance to pay for your car repairs if the person at fault in an accident does not have insurance.

As you can see, automobile insurance is an important tool for managing your risk. Trying to cover the costs of repairs and injuries without insurance is extremely expensive.

With the number of auto accidents and the cost of repairs, there is a good probability that you will be involved in an accident and need to use your insurance. Young drivers, aged 15- to 20-years-old, are especially at risk and vulnerable to death and injury on the roadways. Auto accidents are the leading cause of death for teenagers in America. Mile for mile, teenagers are involved in three times as many fatal crashes as all other drivers.

Since young drivers are more likely to be involved in accidents, then it helps explain why insurance for young drivers is more expensive than insurance for drivers in other age groups. While it may not seem fair that young people pay higher premiums, it is an economic choice for the insurance companies. They charge more because it costs them more to cover the costs for young drivers.

Even with the high premiums, having automobile insurance is a good risk management tool that can protect your financial future. Driving without it is high risk. Just ask Jermaine!

*Jermaine should have taken the time to get his auto insurance. He may even be charged a big fine or lose his driver's license for failing to have insurance on his vehicle. Of course, he will need to repair his car as well as the one he hit.*

*While health insurance can be expensive, it is also very risky to go without it. Jermaine will need to make arrangements with City Hospital to pay for his care. The financial burden is further complicated because he may not be able to work, meaning he may not have any income until his arm heals. He also may be at risk of losing his job since he cannot work.*

*While driving and talking on the phone is not illegal, it can be distracting. When sitting behind the wheel of a vehicle, driving that vehicle should always be your first priority.*

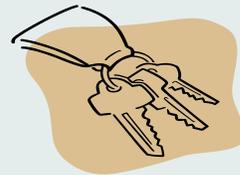
*And if he was in a hurry, he may have been speeding—another high risk behavior. Hopefully, you will make better choices than Jermaine.*

## Conclusion

Insurance is generally considered a valuable risk management tool because it allows a third party—the insurance company—to assume part of your risk and your costs. However, it can become expensive if you buy coverage you really do not need or pay more than you should for the premium. While there are many different kinds of insurance, you are the only person who can decide what is best for you. You probably do not need to insure your legs or your nose like a celebrity, but you will want to have enough insurance to cover any losses to your home, your personal property, or your vehicle. And you will want some form of health insurance in case you become ill and need immediate attention.

### *GIVING OTHERS YOUR KEYS*

If a friend has an accident in your car, it goes on **your** insurance record. Even if they have insurance, it may not matter because you are responsible for who drives your car. The accident will go on your insurance record, and you will pay higher premiums. So, be careful who gets your keys!



Name: \_\_\_\_\_ Class Period: \_\_\_\_\_

## Different Types of Insurance

### Review Lesson 11.2

Answer the following questions and give the completed lesson to your teacher to review.

1. Which kind of insurance should you have if you live in an apartment?
  - a. Liability
  - b. Renters
  - c. Long-Term Care
  - d. Whole Life
  
2. Which kind of insurance protects you if someone is injured on your property or in your apartment?
  - a. Liability
  - b. Renters
  - c. Long-Term Care
  - d. Whole Life
  
3. Which type of life insurance provides coverage for a specified period of time?
  - a. Whole Life
  - b. Universal Life
  - c. Term Life
  - d. Long-Term Care Life
  
4. The amount of money you pay before your insurance provides coverage is called a
  - a. premium.
  - b. copay.
  - c. deductible.
  - d. benefit.
  
5. Payments for insurance are called
  - a. premiums.
  - b. copays.
  - c. deductibles.
  - d. costs.