

The Cost of Insurance Ignorance

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Most insurance agents are paid to sell product, not to help clients manage risk. Knowledge can correct this problem.

Today everyone wants to increase cash flow. All kinds of cost-saving ideas are shared and written about by professionals around the country, but no one is discussing the number one area that can dramatically reduce your cash expenditures. That area is insurance. In my 30 years of financial planning, I have learned one undeniable truth. If people would manage risk rather than "buy insurance," they can save real money in the long run.

First, let us define risk management. Risk management is the process of analyzing the financial impact of an event (such as a death, disability, property loss, etc.) and determining the most cost-effective way to minimize the potential of it causing economic hardship. It does not mean limiting your out of pocket expenses to zero when an event occurs, but merely preventing economic hardship.

Most people buy insurance so that it covers every dollar of medical bills or pays for all repairs of an auto or home loss, with a small deductible. This type of mentality causes too many dollars to go toward nominal risks and too few dollars to go toward the true risk.

Second, economic rewards cause insurance to be sold rather than for advisers to do prudent risk management. For example, there is nominal economic incentive for insurance agents to help people do prudent risk management in the case of life insurance. How many times have you heard an insurance agent tell you that you needed less coverage?

Auto and home insurance rates vary widely from company to company and agents (even independent ones) can only represent a few firms which may or may not be the best deal in your locale.

Lastly, the marketing of insurance policies plays on individual fears and greed to lure customers into worthless gambling-like policies. An example of this would be accidental death insurance, which would shock most purchasers if they actually read the policy description of "an accident" to collect a claim.

Why do people (especially those who are younger) think they are most likely to die accidentally when statistically they are at least 10 times more likely to die due to sickness? Other types of insurance marketing that have little risk management benefit are cancer insurance and hospital income insurance. The costs are usually low and you may actually collect, but consider it gambling and not managing risk. Who wants to win one of these kinds of gambles?

Based on my decades of experience in insurance and risk management, I believe that four out of five people will likely save on the cost of their risk management plan by keeping in mind several key points...