



The Basics

3 costly myths about insurance

If you believe these popular misconceptions, you're going to be underinsured, improperly insured and you're going to pay too much.

By [Liz Pulliam Weston](#)

Many people, I'm convinced, think about insurance in the wrong ways.

They operate based on certain myths about insurance, and those myths can cost them -- big time. They either buy too much or not enough. They get blindsided by huge increases in their premiums, or they get dropped by long-time carriers. They get mad about insurance, instead of getting smart.

Here are the myths and the realities you should be thinking about instead:

Myth: Your benefits should roughly equal the premiums you've paid

Many people feel cheated if they aren't "using" their insurance -- in other words, if they pay premiums for years and never make a claim.

That, however, is exactly what you want to happen with most types of insurance.

Sound insane? It's really not. Most of the time, insurance should be thought of as your protection against true financial catastrophe, not as a buffer against the normal ups and downs of daily living.

You want your homeowners insurance to be there if your house ever burns down, for example, since you probably don't have enough savings to rebuild your home or pay off your mortgage otherwise. On the other hand, you can easily swing the cost of replacing a pane when Sally down the street knocks a line drive through your window.

So why pay extra for a policy with a low deductible, just so you can get your insurance company to cover a cost you could readily handle on your own? Opting for deductibles of \$500 to \$1,000, instead of \$100 to \$250, can save you as much as 35% on your premiums.

You'll also find that higher deductibles reduce the temptation to make lots of claims, and these days, that's a good thing.

Thanks to a tight insurance market, more insurers are dropping customers who make frequent claims. In some areas of the country, State Farm has decided to boot homeowners who have made more than two claims in three years.

Get dropped by one of the major insurers, and you could find yourself facing premiums that are three to four times what you're paying now.

Myth: Insurance should cover disasters that are likely to happen

More than 80% of California homeowners don't have earthquake insurance. That figure often stuns people from out of state, because of the widely held notion that the Golden State is a bowlful of geological jelly.

Californians, however, know that serious earthquakes are pretty rare. Most are mild, and almost all are very localized. So, the chances of your own home getting totaled in one are actually pretty slim. That excuses Californians from buying coverage, right? Hardly. Just as you may not be off the hook if you don't have flood or windstorm insurance.

As noted above, insurance is meant to protect you from financial catastrophe -- disasters from which you could not easily recover on your own.

Some people ignore this advice, figuring the federal government will come through for them in a disaster. You should know, however, that typically this help isn't free. Most help comes in the form of low-interest loans.

Many people lost their homes in the 1994 Northridge quake in California even with this aid. They

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found they couldn't simultaneously pay their mortgages and afford places to live while their homes were being rebuilt.

So if you don't have enough cash saved up to rebuild your home, or at least pay off the mortgage, and you live in an area where natural disasters are a distinct possibility, you need to consider appropriate coverage.

Myth: Insurance is a rip-off. Buy only the minimum required

This idea occasionally surfaces on the [Your Money message boards](#) and in e-mails I get from readers. People's suspicion of the insurance industry can be so profound they'll put themselves in real financial danger -- the old cut-off-your-schnoz-to-spite-your-face response.

Where it's scariest is when people skimp on liability insurance. This pays for the damage you do to other people or that they do to themselves on your property.

Say you're held responsible for an auto accident in which somebody is paralyzed. You can be on the hook for that person's medical expenses, lost income and care for the rest of his or her life. Injure more than one person, and the cost goes up exponentially.

If you don't have liability insurance, or you're carrying too little, most of what you own could be at risk. You could be sued and lose just about everything you've spent a lifetime working and saving to accumulate, plus perhaps your future earnings as well. All this because you wanted to save a couple of bucks on your premiums.

A smarter choice is to get enough liability coverage at least to equal your net worth. (Your net worth is everything you own minus everything you owe.) If your net worth is \$250,000, for example, boost the liability coverage on both your auto insurance and your homeowners insurance to at least \$250,000.

You can get more coverage for not much more money, and that's an especially good idea if you might be a lawsuit target: a doctor, a lawyer or a public figure of any kind.

Since most auto and homeowners policies have an upper limit on how much liability coverage they provide, you might need to buy an additional policy, called a personal liability or umbrella liability policy. These are typically fairly cheap: \$200 to \$300 for \$1 million of coverage.

3 ways to keep costs low

Now that I've talked you into buying more coverage, how can you keep your total insurance tab out of the five-figure range? As mentioned before, higher deductibles are one good way. Here are others:

Shop around. You've heard this one ad nauseam, but if you saw how widely premiums can range for the same coverage, you'd pay attention. One insurer can charge thousands of dollars more for an auto policy than another, for example. So call. Use the Web. Talk to a broker. Spend a little time doing your research, and the payoff could be huge.

Get every discount you can. This is another piece of oft-repeated, and oft-ignored, advice. Think about the things you've done to reduce your risks on your own and see if your insurer agrees they're worth giving you a break. A home or car security system, a good-driver course, not smoking -- all of these can lower your insurance costs.

Be prudent. It may not seem very exciting never to exceed the speed limit, maintain your car and keep your home in good repair, but such Dudley Do-Right behavior pays off in the insurance world. Insurers know that prudent people have fewer claims, so they get the best rates. (You also might want to pay your bills on time, while you're at it. More insurers are using credit scores to help set rates, figuring that people who are prudent about credit are also prudent about managing other risks.)

Most of all, try not to get emotional about your insurance. It's no fun to think about all the bad things that can happen or to write those big checks every year. But once it's done, you can rest easier knowing that you're well and properly covered.

Liz Pulliam Weston's column appears every Monday and Thursday, exclusively on MSN Money. She also answers reader questions in the [Your Money message board](#).