The Basics

Insurance most people can do without

So what kind of insurance may be a bad deal? Here are 10 worth skipping.

By Dan Phelps

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1. Private mortgage insurance

This is something that hits about a quarter of all homebuyers. When you buy a house, the mortgage company wants to make sure it won't be hurt too badly if you skip town without paying off the loan. Unless you can put down at least 20% of the home's value, you may have to get PMI. The policy benefits nobody but the lender and can be so expensive that a year's worth of premiums can add up to a 13th mortgage payment.

Once the outstanding balance on your mortgage drops below 80 percent of the original value of the home, federal law says your lender must notify you that you can cancel the insurance. If your home has appreciated rapidly, you can also apply to cancel it, but you'll probably have to pay for an appraisal ($300 to $400) to prove your point.

2. Service contracts

These "extended warranties" are usually worth skipping. A service contract is simply a promise to perform or pay for certain repairs or services. Service contracts often duplicate what's provided in the standard warranty you get with a car or an appliance. Read your regular warranty carefully. Then compare it to the service contract. Sometimes, you can purchase service contracts later, when the original warranty expires.

3. Separate policies vs. riders

Buying separate policies to cover things like boats or RVs may not be your best choice. While some policies provide added liability coverage and other features, check out if supplemental coverage is already available through your existing homeowners policy.

A major reason is cost. Think of it as buying in bulk. When you add a "rider" to an existing policy, it usually costs less than trying to buy a whole new policy. Also, many of these "things that move" are already covered by your home insurance, albeit at less-than-ideal levels.

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4. Flight insurance

This coverage is pretty cheap. It's a nice way to impress your mate, but a bad bet, thankfully. According to some statisticians, you could fly on a major airline every day for 26,000 years before you'd be involved in a plane crash. Even then, the odds are that you'd survive that crash. Still, it's a big moneymaker for the insurance company. American Express offers cardholders $1 million in coverage for just $14. If every passenger who flew on a scheduled U.S. commercial flight in 1995 paid $14 for a $1 million flight insurance policy, and the insurance company paid $1 million for every person who died in a plane crash that year, the company still would have made $7.4 billion.

Besides, you may already have flight insurance, if you purchased your plane ticket with a credit card. Some credit card companies give you $100,000 in coverage just for charging your ticket on their card.

5. Credit insurance

This insurance is often pushed on consumers. The most important thing to remember about credit insurance is that a lender cannot make you buy it.

While there are several variations (including credit life insurance, credit health or disability insurance and credit unemployment insurance), they all do the same thing: They pay the lender if you can't. So why would you want to pass on credit insurance?

Well, for one reason, you might have enough life insurance, disability insurance or assets to cover your debts. Besides, you might be able to buy a term life insurance policy for less, and the payout would be higher. If a 30-year-old Oregon woman in good health takes out a five-year, $5,000 loan, credit insurance would cost $112.50. The cost of the credit insurance is added to the total loan amount. If this same woman already had a $50,000 term life insurance policy, and tacked on another $5,000 to cover the loan, it would add less than $15 to what she already pays for the life insurance policy over the five-year loan period.

Even if she buys a new term life policy, it would cost her about $500 for five years of at least $50,000 in coverage (that's usually the minimum coverage available). And remember, the credit insurance policy would only pay the lender whatever is owed.

Credit insurance is also a big moneymaker for insurance companies. In Louisiana, for example, insurers and lenders keep 79 cents of every dollar that consumers pay in premiums. Even in the best states (such as Maine and New York), the insurance companies keep about 40 cents of every dollar.

6. Short-term, cash value life insurance

If you don't hold onto them long enough, cash-value life insurance policies are a waste of money. Cash-value life insurance theoretically offers both a death benefit (the money paid to your heirs when you die) and a return on investment. Your equity in the policy -- the cash value -- builds up over the years, and you can borrow against it or simply stop paying on a policy and let the annual dividends keep the policy in force. While your survivors will still get the death benefit, these policies cost you money in big chunks in the first few years.

According to a study by the Consumer Federation of America, it takes five years before one of these policies shows a positive return. And even then, that return is extremely small. Even after 10 years, the average return is only about 2%. All this is due to brokers' commissions and other fees paid in the beginning of the policy's life.

If you're looking for life insurance coverage for a short period, term life is your best bet. The premiums are much lower, and your heirs will still get the death benefit.

7. Life insurance for children

This insurance offers a big death benefit, but kids don't have debts or dependents. If you're thinking that a cash-value kid's life insurance policy would be a good way to save for his or her college education, you could do better elsewhere.

8. Mortgage insurance

It's more expensive than it's worth. Besides, you could do better with another policy -- one that you might already have. These policies are designed to make your mortgage payments if you die or become disabled. If you're worried about burdening your heirs with mortgage payments, you'd be better off buying straight life insurance. Adding onto your existing life insurance policy is less expensive than mortgage life.

9. Cancer insurance

In 1994, about 10 million Americans were covered by a "disease specific" insurance policy for cancer, heart disease or stroke. But if you look closely at what you get, you'll realize there's a better way: health insurance. Some cancer insurance policies promise to refund your premiums every 10 years if you've had no cancer. Not a bad deal -- if you're the insurance company.

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A study done by the federal General Accounting Office in 1994 found that the largest companies selling plans -- that cover only hospital stays or diseases like cancer -- paid out as little as 35% of the premiums they took in. Some states set payout targets of 75% or more for other policies. While $400 a year may not seem like too much to spend for peace of mind, it's the narrow coverage provided by cancer insurance that makes it a bad deal. They'll

cover you if you get cancer, but some policies won't pay for cancer treatments until several years after you've bought the policy. Others require confirmation of the cancer by a pathologist, which sometimes is impractical or even impossible. And skin cancer, probably the most common form of cancer, is often excluded.

10. Short-term medical coverage

There will be arguments a-plenty here. Often, this coverage is offered to those who leave one job for another. Under the federal COBRA law, your old insurance policy can "follow" you for about 18 months after you leave, but you have to pay the whole premium. (Here's where you find out just how much your employer's been kicking in for your insurance coverage.) You don't have to pay the premiums until 100 days after your last day on the payroll. But let's say you're single, run three miles a day, don't smoke and are terrifically healthy. You may decide that the cost of COBRA coverage is too high for the low risk of developing a medical problem before you take your next job. So, don't take the coverage. But, if you have a family, you may conclude that the risk of not having any coverage is too great.

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