Disclaimer
This course is developed for educational purposes and non-commercial use. It should not be construed as endorsement for any financial products or services. It in no way intends to convey legal, real estate, employee benefits, tax, insurance, or financial planning advice. It is a simple overview to educate those who are new to these subjects. Consultation with a professional is recommended for individual advice. These topics are complicated, dynamic, and constantly changing. Please check for current regulations, rules and laws.
Personal Risk Management Lesson Plan

Unit

1. Starting out

Your paycheck

Social Security

Compare employee benefits of major employers.

The future of Social Security and its impact on me

Check out paychecks.

Social Security

Employee benefits

Share your employee benefits. Tell your classmates what benefits you have with your current employer.

Fill out W-4s.

2. 20's

Auto insurance

Liability coverage

Lay out auto insurance needs. Get quotes and evaluate providers.

Share experiences with auto claims. What was covered? What was not?

Calculate your credit score

Employee benefits

Look at Social Security statement

3. 20's to 30's

Healthcare insurance

Coinsurance

Evaluate health insurance.

Common illnesses and their probability of occurring. How much do they cost?

Choosing a doctor.

Out-of-pocket limit

What can you do to improve health risk factors? Must cite evidence.

Evaluate health plan complaints.

Pre-existing condition

Indemnity plan

Managed care

HMO, PPO, POS

Ratings

4. 30s

Homeowner's insurance

Dwelling coverage

Evaluate homeowner's insurance

What factors are important in buying a house?

Create an inventory of possessions

Deductible
Life Insurance
- Personal property
- Share your experiences with property insurance claims.

Perils
- What can you do to reduce risk on your home?

Loss
- 5
- 40s
- Retirement benefits
- 401K
- Evaluate disability insurance.
- What do you have in your 401K?

Class Activities
- Risk return of asset classes.

Disability Income insurance
- IRA
- Deciding on your contribution and funds in a 401K.

Caring for your parents
- Liability
- Defined benefit
- Defined contribution
- Own or any occupation
- Elimination period
- Noncancellable or guaranteed renewable
- Exclusions

50s and 60s
- Long term care
- Home health care
- Evaluate long term care.
- What are your health care needs when you retire?

Medicare
- gap
- Assisted living
- Medicare
- Nursing home
- Eligibility
- Maximum daily benefit
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Personal Risk management is a one-credit course that focuses on how individuals can protect their wealth by risk management. It focuses on the insurance industry and its consumer products. The learner will evaluate personal insurance needs. This course also outlines the basic benefits offered by employers. Learners will become familiar with what these benefits are and how to use them for long-term financial planning.

Insurance:
- Auto insurance (Deductibles, liability, collision, comprehensive)
- Health insurance (Deductibles, co-pays, etc.)
- House insurance – Deductibles, limits, etc.
- Umbrella Insurance
- Life insurance (term, whole life, variable annuities and how they work)
- Long term disability income insurance
- Long term care insurance

Employee benefits:
- Retirement benefits (pensions and 401K plans)
- Health benefits
- Other benefits such as leave, disability, etc.
- Government provided benefits such as Social Security and unemployment insurance
- Dependent Care and Health Care Spending Accounts

The learner will analyze personal risk factors and determine methods of mitigating this risk. They will evaluate various forms of insurance and their benefits and costs. They will prepare personal information for appropriate insurance quotes. They will evaluate the differences in risk between two or more health insurance packages. They will analyze personal risk management. They will review a social security summary statement and evaluate what benefits are received. They will describe major employee benefits (medical, disability, life, etc.) and what they cover. They will analyze a case study of health insurance and determine relevant costs. They will evaluate the differences between three or more medical insurance packages. They will design an employee benefits package using relevant components. They will evaluate the financial benefits of spending a 401K, profit sharing or pension benefits.
About this Course for the Student

Risk management is about conserving your wealth. That is something that you want to think seriously about. It takes you a lot of effort to earn your wealth. It would be regrettable to lose it because you didn’t take precautions to safeguard it from unfortunate events. Some of the ways you can conserve your wealth is by buying insurance to cover for losses and expenses. But insurance is a complicated product. You have to know what you’re buying and carefully evaluate what makes sense to you. This course will teach to you about the auto, health and homeowner’s insurance that just about everybody needs to have. It will also look at life, disability income, and long term care insurance. You will also get a primer on employee benefits and they often provide a safety net for you. At the end of this course, you will be expected to know how to evaluate policies and decide if it is right for you. You will also be expected to define various employee benefits and understand the choices that you will have to make.
### Financial Strategies for a Lifetime

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<th>Twenties</th>
<th>Twenties - Thirties</th>
<th>Thirties</th>
<th>Forties - Fifties</th>
<th>Sixties - Plus</th>
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<td><strong>Protect financial dreams</strong></td>
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<td>● Set exciting goals</td>
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<td>● Create a will to protect your assets</td>
<td>● Updated will</td>
<td>● Ladder ed investments or annuities to cover for retirement income</td>
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<td>● Get adequate auto, health, and rental insurance</td>
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<td>● Expand investment portfolio by asset allocation</td>
<td>● Income to last lifetime</td>
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<td>● Form a financial team with your partner</td>
<td>● Create a plan to financially survive a job change situation.</td>
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<td>● Victimized by identity theft</td>
<td>● Destroying relationships over financial problems</td>
<td>● Taking on too much debt - Bankruptcy</td>
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<td>● Not enough income for retirement</td>
<td></td>
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<td></td>
<td>● Financial ruin from inadequate insurance</td>
<td></td>
<td></td>
<td>● Victimized by fraud because of lack of education</td>
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How does a typical person look---financially? Not as prosperous as most of us believe. The typical family income in Washington State is $63,000 in 2006 dollars. Household income tends to go down during recessions and recover afterwards. Although it’s increased throughout most of the last century, it’s been flattening in recent years and still hasn’t recovered from the last recession to its 2000 peak. This means that income might not grow as quickly in the future. Some evidence suggests that people coming out of school and college now may be the first generation to make less than their parents, mainly because the US economy is not growing as quickly as it used to. According to the Economic Mobility study, the economy grew 17% in the last generation as compared to 52% in previous generations.

<table>
<thead>
<tr>
<th>Washington</th>
<th>2006 Median Income</th>
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<td>Total:</td>
<td>63,705</td>
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<tr>
<td>2-person families</td>
<td>58,584</td>
</tr>
<tr>
<td>3-person families</td>
<td>66,252</td>
</tr>
<tr>
<td>4-person families</td>
<td>75,140</td>
</tr>
<tr>
<td>5-person families</td>
<td>68,562</td>
</tr>
<tr>
<td>6-person families</td>
<td>62,484</td>
</tr>
<tr>
<td>7-or-more-person families</td>
<td>61,212</td>
</tr>
</tbody>
</table>

Source: US Census
Your income changes depending on the economy, tending to go up during good times and down during bad. It also changes depending on where you are in your life. You start your life as a financial drain on your parents, costing most middle-income families about $10,000 a year. Your income rises as you get more established in life, peaks about the time you are 50 years old and then declines as you move towards retirement and retire. But this chart doesn’t tell the whole story.

What can you do to improve your financial status? Education has an impact. Here is a chart that describes the impact of education on your salary. There is a big jump in earnings when you get your college degree and even a bigger jump if you get a professional degree such as engineer, accountant, lawyer or doctor. Keep in mind that even with the same education, women make 60% to 70% of what men make. Some speculate that this is because women are still the main caregivers for both parents and children and may take time off to give this care.
Of course, your financial life doesn't proceed as smoothly as even these charts show. Right now the average time that someone stays in a job is about 5 years. So that there's a pretty good chance that you'll be unemployed, underemployed, or self-employed for periods in your working life. On average folks have 4.5 spells of unemployment during their working life and they last on average about 3 months. This suggests that having an emergency fund or 3 to 6 months of income to tide you over such periods is a very good idea.

Other life events such as marriage (70% of people get married) can have an effect on your financial life. Marriage increases a person’s wealth by about 77% because two can live as cheaply as one and half. Divorce (40% to 50% of first marriages end in divorce) can have a significant impact on your financial life. Divorce can decrease your wealth by 77%. Marriage becomes the most significant financial decision you will make in your lifetime.

You already know that children can have an impact as well. Just as you cost your parents so your kids will cost you $10,000 a year for a total of $184,000. When they go to college, the average cost of a college education at a Washington state public university is $20,000 per year or about $80,000 for a bachelor’s degree. Other colleges can be priced at [http://apps.collegeboard.com/search/index.jsp](http://apps.collegeboard.com/search/index.jsp). At the same time as you pay for your kid’s education, you may have to bear some financial responsibility for your parents ($5500 per year).

It follows that net worth or the amount of wealth you have also increases as you age. Your net worth---what you own (home, retirement accounts, investments, etc.) less what you owe (mortgage, car loans, etc.)---grows over your lifetime and declines as you retire and no longer earn money.
Debt is a big part of your net worth formula. The goal is to keep your financing payments (credit card payments, car loans, student loans and mortgage payments) well below 40% of your income while you are working and to pay down all debt by the time you retire.

For most folks, as can be seen by the graph above, their home is the largest part of their net worth. People tend to buy their first house when they are 32 (typically 1812 square feet for $236,500 in Washington state) and upgrade when they are older ($300,000). That house can also be a financial drain with replacing the roof, appliances, the furnace, or even a major renovation. However, as a financial asset, don’t depend on your home. Most folks view their homes very emotionally and will not sell it even when they retire. About 70% of people who retire don’t sell or even take money out of their homes to fund their retirement.

<table>
<thead>
<tr>
<th>Location</th>
<th>2006 Median Price</th>
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<tr>
<td>Kennewick-Richland-Pasco</td>
<td>$156,100</td>
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<tr>
<td>Portland-Vancouver-Beaverton</td>
<td>280,800</td>
</tr>
<tr>
<td>Seattle-Tacoma-Bellevue</td>
<td>361,200</td>
</tr>
<tr>
<td>Spokane</td>
<td>184,100</td>
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<tr>
<td>Yakima</td>
<td>136,500</td>
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Source: National Association of Realtors

As you head into retirement, you have to deal with making sure that your financial resources last you for the rest of your life and that you have taken precautions to protect your assets. Senior citizens are targets of all the scam artists because they have assets and they are trusting or often lonely. As you navigate your way through your financial life, it’s important to learn crucial skills to help you deal with all the twists
and turns that can be thrown at you. It’s important that you get smart about your money no matter where you are in this journey.

Now that you have a good idea of what your financial life looks like, you need to acquire the investing skills and habits that will serve you through your life. In this first section, you will learn about setting goals and creating a spending plan. These two items are of vital importance in keeping your investing program on track.

**Setting Financial Goals**

The first important step in your strategy to a secure financial future is to have goals. When we don’t have goals we drift and at the end of our work lives, we wonder why we didn’t do what we wanted (whatever that was). When we have goals, we achieve them, especially if they are written down.

Now you will have short-term and long term goals. The short-term ones can include a car or a vacation. Long term goals are the house, your children’s education and your retirement. Lay out your lifetime financial goals. That’s right—for your whole life. It is tough because we tend to have short-term horizons. But, you need to think about all your goals now because some of them will take a long time to achieve.

According to The Facts about Saving and Investing (1999) put out by the SEC, two out of three of all US families fail to reach one major financial goal. Identify financial or saving goals that excite you, such as saving to buy a car; staying home with the kids; leaving an awful job; paying off your mortgage; starting your own business; traveling with your family or friends, helping others, and more.

Set realistic goals using the SMART approach:

- **Specific.** Smart goals are specific enough to suggest action.
  
  “Save money for a used car.”

- **Measurable.** Goals need to be measurable when you’ve reached your goal.
  
  “This used car will cost $8000 so I need to save $1,000 for a down payment.

- **Attainable.** Goals need to be reasonable.
  
  “$8000 for a used car (versus $20,000 for a new car) is reasonable for my circumstances.”

- **Realistic.** The goals need to make sense.
  
  “I make $30,000 a year so a used car so saving $84 a month for $1000 makes sense.”

- **Time-related.** Set a definite target date.
  
  “I can save $84 per month and reach $1000 within 12 months.”
Education

Education seems to be a necessity in this new global age where higher skill sets are necessary. But, education is also a big ticket item with students paying on average $10,000 a year in tuition plus $10,000 in living expenses to go to Washington state’s public four-year universities. For four years, this can add up to $80,000. If you go on to pursue a professional degree such as a law or medical degree, the cost goes over $100,000. Even community college costs $4000 a year. With this large cost, often grandparents must chip in along with parents to ensure that the kids in the family have a chance to get the college education.

Activity

What is the difference in cost between a public and private university? Check out colleges in Washington State such as Seattle University and Whitman and compare them to the University of Washington and Washington State. http://cgi.money.cnn.com/tools/collegecost/collegecost.html

First House

The first major financial goal for most folks starting out is the house. If you’re living in a typical Washington state city a house might cost you $200,000, or $40,000 down payment (keep in mind that these prices vary greatly depending on where you live).

Activity

Although these sites are not totally accurate, check out www.zillow.com as to the price of a house in a neighborhood that you want to live in. How much will you have to pay for the house?

Retirement
Most of you are going to live longer than the current life expectancy (about 78 years) because of developments that are prolonging life. This means that you will have to ensure that you have enough money for a longer period of time. If you think Social Security will take care of your lengthening requirements, you might want to reconsider. Social Security currently gives you a minimum wage (the average payment as of 2006 is $955 a month and the maximum is $1500). It covers about 42% of retired people’s needs if they made $15,000 before they retired. If they made $60,000, Social Security covers 25% of their needs. Right now workers are putting more into the social security than retirees are taking out. But that is expected to change in about 25 years. At that time, according to the Social Security Administration, people who retire will receive only 75% of the current entitlement. Reviewing your Social Security report gives you an amount that you can consider as a “floor” of your retirement income. If you don’t want to live at that income level (about 25%) you will need to start saving. We will address Social Security again in Unit 6.

Although folks think that they will reduce spending when they retire, most keep their level of spending up. Many people keep their homes (and all the expenses that come with them) when they retire. When you get older, some expenses get bigger. Your medical costs increase. Medicare takes care of 54% of your needs, but you must pay extra for doctor’s visits. If you need long-term care such as a nursing home, you have to pay the bill yourself.

Nowadays, most people are resigned to the fact that employers will no longer take care of you when you retire. Most people don’t work long enough at any company to even qualify for the traditional pension plans. It’s true that employers are slowly phasing out traditional pension plans and phasing in retirement savings plans (401k) that require you to save and invest for yourself. Employers believe that these types of plans match what workers do. Most workers don’t stay the 5 years necessary to get any benefits, let alone the 30 years it takes to get adequate benefits from the traditional plans. With the 401k plans, when these workers leave they can take their retirement accounts with them.

Although many people know that these retirement savings plans will be their main source of retirement income, about 18% don’t contribute at all. When people leave their companies, many cash out and spend their retirement money instead of “rolling it over” into other retirement plans. This means at their next job, they start out with nothing in retirement. Younger folks tend to do this most and they are the most hurt by cashing out. Even small amounts set aside early in your working life can work hard for you over time. If you’re cashing out, most of the benefits of compounding are lost.

The experts don’t always agree on the amount you need for retirement because there’s so much uncertainty involved in the amount of social security and your longevity not to mention inflation rates and rates of return. It’s estimated that baby boomers (who are starting to retire now) have about one third of what they need to retire.

As a rule of thumb, you can estimate the amount of money that you expect to live on a year and divide by 4% to come up with what you might need in your retirement fund if you have no other sources of retirement income.

**Question**

When you retire, Medicare takes care of what portion of your medical expenses when you retire?

a) One quarter  
b) One half  
c) Three quarters

---

**Financial Education at BCC**

Investing in Washington’s Future

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Question
When you retire, Social Security benefits can cover what portion of your living expenses?

a) One quarter  
b) One half  
c) Three quarters

Question
Your life expectancy when you reach age 65 is:

a) 13 years  
b) 18 years  
c) 23 years
Other goals

Maybe you've got other goals, like starting your own business (Jeff Bezos used $60,000 of his own money to start Amazon.com). Lay them all out and put a price on them. You won't get there from here unless you do. According to the 2004 Consumer Finance Survey, here are the top reasons people save:

<table>
<thead>
<tr>
<th>Goal</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Retirement</td>
<td>34.7%</td>
</tr>
<tr>
<td>Liquidity</td>
<td>30%</td>
</tr>
<tr>
<td>Purchases</td>
<td>7.7%</td>
</tr>
<tr>
<td>Buying own home</td>
<td>5%</td>
</tr>
<tr>
<td>For the family</td>
<td>4.7%</td>
</tr>
<tr>
<td>Investment</td>
<td>1.5%</td>
</tr>
<tr>
<td>Education</td>
<td>11.60%</td>
</tr>
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</table>

Once you've got your list of goals, post them where you will see them every day, re-evaluate every year. Your needs may change. Tax time is a good time since you're looking at your finances any way. Your tax return will tell you how much you earned and you should figure out how much you spent. Did you save enough for the year? Check out your goals. Do you have additional goals now? (A life event—marriage, having kids, etc. — tends to change your financial goals.)

Activity

Estimate how much you will need when you retire. Use a simple rule of thumb. Most people will take out 4% of their retirement fund for annual living expenses. Decide what level of lifestyle you want when you retire (e.g. $40,000, $60,000, etc.) and divide by 4%.

Create a spending plan

A spending plan is a planning tool to help you manage your money. It is the core of your financial strategy and if implemented and made a habit all your life, you will achieve financial security. A spending plan helps you identify your personal financial goals, analyze what income you have available, know what you are spending money on, and develop steps to achieve your personal financial goals. A spending plan will help you:

- Achieve financial goals and dreams.
- Keep a positive attitude about personal finances.
- Save for those important things such as a new car, college education, wedding, new house, comfortable retirement, or travel.
- Lower stress level and reduce conflicts in your family.
- Control spending so that you conserve your wealth.
- Eliminate unnecessary debt.

This is how Americans spend their money according to the *Bureau of Labor Table of 2004 Expenses by Family Size*. 
Start by collecting your pay stubs, household and other bills, expense receipts, checkbook or online checking data, checking and credit card statements. Sort the receipts by categories and sections listed on the Spending Plan Worksheet (see appendix). The sections are: Income, Fixed Expenses, Variable Expenses Discretionary Expenses and Adjustments to Spending Plan. Total the dollar amounts in each of these categories for one month. Don't forget to record your cash expenditures and online transactions. Look to see where your cash goes, especially if you make frequent ATM withdrawals from your bank accounts.

To make it easier to create a spending plan that will work for you, a 4-step process will be used to develop each section of the Spending Plan Worksheet.

1. Calculate your monthly income
2. Calculate fixed, variable and discretionary expenses
3. Calculate Net Income (Monthly Income minus Total Expenses)
4. Analyze expenses starting with your discretionary expenses and make spending plan adjustments such that you can achieve your saving goals. If necessary, identify your debts to pay down and create a debt reduction plan

For more details on how to create a spending plan, you can refer to the first module of this series on Money Management. It is important that you have a spending plan each year and that you track all expenses to your spending plan. This could include a good manual record-keeping system. Here are some suggestions on the financial records you should keep.
<table>
<thead>
<tr>
<th>Type of record</th>
<th>Length of Time</th>
<th>Reason to Keep</th>
</tr>
</thead>
</table>
| Bills                                  | One-year to permanently | • Review your bill statements once a year.  
• For most cases, when the canceled check from a paid bill was shown on your checking statement (or the canceled check has been returned with your statement), you can shred or burn the bill.  
• However, bills for large purchases, such as appliances, furniture, cars, jewelry, computers, rugs, collectibles, antiques, etc., should be kept in an insurance file for proof of their value in the event of loss, damage, flood, or fire. |
| Credit card receipts and statements    | 45 days to seven years | • Keep your original receipts until you get your monthly statement.  
• Shred or burn the receipts if the receipts match the monthly statement  
• If a large purchase listed above, keep the receipt. |
| Bank records                           | One-year to permanently | • Go through your checks each year and keep those related to your taxes, business expenses, mortgage payments and home improvements.  
• Shred or burn those that have no long-term importance. |
| Paycheck stubs                         | One year             | • Keep all your paycheck stubs until you receive your annual W-2 form from your employer; make sure the information matches the stubs and W-2.  
• If it does match, shred or burn the stubs.  
• If it does not match, request a corrected form, known as a W-2c. |
| Taxes                                  | Seven years          | The IRS has three years from your tax filing date to audit your tax returns, if it finds questionable good faith errors.  
• The three-year deadline also applies if you discover a mistake in your return and decide to file an amended tax return to claim a refund.  
• The IRS has six years to challenge your return if it thinks you under-reported your gross income by 25% or more.  
There is no time limit if you failed to file your return or filed a fraudulent tax return. |
<p>| IRA contributions                      | Permanently          | If you made a non-deductible contribution to your |</p>
<table>
<thead>
<tr>
<th>Category</th>
<th>Retention Period</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>IRA</td>
<td>Indefinitely</td>
<td>Keep your records indefinitely to prove that you paid tax on this money when it comes time for you to withdraw from your IRA account(s).</td>
</tr>
</tbody>
</table>
| Retirement/Savings plan statements           | One year to permanently | - Keep the quarterly statements from your 401(k) or other plans until you receive the annual summary statement. If it matches up, then shred or burn the quarterly statements.  
- Keep the annual summary statements until you retire or close the account. |
| Brokerage statements                         | Until you sell the securities | Keep the purchase confirmations or sales slips from your brokerage or mutual fund to prove whether you have capital gains or losses at tax time. |
| House/condominium records                    | Six years to permanently | - Maintain deeds, mortgage documents, title, cost of improvements, and closing statements in a safe place permanently.  
- Keep tax, rental agreements, rental receipts and repairs for 7 years.  
- Keep records of the expenses incurred in selling and buying the house/property, such as legal fees and your real estate agent’s commission, for six years after you sell your house.  
- Keeping these records is important because any improvements you make on your house, as well as expenses in selling it, are added to the original purchase price or cost basis. This adds up to a greater profit (also called capital gains) when you sell your house. Therefore, you lower your capital gains tax from the sale of your house. |
| Loan agreements                              | When outstanding | Keep copies of all outstanding loan agreements and most recent statements indicating how much you have repaid. |
| Insurance policies                           | Long term care and life insurance – permanently | - Keep your insurance cards in your cars as required by law.  
- Keep copies of your most recent homeowners, auto, and umbrella insurance policies so that claims can be made easily and efficiently.  
- Keep both long-term care and life insurance in a safe place and let a responsible person know how to find them.  
- Create and update an annual inventory of all personal property. Include appraisals or receipts. Keep a copy of this in a safe place outside of your home. |
|                                             | Others one year after expiration |                                                                                                                                     |
| Health care expenses                         | One year to seven years | - Keep your original receipts to file health insurance and flexible spending account claims.                                                                                           |
Protect Your Wealth

The Federal Trade Commission received over 674,354 Consumer Sentinel complaints in 2006. 64% represented fraud and 36% were identity theft complaints. Identity theft occurs when a thief uses another person’s personal identification to open new credit card accounts, take over existing accounts, and obtains loans in the victim’s name, of otherwise steal funds from the victim. Victims go through a difficult and time-consuming ordeal to clear their names. They must first try to convince the lenders and the credit-reporting agencies that they are victims of identity theft. They also must deal with calls from collection agencies and endless paperwork in trying to remove erroneous information and fraudulent accounts from a credit record.

Credit card fraud (28%) was the most common form of reported identity theft followed by phone or utilities fraud (19%), bank fraud (18%), and employment fraud (13%). Other significant categories of identity theft reported by victims were government documents/benefits fraud and loan fraud. The percentage of complaints about “Electronic Fund Transfer” related identity theft doubled between 2002 and 2004.

Thieves get information from
- Garbage – pre-approved credit cards, bank and credit card statements, and utility bills
- Mailboxes – both incoming and outgoing mail
- Loan applications – banks, car dealerships, mortgage companies
- Rental applications – cars or apartments
- Schools – classroom attendance sheets that list the student’s Social Security number
- Desk drawers in the workplace
- Certifications/licenses placed on walls (in the workplace)
- Job applications
- Health club applications
- Internet – information resulting from the sale of personal banking and investment details, chat rooms, and false merchants
- Telephone companies
- Information freely given by the public – from warranty cards, for contests, to department stores, and “Win a Free Membership…” forms

Advice to avoid identity theft
- Don’t disclose any personal information that isn’t integral to a transaction.
- Be careful of any personal information that you give on yourself in social networking sites and safeguard financial information on your computer or other file storage centers.
- Carry only one or two credit cards that you use regularly.
- Keep your Social Security number as private as possible. If a salesperson requests it, don’t give it. If your health plan prints it on your membership card, ask for one without it. Don’t write it on your class attendance sheet (your school already has your number on official records). Divulge this number only for legitimate purposes, such as paying taxes, requesting credit, or obtaining a driver’s license. Check to see if your social security number is on the internet at StolenIDSearch.com.
- Shred or burn mail containing personal information – from account numbers to travel itineraries.
- Prevent mail theft. Have a locked mailbox. Don’t leave mail in your mailbox for the mail carrier. Don’t have new checkbooks delivered to your home.
- Lock up your personal papers and canceled checks in your home, in case of a break-in.
- Be cautious on the telephone. Never give out your name, address, Social Security number, or other personal information unless you initiate the call and you check to see that the number of legitimate.
- Secure all your financial files on your computer and don’t store your personal information on the web storage files that can be hacked into. Don’t disclose personal information on social networking sites.
- Demand secure information handling. If you’re filling out a credit application at a department store or auto dealership, find out what the establishment does with old applications. If it doesn’t lock them in file cabinets or shred them, take your business elsewhere.
- Pay attention to your bills. If you suddenly stop receiving your mail, particularly bills, that could be a sign that someone has taken over your account.

Fraud examiners recommend that people review their credit reports once a year; all three bureaus will need to be contacted.
- Equifax – To order a credit report: 800-685-1111. To report fraud: 800-525-6285
- Experian – To order a credit report and report fraud: 888-EXPERIAN (888-397-3742)
- Trans Union – To order a credit report: 800-888-4213. To report fraud: 800-680-7289

It’s also wise to opt out of pre-approved credit offers by calling 888-5-OPT-OUT (888-567-8688). A scam artist can retrieve a discarded credit card offer and send it to the company, saying, “Yes, I’m interested – and here’s my new mailing address!” Sign up on the National “Do Not Call” Registry (www.donotcall.gov or 1-888-382-1222) to eliminate telephone calls.
Future Financial Behavior Evaluation

<table>
<thead>
<tr>
<th>The goal of all financial education is to get you to adopt important behaviors that will ensure your financial security. Check all the financial behaviors that you engage in. Do this inventory every year.</th>
<th>Check if you will adopt in the next year.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pay all my bills and loan payments on time.</td>
<td></td>
</tr>
<tr>
<td>Have a recordkeeping system for my financial affairs.</td>
<td></td>
</tr>
<tr>
<td>Balance my checkbook and monitor all my financial transactions monthly.</td>
<td></td>
</tr>
<tr>
<td>Track all my expenses.</td>
<td></td>
</tr>
<tr>
<td>Use a spending plan or budget.</td>
<td></td>
</tr>
<tr>
<td>Have an emergency savings fund. If yes, how many months of expenses: 1-3 months ____ 4-6 months ____</td>
<td></td>
</tr>
<tr>
<td>Save or invest money from every paycheck. If yes, percent paycheck saved __%</td>
<td></td>
</tr>
<tr>
<td>Save for long-term goals. If yes, which goals: (Check any that apply.) Education ____ Car ____ Home ____ Home upgrade ____ Vacation ____</td>
<td></td>
</tr>
<tr>
<td>Plan and set goals for financial future.</td>
<td></td>
</tr>
<tr>
<td>Have money in more than one type of investment. If yes, check any that apply: Individual stocks ____ Mutual Funds ____ Bonds ____ Real Estate ____ Treasury bills or CDs ____ International ____ Commodities ____</td>
<td></td>
</tr>
<tr>
<td>Calculated net worth in the past two years.</td>
<td></td>
</tr>
<tr>
<td>Participate in employer’s retirement plan. 401(k) ____ 403 (b) ____ Other: ____</td>
<td></td>
</tr>
<tr>
<td>Have insurance to protect my loved ones. If yes, check any that apply: Health ____ Life ____ Property ____ Auto ____ Disability ____ Umbrella ____</td>
<td></td>
</tr>
<tr>
<td>Put money into other retirement plan: Roth IRA ____ Traditional IRA ____ SEP or SIMPLE IRA ____</td>
<td></td>
</tr>
<tr>
<td>Review my credit report annually.</td>
<td></td>
</tr>
<tr>
<td>Pay credit card balances in full each month.</td>
<td></td>
</tr>
<tr>
<td>Research and compare offers before applying for a credit card or loan.</td>
<td></td>
</tr>
<tr>
<td>Do my own taxes.</td>
<td></td>
</tr>
<tr>
<td>Read about personal money management to improve how I’m doing.</td>
<td></td>
</tr>
</tbody>
</table>
Managing risk all your life will be a product of managing the safety net the government has set up, the benefits your employer gives, and the insurance you purchase. It is important to know about all these elements. The government manages social security which gives you benefits based on contributions made by you and your employer. It also manages Medicare which provides health insurance to people over age 65. Other programs such as Medicaid assist low or no income families with health needs.

Employers can provide some or a full menu of health insurance, disability and other benefits which cover you, and your family’s, needs. Insurance is a service that is paid for with the hope that the insured person will never need to use the service. However, the likelihood that it will be needed makes it a necessary element in financial planning. During different stages in life, there are different needs for insurance. As you start out, auto, health, and renter’s insurance may be all you need. As you grow older, buy a house, and have a family, you may need property, life and long term disability insurance. The more assets you accumulate, the more necessary it is to review your current policy limits and needs. You may need an umbrella policy to cover liability in excess of what you are covered for. It is also advisable to review the laws of the state to determine if you are in compliance when evaluating insurance requirements.

There are four main risks in insurance. They are:
1. Being uninsured/under-insured and unable to absorb the costs of the occurrence without taking a hit to your net worth.
2. Being over-insured and paying for more insurance than is necessary given your circumstances.
3. Not being in compliance with state law and suffering the consequences.
4. Being ill informed and making poor insurance decisions resulting in being under or over insured.
Insurance is a multi-billion dollar industry in the United States. This industry uses specific terms and vocabulary. It is necessary to understand the vocabulary to evaluate what kind of insurance you are purchasing, what it will cover and what it will not cover (exclusions). Only then can an intelligent decision be made on if the cost is worth the value for the insurance policy.

The insurance policy is a contract between you and an insurance company in which you pay premiums and they will cover the loss if it happens. Insurance companies would prefer to collect premiums, have no claims, and increase their profits. And they will stick to the letter of the policy when you make a claim. You want to make sure that you are clear on everything before you sign the policy so there are no surprises.

**Question:**
What relationship does risk management have to conserving your wealth?

**Question:**
There are four main risks in insurance, what are they?

---

**Unit 1: Starting Out**

Your Paycheck

Your Paycheck Summary

1. Payroll checks can be monthly, bi-weekly, or weekly.
2. Your payroll check can be a paper check or electronic deposit.
3. Understanding your paycheck is important.
4. Your paycheck will have deductions from your gross payroll for taxes. These include Social Security, Medicare, federal income tax withholding.
5. Your paycheck will have deductions from your gross payroll for other items, such as medical premiums and 401k contributions if your company provides these benefits.
6. The employers may show the employer contribution costs associated with your employment, such as, matching the Social Security and Medicare, worker’s compensation, medical premium, 401k, etc.
7. US citizens and non-citizens, who are permitted to work, must have a social security number to get a job.
8. It is best to withhold the correct amount of Federal Income Tax, not more, or less than required. If you withhold too little you may face IRS penalties if you withhold too much you are giving the government free use of your money.
Deciphering your paycheck is an important step towards understanding personal risk management. Although some folks receive monthly paychecks and some weekly, most people receive a biweekly (every two weeks) pay check. Some folks receive their paychecks in paper form and deposit it in the bank. Others get them directly deposited into their accounts. A pay stub tells you what your gross pay is and what was deducted. These are received in paper form or they may be available to you on an employee website.

The following is a very simple pay check for Jill. Jill makes $30,643 from her job as a manager of a store. On the left side, you can see Jill’s gross biweekly salary and deductions. The first two are US government “safety net” entitlements: Social Security for elderly income and Medicare for elderly healthcare. Withholding refers to the taxes that are set aside to pay for federal taxes. This is reconciled with what you actually owe when you file your tax return on or about April 15 of every year. Withholding too much or too little taxes can is not in your best interest. It’s best to try to estimate what you will be paying and make your withholding match it. Medical premium covers Jill’s share of the medical coverage provided by her employer. The 401K is her contribution to her retirement savings account. Out of her gross biweekly pay of $1178.26, Jill gets to take home $900.96.

On the right hand side of your paycheck, employers often like to show their share of benefits. The first two items show the employer’s share of Social Security and Medicare. Employers are required to match the payments made by employees on these items. They are required to pay worker’s compensation into a pool that will cover any work-related injuries or illness. Unemployment covers benefits paid to laid-off workers. The 401K contribution is a match to the employee’s contribution and goes into the employee’s retirement account. Employers often pay the bulk of the premiums for medical coverage.

**Biweekly Paycheck for Annual Salary of $30,643**

<table>
<thead>
<tr>
<th>Gross Pay</th>
<th>Employer Contribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Social Security (6.2%)</td>
<td>Social Security</td>
</tr>
<tr>
<td>73.05</td>
<td>73.05</td>
</tr>
<tr>
<td>Medicare (1.45%)</td>
<td>Medicare</td>
</tr>
<tr>
<td>17.08</td>
<td>17.08</td>
</tr>
<tr>
<td>Withholding taxes</td>
<td>State Unemployment</td>
</tr>
<tr>
<td>117.83</td>
<td>22.35</td>
</tr>
<tr>
<td>Medical Premium</td>
<td>Medical Premium</td>
</tr>
<tr>
<td>22.20</td>
<td>101.16</td>
</tr>
<tr>
<td>401K</td>
<td>401K</td>
</tr>
<tr>
<td>47.13</td>
<td>47.13</td>
</tr>
<tr>
<td>Net Pay</td>
<td>Worker’s Compensation</td>
</tr>
<tr>
<td><strong>900.96</strong></td>
<td>33.95</td>
</tr>
<tr>
<td></td>
<td>Federal Unemployment</td>
</tr>
<tr>
<td></td>
<td>2.15</td>
</tr>
<tr>
<td></td>
<td><strong>296.87</strong></td>
</tr>
</tbody>
</table>

Even on this relatively simple paycheck, which might be typical for a smaller firms, your employer pays about one-quarter of your pay in benefits. Larger firms typically offer more benefits (up to 35% of your pay).

**Social Security**
All employees need a social security number to get a job. It's important for collecting social security benefits and receiving some other government services. When you get a job, your employer will ask for a copy of your social security card. US citizens and non-citizens who are permitted to work in the US can apply for a social security number. The Social Security Administration requires proof of citizenship, identity and age. Anyone over 18 years of age must apply in person. For more information on how to apply, go to [www.ssa.gov](http://www.ssa.gov).

Social Security

**Social Security Summary**

1. You will get only one Social Security number in your life. Safeguard it. Don’t give it out unless you know that it will be safeguarded. It is not necessary to give it to health clubs, storage centers, health plans, etc.
2. Social Security taxes are collected both from the employer and the employee.
3. There is a maximum taxable amount that can be changed annually by the government; for 2008 it is $102,000.
4. It is important to verify that your records with social security reflect the amounts shown in your payroll records. This can be done on line at the social security website.
5. If you retire before the social security age for full benefits (65 if born before 1952, 67 if after 1952) you will receive reduced benefits for the rest of your lifetime.
6. Social security includes OASI, DI and Medicare programs
7. The OASDI Trustee Report states that in 2017 the social security administration will pay more benefits than it receives in contributions. They estimate that in 2040, social security will only be able to pay 74 cents of every dollar owed beneficiaries under the current benefit structure.
8. The Social Security funding issues make the current stated benefits only “estimates”, not amounts that you can “depend on”.
9. It is important to not rely on social security to take care of your needs.

Social security was started in 1935 as safety net for the elderly. It is a mandatory program for all workers. People can get information on how to get a social security number from [www.socialsecurity.gov](http://www.socialsecurity.gov). It is important because you need it to get a job, collect Social security benefits and receive other government services. Many other businesses, such as banks and credit companies, will ask for this number. If you are a non-citizen, the Social Security Administration will require a work permit or immigrant status in order for...
you to apply. Once you get your number, it is important to safeguard it. Social security numbers can be used for identify theft.

Although most people think of it as providing for income after age 65, it has three programs:

- **Old age and survivor insurance (OASI)** – This provides income for the elderly and their survivors. This includes under-age children.

- **Disability insurance (DI)** – This provides income for those disabled and unable to earn income. It also provides income for those dependent on the disabled individual for their support.

- **Medicare** – This is health insurance for the elderly and will be discussed in the section on health care.

According to the 2006 OASDI Trustees Report, 156.6 million workers paying social security taxes contributed $593 billion to the trust fund in 2005. They are taxed 5.3% for OASI and 0.9% for DI for a total of 6.2% up to the maximum of $102,000 in 2008. Employers must match this contribution with their own 6.2%. Any income over $102,000 is not taxed. This maximum income has been adjusted throughout the years, so a worker was taxed on a smaller maximum in the past. It is up to the employer to collect this tax from the employee, match it with their own contribution and submit it on a timely basis to social security.

In 2005, social security cost $530 billion with a total of 39.7 million receiving benefits. Retired workers accounted for 30.0 million, the wife, husband, child of retired worker accounted for another 3.1 million, and survivors accounted for 6.7 million. The average monthly benefit to a retired worker in 2007 was $1,044 955. The maximum benefit that could be received in 2007 was $2,116.

**Social Security Benefits**

A worker is considered fully insured if you’ve worked 40 credits (previously known as quarters, which can equate to 10 years). With the way the system works, those who earn the most get the most but lower-income folks get relatively more as a proportion of their working income. Currently, an individual can retire at age 62 with a reduced benefit. For folks born after 1952, full benefits don’t accrue until age 67. The age for full benefits is scheduled to go up to 69. The benefits do not go up when you reach the full retirement age. They are set when you retire, and would only increase with inflation (a cost of living) allowance. Social security benefits increase the more you if you delay retirement until you reach full retirement benefit age. If you work after you start receiving benefits, here are limits to how much you can earn and still receive the benefits. Social security benefits increase with inflation. If you are a couple and both receive benefits, and one of you dies, the benefit is reduced to higher of the two benefits. An example, a husband and wife receive $1,200 and $1,000 dollars a month respectively. Your household receives $2,200 in social security. The husband dies. The wife now receives the higher of the two benefits, $1,200. Your household now only receives the $1,200. This continues as a widow(er) status. Remarriage changes this status. Visit [www.socialsecurity.gov](http://www.socialsecurity.gov) for complete details, laws and rules.

Actual benefit calculation is complicated so you are encouraged to get and review your social security statement every year. You can obtain your social security statement at [www.socialsecurity.gov](http://www.socialsecurity.gov).

The following tables show how much of your retirement income will be based on social security by what income group you are in. This shows that as you get older, your income gets lower and a larger percent is dependent on social security.
## Married 2002 -- AGES 65-74

<table>
<thead>
<tr>
<th>Income Level</th>
<th>Lowest 20%</th>
<th>20% - 40%</th>
<th>40% - 60%</th>
<th>60% - 80%</th>
<th>Highest 20%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets</td>
<td>516</td>
<td>1,862</td>
<td>4,423</td>
<td>7,780</td>
<td>35,500</td>
</tr>
<tr>
<td>Pension benefits</td>
<td>1,552</td>
<td>6,052</td>
<td>12,781</td>
<td>21,467</td>
<td>49,555</td>
</tr>
<tr>
<td>Social Security and other government programs</td>
<td>12,715</td>
<td>16,895</td>
<td>17,815</td>
<td>18,197</td>
<td>19,184</td>
</tr>
<tr>
<td>Earnings</td>
<td>963</td>
<td>3,325</td>
<td>6,710</td>
<td>14,723</td>
<td>63,612</td>
</tr>
</tbody>
</table>

## Married 2002 -- AGES 75-84

<table>
<thead>
<tr>
<th>Income Level</th>
<th>Lowest 20%</th>
<th>20% - 40%</th>
<th>40% - 60%</th>
<th>60% - 80%</th>
<th>Highest 20%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets</td>
<td>431</td>
<td>1,628</td>
<td>4,695</td>
<td>7,847</td>
<td>29,719</td>
</tr>
<tr>
<td>Pension benefits</td>
<td>1,207</td>
<td>5,485</td>
<td>9,092</td>
<td>16,261</td>
<td>44,695</td>
</tr>
<tr>
<td>Social Security and other government programs</td>
<td>12,785</td>
<td>16,655</td>
<td>18,726</td>
<td>19,189</td>
<td>22,113</td>
</tr>
<tr>
<td>Earnings</td>
<td>159</td>
<td>953</td>
<td>1,523</td>
<td>4,557</td>
<td>15,769</td>
</tr>
</tbody>
</table>

## Married 2002 -- AGES 85+

<table>
<thead>
<tr>
<th>Income Level</th>
<th>Lowest 20%</th>
<th>20% - 40%</th>
<th>40% - 60%</th>
<th>60% - 80%</th>
<th>Highest 20%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets</td>
<td>327</td>
<td>1,694</td>
<td>2,941</td>
<td>9,027</td>
<td>65,415</td>
</tr>
<tr>
<td>Pension benefits</td>
<td>370</td>
<td>2,434</td>
<td>6,288</td>
<td>8,657</td>
<td>23,379</td>
</tr>
<tr>
<td>Social Security and other government programs</td>
<td>10,794</td>
<td>17,083</td>
<td>19,481</td>
<td>20,776</td>
<td>21,769</td>
</tr>
<tr>
<td>Earnings</td>
<td>53</td>
<td>62</td>
<td>503</td>
<td>915</td>
<td>6,029</td>
</tr>
</tbody>
</table>

### Issues with Social Security

Social security accounts for 3.54% of our Gross Domestic Product, or GDP (total economy of the US) and it is projected to increase to 6.1% in 2030. Right now there are more contributions than benefits being paid because there are currently 3.3 workers to every retiree. There is currently a trust of $1.7 trillion however the government is borrowing from the surplus for other spending. According to the 2006 OASDI Trustees Report, in 2017 the social security administration will pay more benefits than contributions it receives. In 2040, there will be 2.5 workers for every retiree and social security will be only able to pay 74 cents of every dollar of benefits are currently stipulated. As a worker, it is important to save for your own retirement because for most younger folks, social security will not take care of all your needs.

### Withholding

Withholding means that a certain amount of money will be deducted from each paycheck to be sent to the government. Employers will ask you to fill out a W-4 form which tells them how much money you want to
withhold in taxes. You do this by noting the number of exemptions you want to declare. Exemptions relate to the number of dependents you have and other deductions you might take. The trick is to withhold the right amount. If you withhold too much, you will lose the use of the money until you file your tax return and get a refund. If you withhold too little, you can face penalties if you underpaid by at least $1000 or more and 10% of your taxes due. Check out the IRS withholding calculator if you want to determine how many exemptions to declare: http://www.irs.gov/individuals/article/0,,id=96196,00.html.

Question

Reading a Social Security Statement
Download “Your Social Security Statement” from http://ssa.gov/mystatement/07sample1.htm

Only individuals pay social security tax (T/F)
What is the maximum salary taxed?
What part of the statement should be checked every year?
You can’t retire before age 65 (T/F)
How much will this individual get if she retires at age 67?
This is an accurate amount that she can depend on. (T/F)

Answer 1

Only individuals pay social security tax (F Employers pay, too.)
What is the maximum salary taxed? $97,500 as of 2007
What part of the statement should be checked every year? Your taxed social security earnings – make sure it is the same as what you show in payroll records.
You can’t retire before age 65 (F But you will get less benefits. It’s best to work until you get the maximum)
How much will this individual get if she retires at age 67? $1412.
This is an accurate amount that she can depend on. (F It is an estimate.)

Question

It is best to withhold:
   a) Much more than the taxes you pay for the year
   b) Much less than the taxes you pay for the year

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c) An estimate of the taxes you will pay for the year
d) Nothing at all

Answer

It is best to withhold:
   a) Much more than the taxes you pay for the year
   b) Much less than the taxes you pay for the year
   c) An estimate of the taxes you will pay for the year
   d) Nothing at all

Question

Please classify what the employee pays, what the employer pays and what both pay:

<table>
<thead>
<tr>
<th>Payable Account</th>
<th>Employee Pays</th>
<th>Employer Pays</th>
<th>Both Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Social Security</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Worker’s Compensation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Medicare</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Answer

Please classify what the employee pays, what the employer pays and what both pay:

<table>
<thead>
<tr>
<th>Payable Account</th>
<th>Employee Pays</th>
<th>Employer Pays</th>
<th>Both Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment</td>
<td></td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>Social Security</td>
<td></td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>Worker’s Compensation</td>
<td></td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>Medicare</td>
<td></td>
<td></td>
<td>X</td>
</tr>
</tbody>
</table>

Employee Benefits Overview

Employee benefits are usually provided by a partnership between the individual, the employer and the government. Individuals need the security provided by benefits to be productive while employers want to attract and retain employees with their benefits. The US has a national policy of providing a safety net for its citizens with benefits such as social security and Medicare. At the same time, it supports employer-provided benefits by providing tax benefits to companies that offer employee benefits. This is a safety net and will only provide about 35% of your income in retirement. According to the 2006 OASDI Trustees Report, in 2017, the social security administration will pay more benefits than contributions it receives. There is speculation that there will have to be large tax increases in the future to support the social security system if it is to continue. It is important to take this into consideration when planning for your future retirement needs and not depend on social security as your primary source of retirement. It is critical that you plan on how to manage your own retirement beyond your social security benefits.

Larger companies tend to offer employees more benefits. White collar jobs have more benefits. Unionized workers tend to have more benefits. Here is a comprehensive listing of employee benefits. The more common ones will be described in detail later in the text.
<table>
<thead>
<tr>
<th>Benefit Type</th>
<th>Description</th>
<th>Percentage of Workers Covered</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Common Employee Benefits</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Retirement</td>
<td>Defined Benefit – Traditional pension plan based on number of years of service and salary.</td>
<td>21%</td>
</tr>
<tr>
<td></td>
<td>Defined Contribution – Benefit will be based on what worker and employer contribute and investment returns.</td>
<td>54%</td>
</tr>
<tr>
<td>Health</td>
<td>Medical care – Coverage of medical expenses.</td>
<td>71%</td>
</tr>
<tr>
<td></td>
<td>Dental care – Coverage of dental cleanings and fillings.</td>
<td>46%</td>
</tr>
<tr>
<td></td>
<td>Vision care – Coverage of eye exams and eye glasses.</td>
<td>29%</td>
</tr>
<tr>
<td></td>
<td>Prescription Drugs – Outpatient prescription drugs.</td>
<td>67%</td>
</tr>
<tr>
<td>Life</td>
<td>Life Insurance – Employer may provide group life insurance for a multiple times salary. The typical one is two times salary. Often employees can pay for additional coverage.</td>
<td>52%</td>
</tr>
<tr>
<td>Disability</td>
<td>Short-term disability such as sick leave for a few weeks.</td>
<td>39%</td>
</tr>
<tr>
<td></td>
<td>Long-term disability replacement of a percent of income in the event of long-term incapacitation.</td>
<td>30%</td>
</tr>
<tr>
<td>Leave</td>
<td>Paid holidays – Days off for holidays such as Thanksgiving or Christmas. Most commonly there are 9 paid holidays per year.</td>
<td>76%</td>
</tr>
<tr>
<td></td>
<td>Paid sick leave – paid leave in case of illness. Most full-time employees are allowed sick days or paid days when sick.</td>
<td>57%</td>
</tr>
<tr>
<td></td>
<td>Paid vacation – paid vacation leave earned based on years of service. On average, employees are given 8.9 days after the first year.</td>
<td>77%</td>
</tr>
<tr>
<td></td>
<td>Paid personal leave – usually two days which may be used at the discretion of the employee.</td>
<td>37%</td>
</tr>
<tr>
<td></td>
<td>Paid funeral leave – time (usually a few hours) off to attend funeral. (Paid bereavement leave for a family members is normally a few days)</td>
<td>68%</td>
</tr>
<tr>
<td></td>
<td>Paid jury duty – time off for jury duty.</td>
<td>70%</td>
</tr>
<tr>
<td></td>
<td>Paid military leave – up to 15 days for military duty.</td>
<td>48%</td>
</tr>
</tbody>
</table>
### Paid family leave
- Time off for the birth and care of a child and other family matters.  
  - **8%**

### Unpaid family leave
- The law allows for unpaid time off for birth of a child.  
  - **82%**

### Other Benefits

<table>
<thead>
<tr>
<th>Benefit</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Childcare – Some large companies have day care centers on site which may or may not require employee contributions. More commonly, employers will have dependent care spending accounts that allow employees to pay for this with pretax dollars.</td>
<td>15%</td>
</tr>
<tr>
<td>Adoption – Some large companies assist in the adoption of a child.</td>
<td>10%</td>
</tr>
<tr>
<td>Long-term care insurance – Some employers will make long-term care insurance available to its workers at group rates.</td>
<td>12%</td>
</tr>
<tr>
<td>Flexible workplace – This includes telecommuting (working from home) and flexible days. For example working 80 hours over 9 days versus 10.</td>
<td>4%</td>
</tr>
<tr>
<td>Employer provided computer – Some employers provide a computer so the employee can work at home.</td>
<td>2%</td>
</tr>
<tr>
<td>Subsidized commuting – Van pools or public transit subsidies may be given by employers.</td>
<td>5%</td>
</tr>
<tr>
<td>Health savings account – An account where you can make contributions to pay for health care costs if you have a health plan with a high deductible.</td>
<td>6%</td>
</tr>
<tr>
<td>Flexible benefits – Cafeteria-style benefits allow employees to choose from a menu of benefits with benefit dollars or credits.</td>
<td>17%</td>
</tr>
<tr>
<td>Dependent care accounts – Using pretax dollars to pay for child or other dependent care.</td>
<td>30%</td>
</tr>
<tr>
<td>Healthcare reimbursement accounts – Using pretax dollars to pay for unreimbursed medical expenses</td>
<td>32%</td>
</tr>
<tr>
<td>Cash or deferred (compensation) without employer contributions – Some employers allow employees to defer compensation to a future date when the employee’s tax rate may be lower.</td>
<td>16%</td>
</tr>
<tr>
<td>Job-related travel insurance – Insurance for accidents while traveling on company business.</td>
<td>22%</td>
</tr>
<tr>
<td>Education assistance – Tuition reimbursement for employees to improve skills. Some companies allow education of any kind.</td>
<td>49%</td>
</tr>
</tbody>
</table>
Wellness programs – Some companies may pay for programs that promote wellness such as weight loss, etc.. 23%

Fitness centers – Companies may have an onsite fitness center. 13%

Employee assistance programs – These programs provide counseling for alcohol or drug dependencies. Counseling on a variety of topics such as stress or depression, relationships, financial or legal problems, elder care, grief, and job-related problems and co-worker conflicts may also be covered. 40%

Nonproduction bonuses – Bonuses that are not based on performance. 46%

Stock options – The ability to buy stock at a set price. (This can be an E.S.O.P, Employee Stock Option Program) 8%

Source: National Compensation Survey, Department of Labor, 2006 (Parenthetical notes added by the author.)

Summary of Employee Benefits Overview

1. The most common employee benefits fall into three categories:
   • retirement,
   • healthcare
   • holidays and other paid time off
2. Employers may provide other benefits related to life or disability insurance, childcare.

Question

What are the most common employee benefits?

Answer

What are the most common employee benefits?

The most common employee benefits fall into three categories:
   • Retirement benefits provide income security when the employee when they no longer work.
   • Healthcare benefits cover for doctor, hospital or prescription drug expenses.
   • Leave or days off with pay give the employee a rest period.

Activity - Employee Benefits

Compare benefits for major employers in Washington state.
Form students into teams of 3. They may choose local companies and research the benefits provided. Each group will present their summary to the class. As a class answer the following questions. What are the differences? Which employer would you prefer?

http://www.starbucks.com/customer/faq_qanda.asp?name=jobs
http://members.microsoft.com/careers/mslife/benefits/plan.mspx
http://www.seattle.gov/personnel/employment/benefits.asp
http://www.wamu.com/about/jobs/whyworkatwamu/benefits.asp

Activity – What is the future of social security?

What is the future of social security and its impact on me? Do research on what experts predict will happen to social security. Post it to the discussion forum.

Share your employee benefits. Tell your classmates what benefits you have with your current employer. Which ones do you want? Which are your most valuable?

Activity - Paycheck

Have students look at their paychecks and describe what kinds of deductions are listed. If the student privacy prevents a review of their personal information, use “Biweekly Paycheck for Annual Salary of $30,643” presented in text.

Activity – W-4

Have students fill out W-4 forms for withholding.

Activity – Employee benefits

Have students list all the employee benefits they have. Then have them contact their employee benefits offices to get a listing. How many were missing? Which benefits would they like that they do not have.

Activity - Review your social security report

- Review Unit 1, “Retirement” section in the book and Unit 6, “Social Security”.
- Visit this website to obtain a copy of your Social Security Earnings statement: http://ssa.gov/mystatement/
- Your objective is to:
  o Obtain a copy of your Social Security Earnings statement;
  o Review your Social Security Earnings statement for accuracy;
  o Start the process to correct inaccuracies on your Social Security Earnings statement.
  o Estimate Social Security Contributions to your retirement.
- Your instructor must confirm you have completed your objective, but for privacy reasons will not request a copy of your Social Security Earnings statement.
- This statement is found on your Social Security Earnings statement:
  o “Your estimated benefits are based on current law. Congress has made changes to the law in the past and can do so at any time. The law governing benefit amounts may change because, by 2041, the payroll taxes collected will be enough to pay only about 75 percent of scheduled benefits.”
What does this statement tell you about the benefits you can expect to receive after 2041 if taxes are not increased to cover the expected shortfall?

Submit your response to your instructor.

Unit 2: Risk Management in Your 20s

Auto Insurance

Summary of Auto Insurance
1. Buy a car that is not expensive to insure.
2. Make a list of all the people in your household who have driver's licenses.
3. Make a list of all the coverage you want.
4. Pull your credit report to see and correct any errors.
5. Have a history of your auto claims and traffic violations.
6. Use internet quoting services to get an idea of how much your auto insurance will cost and keep it in a file.
7. Check rating services such as Consumer Reports and JD Powers. Ask a reputable auto body repair shop which insurance company is the best. Check the Washington state Insurance Commissioner for complaints. Check for financial stability at AM Best or Standard and Poor's.
8. Call the agent or broker for the insurance company you want to check out.
9. Get the quote in writing.
10. Compare all quotes and choose the best for you.
11. Always drive safely, abstain from alcohol when driving, wear your seat belt, and make sure that everyone in your household does this same.

Why auto insurance?

Why do people have to have auto insurance? In 2006, there were 5.93 million crashes in the US. Of these 39,182 involved fatalities, 1.7 million involved injury and 4.18 million involved property damage only. In 2005, the insurance industry incurred $114 billion in losses from auto crashes.

<table>
<thead>
<tr>
<th>Year</th>
<th>Fatal</th>
<th>Injury</th>
<th>Property damage only</th>
<th>Total crashes</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td>37,324</td>
<td>2,149,000</td>
<td>4,438,000</td>
<td>6,624,324</td>
</tr>
<tr>
<td>1998</td>
<td>37,107</td>
<td>2,029,000</td>
<td>4,269,000</td>
<td>6,335,107</td>
</tr>
<tr>
<td>1999</td>
<td>37,140</td>
<td>2,054,000</td>
<td>4,188,000</td>
<td>6,279,140</td>
</tr>
<tr>
<td>2000</td>
<td>37,526</td>
<td>2,070,000</td>
<td>4,286,000</td>
<td>6,393,526</td>
</tr>
<tr>
<td>2001</td>
<td>37,862</td>
<td>2,003,000</td>
<td>4,282,000</td>
<td>6,322,862</td>
</tr>
<tr>
<td>2002</td>
<td>38,491</td>
<td>1,929,000</td>
<td>4,348,000</td>
<td>6,315,491</td>
</tr>
<tr>
<td>2003</td>
<td>38,477</td>
<td>1,925,000</td>
<td>4,365,000</td>
<td>6,328,477</td>
</tr>
<tr>
<td>2004</td>
<td>38,444</td>
<td>1,862,000</td>
<td>4,281,000</td>
<td>6,181,444</td>
</tr>
<tr>
<td>2005</td>
<td>39,189</td>
<td>1,816,000</td>
<td>4,304,000</td>
<td>6,159,189</td>
</tr>
<tr>
<td>2006</td>
<td>39,182</td>
<td>1,710,000</td>
<td>4,181,000</td>
<td>5,930,182</td>
</tr>
</tbody>
</table>


Involvement in accidents occurs disproportionately among younger drivers. In particular, new drivers aged 16 have a very high incidence of crashes as can be seen by the table below. Inexperience with driving, lack of seat belts, and alcohol were factors in more accidents in this age group.
<table>
<thead>
<tr>
<th>Age group</th>
<th>Number of drivers</th>
<th>Percent of total</th>
<th>Drivers in fatal accidents</th>
<th>Percent of total</th>
<th>Drivers in all accidents</th>
<th>Percent of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under 20</td>
<td>9,396,000</td>
<td>4.70%</td>
<td>6,300</td>
<td>10.10%</td>
<td>2,490,000</td>
<td>13.50%</td>
</tr>
<tr>
<td>20–24</td>
<td>16,886,000</td>
<td>8.4</td>
<td>8,900</td>
<td>14.3</td>
<td>2,640,000</td>
<td>14.3</td>
</tr>
<tr>
<td>25–34</td>
<td>36,003,000</td>
<td>17.9</td>
<td>11,300</td>
<td>18.1</td>
<td>3,820,000</td>
<td>20.8</td>
</tr>
<tr>
<td>35–44</td>
<td>40,394,000</td>
<td>20</td>
<td>10,400</td>
<td>16.7</td>
<td>3,420,000</td>
<td>18.6</td>
</tr>
<tr>
<td>45–54</td>
<td>39,851,000</td>
<td>19.8</td>
<td>9,600</td>
<td>15.4</td>
<td>3,060,000</td>
<td>16.6</td>
</tr>
<tr>
<td>55–64</td>
<td>29,685,000</td>
<td>14.7</td>
<td>6,600</td>
<td>10.6</td>
<td>1,610,000</td>
<td>8.8</td>
</tr>
<tr>
<td>65–74</td>
<td>16,492,000</td>
<td>8.2</td>
<td>4,200</td>
<td>6.7</td>
<td>800,000</td>
<td>4.3</td>
</tr>
<tr>
<td>Over 74</td>
<td>12,793,000</td>
<td>6.4</td>
<td>5,000</td>
<td>8</td>
<td>560,000</td>
<td>3</td>
</tr>
<tr>
<td>Total</td>
<td>201,500,000</td>
<td>100</td>
<td>62,300</td>
<td>100</td>
<td>18,400,000</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: National Safety Council

There were 42,642 teenagers killed in auto crashes and 2.6 million injured. Blood alcohol levels were over the limit of .08 in 15,124 of the fatalities. Much evidence suggests that the younger the person, the more unable they are to make sound judgments about driving. Auto accidents tend to happen to male teenagers, at night, and when they are with other teenagers. As noted before, alcohol is often involved as is the lack of seat belt use.

All this shows that auto insurance is very necessary. It protects you if you have an accident or if your car is otherwise damaged. For example, if you have an accident, the insurance company will get an estimate of what it will cost to get the damage fixed, and you will be reimbursed a certain amount which may not cover the entire cost of the repair. Coverage is a term that defines when you will be reimbursed and at what amount.

There are many different types of coverage available to meet your auto insurance needs. They are applied after you have met your deductible. Some are required and some are optional. Here are brief descriptions of the kinds of coverage that is available:

There are three kinds of liability coverage:

1. **Bodily injury.** This covers damage you have done to someone else involved in an accident for medical expenses, lost wages and pain and suffering from the accident. There are limits per person and for the accident in your policy.

2. **Property damage.** Damage to another’s property caused by you or by someone who is driving your car with your permission is the second kind of liability covered by auto insurance.

3. **Uninsured/underinsured motorist.** This coverage protects you if you are involved in an accident with a person who is not insured. It takes the place of the insurance that the driver should have purchase. It can cover bodily injury and property damage. A claim that involves an uninsured motorist does not have the same deductible as a collision/comprehensive claim. Currently Washington state has a limit of $250 as the deductible when the damage was responsible to an uninsured motorist (that can be identified).

Washington state law requires anyone driving a motor vehicle in the state to have an insurance policy, a certificate of deposit, or a liability bond. Under the law, you're required to have a liability policy with limits of at least 25/50/10. This means that your insurance coverage must be $25,000 for injury to another person, $50,000 for injuries to all other persons, and $10,000 for damage to another's property. You must
carry the same limits if you choose to buy a bond instead of an insurance policy. If you use a certificate of deposit, you must deposit $60,000 in cash or securities with the Office of the State Treasurer. How much liability coverage you will need beyond the minimum state requirements depends on the value of your assets. General guidelines are 50/100/25 but check with your agent or broker as to what is appropriate for you.

**Understand Your Auto Insurance Coverage**

**Personal injury protection (PIP):** PIP covers reasonable and necessary medical expenses for injuries sustained in an automobile accident, up to three years from the date of the accident and up to $10,000. PIP also offers income replacement coverage limited to a maximum of $200 per week for one year, after a person has been disabled for 14 days after the accident. Funeral expenses of $2,000 and loss of services (payment to others for work you can't do) of up to $5,000 are also included in the coverage. Payments are made for costs that are actually incurred by the injured person. If you have adequate health and disability income coverage from other sources, you may not need this.

**Collision coverage:** This covers damage to your car that is caused by a collision or your car hitting something else. According to the Highway Loss Data Institute, the average collision claim for a car was $3912. The average for a pickup was $4299. The average for a SUV was $3821.

**Comprehensive coverage** (other than collision): This covers damage to your car that is not caused by collision. For example, if a tree falls on your car or someone breaks into the car and damages it. Insurers paid $2 billion in losses due to vehicle theft in 2006 with a $6057 average loss for the US.

If you don't think you could afford to fix your car yourself if it was involved in an accident, you may want to carry collision and comprehensive coverage. These overages protect owners of expensive and late-model autos against the cost of repairs. Though coverage may increase your rates, you may want to think about it if the difference in what you pay would exceed your ability to pay the repair bills. Your lender may require these overages until you've paid off your car. You are always responsible for your deductible before the insurance company will pay any money on the claim. If you have a cash reserve that would allow you to absorb the costs of repairs to your vehicle, you might consider increasing your deductible to that amount.

**Other coverage could include:**

- Medical payments: This covers medical and funeral expenses for you up to about $5000.
- Emergency road service: This covers towing when your car breaks down.
- Car rental expense: If you have a claim that is covered under your auto policy, this coverage pays to rent a car. Be sure to check your policy for any limitations.
- Death, dismemberment and loss of sight: This pays for death and certain injuries to people named in your policy due to an auto accident.
- GAP coverage: In the event your vehicle is a total loss, this pays the difference between the current market value of your auto and the amount you still owe the lender.
- Custom equipment coverage: This covers direct and accidental loss to custom furnishings or equipment.

An endorsement is additional coverage for other items or events. If the item is not specifically covered in your policy, you need an endorsement to cover it. Many companies also offer endorsements for trailer/campers, snowmobiles, and auto loan or lease coverage.
If you're stopped by a law enforcement officer, you must present an insurance identification card. This card is given by your insurance company when they issue or renew your auto policy. The card must include the name of the insurance company, the policy number, and the policy's effective and expiration dates. It must also include a description of the insured vehicle and the name of the insured driver. If you do not carry proof of insurance, you could be fined $450 and it may go on your driving record. The courts could add other fees to your fines, such as a public safety and education assessment, which is 70 percent of all fines. Even out-of-state drivers who drive in Washington must comply with Washington's Mandatory Auto Insurance Law.

Some vehicles such as collector vehicles, motorcycles, or publicly-owned vehicles are exempt. Check the Insurance Commissioner’s website for the exact list. Regardless of this exemption, all drivers are subject to the state's Financial Responsibility Law. This law requires the person who is responsible for the damage or injury to pay the loss. Even though this is the current Washington law, an estimated 25% of the current drivers do not have auto insurance.

**Cost of Auto Insurance**

Many insurers offer auto insurance in Washington state. Under state law, insurers may consider your age, driving record, where you live, credit history, and other factors to decide if they will offer you coverage. Not every insurer will offer you coverage. If an agent or broker is unable to find coverage for you, you need to try some other brokers and agents.

There are three segments of the auto insurance market:

1. **Preferred market** -- This market refers to low-risk drivers with exceptional driving records. These folks enjoy the lowest premiums.

2. **Standard market** -- This market refers to the average driver who uses family-type cars and has a reasonably good driving record. Insurance premiums are higher.

3. **Non-standard market** -- Some drivers have a hard time obtaining insurance. This can result from a poor driving record, type of vehicle, claims history, experience, etc. There are insurance companies that write non-standard policies if your driving record prevents you from obtaining standard policies. The Washington State Legislature created this plan to provide auto insurance coverage to high-risk drivers who are unable to find coverage. To qualify for this special coverage, you must be a Washington state resident or a member of the U.S. military, hold a valid Washington state driver's license, and not have any debt from previous auto insurance coverage. This group has the highest insurance premiums.

Insurance companies must submit rates to the state Insurance Commissioner for approval. If they can prove that a certain type of driver results in higher risk for them, then the Insurance Commissioner will approve the rate. Insurance companies can rate or determine the appropriate premium for all licensed drivers in the household -- the policyholder and his or her spouse, and other household members including roommates, whether or not they are related by blood. If a driver is part of your household and they are not listed on the policy, more than likely they will not be insured in the case of an accident.

The premium you pay consists of a "base rate" calculated with factors such as your age, sex, marital status, driving pattern, claims history, location, credit history, and the make, model and year of your vehicle. Insurance companies will gather data over a period of time and determine based on statistical analysis which groups are higher risk. Higher risk groups will pay higher premiums. In 2004 Washington drivers paid on average $532.96 for liability, $273.98 for collision, and $136.50 for comprehensive for a total of $838.61. Washington state ranked 19th in the US for cost.
The factors in the following table may determine how much you will pay for auto insurance:

<table>
<thead>
<tr>
<th>Characteristic</th>
<th>How it affects your premium</th>
</tr>
</thead>
<tbody>
<tr>
<td>Age</td>
<td>Drivers under age 25 are involved in more accidents than adults between age 25 and 65 so they are higher risk. Families with younger drivers in the household may pay more for their insurance. Statistics also show that senior citizens are also a higher-than-average risk to insurance companies.</td>
</tr>
<tr>
<td>Sex</td>
<td>Insurance companies can discriminate on the basis of sex if that discrimination is based on statistical evidence. For example, young men under age 25 are involved in more accidents and typically pay higher insurance rates.</td>
</tr>
<tr>
<td>Marital Status</td>
<td>Married couples have fewer accidents than singles and generally pay lower rates.</td>
</tr>
<tr>
<td>Vehicle</td>
<td>The more expensive your vehicle, the more you will pay for insurance. Sports cars and high-performance cars are involved in more accidents, cost more to repair, and are stolen more often, so they cost more to insure.</td>
</tr>
<tr>
<td>Location</td>
<td>If you live in an area with higher than average crime rate, the base rate for comprehensive coverage will be higher. If a lower than average number of accidents happen in the base rate for liability and collision coverage may decrease.</td>
</tr>
<tr>
<td>Driving Record</td>
<td>The number of miles you drive per year can increase your rate.</td>
</tr>
<tr>
<td>Credit History</td>
<td>Washington state has one of the toughest laws restricting how insurance companies use credit history. But your insurer still may use information in your credit history to determine your insurance score and that may raise or lower your premium.</td>
</tr>
</tbody>
</table>

**Buying Auto Insurance**

You can buy your auto insurance from an agent, direct writer, broker or over the internet. These sellers must be licensed in the state of Washington so it’s good to check before you buy.

**Agents**

Many individuals and businesses buy their insurance coverage from agents, who represent either specific companies or a number of companies. The agent’s job, which is commission based, is to sell you the policies of the company he or she represents.

**Direct Writers**

A direct writer is an insurance company that sells its policies through salaried employees who are licensed agents and represent that company exclusively. Direct writers offer you the convenience of a single phone call or 24-hour, toll free service. The company does not usually pay a commission to agents.

**Brokers**

Brokers represent and work for you, but they also work for the insurance companies that pay them. Typically, you tell the broker the type of coverage you want and the amount you want to spend. Brokers survey the market and bring back options for you to review. Many businesses prefer to use brokers because they want an independent person who may be able to sample a broader range of coverage available, and put together the best package for specific business and coverage circumstances. Brokers also receive a commission on their sales.
Check with your friends, neighbors, co-workers, and family. Speak to people who have had a difficult time with claims or coverage. Check to see if any complaints against your insurance company have been filed with the Office of the Insurance Commissioner (http://www.insurance.wa.gov/oic/contact.asp).

The cheapest insurance is not always the best. You always have to balance the coverage you get against the cost of the premium.

<table>
<thead>
<tr>
<th></th>
<th>Company Name:</th>
<th>Company Name:</th>
<th>Company Name:</th>
</tr>
</thead>
<tbody>
<tr>
<td>List all people to be insured and all people in your household:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Liability coverage required. Required 25/50/20. Typical is 50/100/25.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Personal Injury Protection (May not be necessary if you have other coverage.)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Uninsured motorist bodily injury coverage (per person and per accident)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Uninsured motorist property damage coverage</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deductible</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Collision coverage</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Comprehensive coverage</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other coverage: Emergency Road Service Rental Reimbursement Medical payments</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Discounts Anti-Lock Brakes Air bags Car alarm Professional group Low risk occupation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Claims record</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Complaint record</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Check on insurance costs before you buy a car: The type of car you own will affect how much you pay for insurance. Before you purchase a car, check with your agent or ask your company how much it will cost to insure the model you want to buy. To create a short list of insurance companies to research, ask reputable mechanics or body repair shops which insurance companies services claims the best.

Research the insurance company thoroughly. Make sure that it is financially stable by checking its AM Best (www.ambest.com) and Standard and Poor’s (www.standardandpoors.com) ratings. These also can be obtained at your local library. Find out how it fares on processing claims for its customers. Consumer Reports (also available at your local library) publishes information on that. Check other rating services such as JD Powers Ratings http://www.jdpower.com/finance/ratings/auto_insurance/index.asp

Research thoroughly. Make sure that it is financially stable by checking its AM Best (www.ambest.com) and Standard and Poor’s (www.standardandpoors.com) ratings. These also can be obtained at your local library. Find out how it fares on processing claims for its customers. Consumer Reports (also available at your local library) publishes information on that. Check other rating services such as JD Powers Ratings http://www.jdpower.com/finance/ratings/auto_insurance/index.asp


The amount of the deductible you select will affect your premium. For example, you may save money by raising your collision and comprehensive deductibles from $200 to $500, or even to $1000. Remember you are responsible for all of your deductible.

When traveling, many people rent cars. You will be offered optional rental car insurance at the time of the rental. If you have automobile insurance you may not need the optional rental car insurance. However, if your car is broken into, or stolen, you will have to file a claim against your normal automobile insurance policy. Some premium credit cards offer “free rental car insurance” if you rent a car and charge the rental to that credit card. If you have a claim, the credit card will cover the claim up to the deductible that you have on your automobile insurance.

Ask your agent or company if they offer any special discounts. These include discounts for features such as anti-lock brakes, air bags, and car alarms. They may also offer discounts if you are in a low risk occupation or belong to a professional group. Some companies might offer a discount for successful completion of a defensive driving course. Young drivers, who are good students or who have finished a driver’s education course, may qualify for a discount. Also, many companies will give you a discount on your auto premiums if you also insure your house through the same company.

Follow safe behavior to reduce the possibility of an accident. Take special precautions with teenagers and cars. Have an anti-theft device that is both an alarm and that will shut off the fuel or otherwise disable the car. Consider installing a tracking device on your car. Always wear seat belts and don’t drink and drive.

The law requires insurance companies to give discounts to seniors who complete the “55-Alive” program. This program is offered in various Washington locations. Information on this program is available from the Washington Traffic Safety Commission, 100 S. Cherry Street, Olympia, WA 98504.

Question:

Define and give an example of the following auto insurance terms:
Liability insurance
Uninsured/underinsured motorist property damage
Collision
Comprehensive
Deductible
Personal injury protection
Uninsured/underinsured motorist bodily injury

Question
In Washington state, 25/50/10 liability insurance is required. Explain what this is.

Question
What does not affect the premium you pay on a car:
Model and make of car.
Theft-ability of car
Whether it has anti-lock brakes
Fuel efficiency
Question

True or False
Your credit report has no bearing on your premiums.
Low academic grades can result in higher premiums for students.
If you don’t pay your premiums on time, you will still have auto coverage.

Question

Match the following

| Collision                      | Medical expenses for injuries sustained in an automobile accident. |
| Comprehensive                 | Damage to your car due to someone breaking in.                     |
| Personal Injury Protection    | In an accident when the other driver doesn’t have insurance        |
| Uninsured/underinsured motorist | Damage to your car that is caused by your car hitting something else. |

Question

Will the following make your auto insurance premiums be higher or lower?
Married
Over 65
Under 25 and male
Low crime neighborhood
Drive less than average miles in a year
No traffic violations
Two previous accidents
High deductible for collision
Low deductible for comprehensive
Question

What information should you gather if you have an auto accident?

Credit Score and Auto Insurance

**Summary on Credit and Auto Insurance**

1. Ask your insurance agent or company if they use credit information, how they use it and whether it affects your premium.
2. Get a copy of your credit report from each of the three national credit bureaus and correct any errors.
3. Tell your insurance agent and company about any errors, and tell them your side of the story.
4. Improve your credit history if you have had past credit problems. Ask your agent or company for the primary reasons (factors) that your insurance credit score is low and work to improve those pieces of your credit history.
5. If you are paying higher premiums because of your credit history, ask your insurer to re-evaluate you when your credit improves.
6. Shop around for insurance. Insurance companies use credit information in different ways, so your rates can vary dramatically from company to company.

A credit score is a number that insurance companies assign consumers based on their credit history. Bill paying history, the number and type of accounts they have, late payments, collection actions, outstanding debt and the age of your accounts can affect your credit score. Both the federal and state Fair Credit Reporting Acts (FCRA), say that insurance companies may look at credit information without your permission for underwriting practices.

Some insurance companies believe there is a correlation between financial responsibility and insurance losses. They believe that credit information is a good measure of financial responsibility. They believe that consumers who show less financial responsibility will file more claims, so they should pay more for their insurance. Many consumer groups feel insurers should not use credit information to determine premiums or to decide who they will insure. Some consumer groups believe that the use of credit information may have a harmful impact on minority groups that result in those groups paying more for insurance.

**Your Credit Score**

![Credit Score Diagram]

Source: [www.fico.com](http://www.fico.com)

**Payment History**

Your payment history is the largest component of your credit score. In assessing your payment history, the credit company will look at account payment information on credit cards, retail accounts, installment loans, finance company accounts, mortgage, etc. They will look to see if you paid on time or how long you were delinquent in payments. They will look for adverse public records such as bankruptcy (up to 10 years).
years), judgments, suits, liens, wage attachments, collection items, and/or delinquency (up to 7 years on past due items). How long your payments were past due and how much you owed will figure into your payment history score. The number of past due items on file will be reviewed as will the number of accounts paid on time.

**Amounts Owed**
The credit rating company will look at the number of your accounts, the amount owing on each account, proportion of credit lines used (how much of the credit limit) and proportion of installment loans still owing (proportion of balance as compared to original loan). If you have a tendency to spend up to your credit limit then, that will count against you.

**Length of Credit History**
The length of time since accounts have been opened will be considered and the time of the account activity will be considered. Anyone who has had a long history of paying on time will have a better credit rating.

**New Credit**
Any number of recently opened accounts, and proportion of accounts that are recently opened, by type of account will factor into the new credit proportion of your credit score. Although there is legislation against this, the number of recent credit inquiries may affect your credit rating. Re-establishment of the positive credit history following past payment problems will also be examined.

**Types of Credit Used**
The number of various types of accounts (credit cards, retail accounts, installment loans, mortgage, and consumer finance accounts) will be examined.

**Maintaining Complete and Accurate Credit Records**
Mistakes on your credit record can hurt your financial future. Your credit rating is important, so be sure that credit-bureau records are complete and accurate. The Fair Credit Reporting Act says that you must be told what’s in your credit file and have any errors corrected.

The three credit scoring companies have set up a central website, a toll-free telephone number, and a mailing address through which you can order your free annual report. To order, click on annualcreditreport.com, call 1-877-322-8228, or complete the Annual Credit Report Request Form and mail it to: Annual Credit Report Request Service, P.O. Box 105281, Atlanta, GA 30348-5281. You may order your reports from each of the three nationwide consumer reporting companies at the same time or one at a time.

If an insurance company refuses you coverage because of unfavorable information in your credit report, you have a right to get the name and address of the agency that keeps your report and request a copy of the file. The law also says that the credit bureau must help you interpret the data in if you don’t understand it. If you’re questioning denial of credit made within the past 60 days, the credit rating service cannot charge a fee for giving you information.

If you notify the credit rating service about an error, generally it must investigate and resolve the dispute within 30 days of receiving your letter. The credit rating service will contact the creditor who supplied the data and remove any information that is incomplete or inaccurate from your credit file. If you disagree with the findings, you can file a short statement (100 words) in your record, giving your side of the story. Future reports to creditors must include this statement or a summary of it.

There is a limit on how long certain information may be kept in your file. Bankruptcies must not be reported after 10 years. However, information about any bankruptcies at any time may be reported if you
apply for life insurance with a face value over $150,000, for a job paying $75,000 or more, or for credit with a principal amount of $150,000 or more. Suits and judgments paid, tax liens, and most other kinds of unfavorable information must not be reported after 7 years. Your credit record may not be given to anyone who does not have a legitimate business need for it. Stores to which you are applying for credit may examine your record; curious neighbors may not. Prospective employers may examine your record with your permission which often is granted when you sign an application form with the employer.

If you write to your creditor about an error the creditor must not release information to other creditors or credit bureaus that would hurt your credit reputation. Until your complaint is answered, the creditor cannot collect the disputed amount. If the creditor disagrees with your error and you do not pay in the time allowed, you may be reported as delinquent and the creditor may take action to collect. You can still disagree in writing and the creditor must report that you have challenged your bill and give you the name and address of each person who has received information about your account. When the matter is settled, the creditor must report the outcome to each person who has received that information. Remember that you may tell your own side in your credit record with a 100-word explanation.

Your rights

Ask your insurance agent or company if they use credit information for underwriting and rating. If credit history is used for underwriting, ask how it affects your eligibility for coverage. If credit history is used for rating, ask how it affects your insurance premium. Finally, you should ask if the insurance company will check the credit history of other people insured on your policy, such as family members, and how they will affect your policy.

Here are some restrictions on how insurers can use your credit report:

- Insurers are restricted from increasing your rates if you don't have a credit history unless they have documented with the Insurance Commissioner that lack of credit history results in more risk.
- Insurance companies cannot use your credit history to cancel or non-renew your current insurance policy. They cannot deny you coverage based on absence of credit history, number of credit inquiries, purchase of a vehicle or house that increases the amount of debt you have, particular use type of credit or charge card, or total amount of available credit.
- If you are applying for new coverage, the insurance company cannot use just your credit score. It must also consider other substantive factors when deciding whether or not to offer your coverage.
- By law your insurance rates cannot be based on these number of credit inquiries, the initial purchase of a new vehicle or house that increases the amount of debt you have, particular use type of credit or charge card, or total amount of available credit, or total amount of available credit, or an absence of credit history unless they have documented that this causes more risk.

Washington state law requires specific notice in clear and concise language if an insurer takes one of the following actions based on credit history:

- Cancels, denies or non-renews coverage
- Gives more limited coverage
- Limits benefits, such as eligibility for dividends
- Does not offer the best rate available
- Adds a premium surcharge or does not offer a discount

Dealing with Credit Problems

Poor money management from compulsive shopping and buying things you can't afford can result in credit problems. In this case, working towards a good spending plan is the path to take.
These coping tips are adapted from Consumer Credit Counseling Services (CCCS), part of the National Foundation for Credit Counseling. For more go to www.nfcc.org.

Stay calm and work your way slowly and surely through the problem. By taking action you are already improving the situation as it is better to manage the problem now before it gets bigger. Don’t delay. Take action now and make it a priority.

Get a copy of your credit report. If you feel that an error caused your credit problem, tell the credit rating service what information you think is wrong (they must respond within 30 days). Provide copies (not originals) of documentation. Be diligent about monitoring your credit report.

Seek financial counseling right away. Use free counseling services that are listed in www.usdoj.gov/ust. It helps to have experienced and clear eyes looking at your problem. But be aware of credit counseling services (even though they claim to be nonprofit) that charge you fees.

Make a list of all the debts you owe with the creditor names and addresses. Call your lenders and creditors. Let them know you’re having financial difficulties. Some of them have different credit standards and you may still be able to get credit to bid you over.

Prepare a realistic spending plan to pay down your debt. Some folks pay the higher interest rate debts first. Others pay smaller debts first so they can feel a sense of accomplishment that will help them tackle the rest. You might even be able to restructure your debt. They would rather you pay something than nothing at all.

Pay bills. If you have savings, consider using it to pay as many bills as you can. Consider selling some assets. Consider getting a second job to pay off your debt.

It might take longer than you think for your financial crisis to go away. Be persistent with your creditors and payment plan. Establishing a good relationship will get you farther than running away from your obligations. As you start to pull yourself out of the financial crisis, remember to set aside money for savings. This will give you a safety net for financial crises in the future.

Only time, a concerted and persistent effort, and a personal debt repayment plan will improve your credit report. Reputable credit counseling organizations can advise you on managing your money and debts, help you develop a budget, and offer free educational materials and workshops. Their counselors are certified and trained in the areas of consumer credit, money and debt management, and budgeting. Counselors discuss your entire financial situation with you, and help you develop a personalized plan to solve your money problems. An initial counseling session typically lasts an hour, with an offer of follow-up sessions.

Making an Auto Claim

If you are involved in a car accident, put your car in a safe place and turn off the ignition. Check to see if the accident area is safe. Recruit a bystander to help if necessary. Warn oncoming traffic of the danger at the scene. Every driver involved in an accident is legally required to remain at the scene. He or she must also offer aid and give necessary information to others involved and to law enforcement officers.

Try to make the scene as safe as possible. Check for injuries but do not move the injured person. Call 911 and report any injuries. If there is any injury or death, or if property damage exceeds $700 in damage to property, you must notify the appropriate law enforcement. If you don’t complete a written report where required, it may result in the suspension of your driver’s license.
Keep a form in your car to fill out in case of accidents. Take down the following information:

**Accident Form**

<table>
<thead>
<tr>
<th>Model and make of other car</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Model year of other car</td>
<td></td>
</tr>
<tr>
<td>License plate number</td>
<td></td>
</tr>
<tr>
<td>Driver's name</td>
<td></td>
</tr>
<tr>
<td>Address</td>
<td></td>
</tr>
<tr>
<td>Driver's license number</td>
<td></td>
</tr>
<tr>
<td>Insurance company and policy number</td>
<td></td>
</tr>
<tr>
<td>(Look at insurance card)</td>
<td></td>
</tr>
<tr>
<td>Name of car’s owner if not driver</td>
<td></td>
</tr>
<tr>
<td>Names, addresses of other passengers and witnesses</td>
<td></td>
</tr>
<tr>
<td>Name and badge number of police</td>
<td></td>
</tr>
<tr>
<td>Name and badge number of emergency personnel</td>
<td></td>
</tr>
<tr>
<td>Ask for copy of police report</td>
<td></td>
</tr>
<tr>
<td>Time of day</td>
<td></td>
</tr>
<tr>
<td>Weather</td>
<td></td>
</tr>
<tr>
<td>Driving speed at the time of accident</td>
<td></td>
</tr>
<tr>
<td>Road hazards, signs, stop signals, etc.</td>
<td></td>
</tr>
<tr>
<td>Draw a picture of the scene and take pictures</td>
<td></td>
</tr>
</tbody>
</table>

Here is some other helpful advice:

- If you suspect that the other driver was under the influence of alcohol or drugs, ask that a breath test be performed on you and the other driver.
- Cooperate with the police, but do not admit responsibility for the accident in any way as it is difficult to ascertain exactly what happened in this type of situation. You will be required to show proof of insurance, but do not reveal how much coverage you have.
- Do not negotiate with the other driver. Do not accept money or agree to forget about it because it seems minor. By accepting money, you may give up your right to file a claim against the other driver. There may be hidden damages and injuries or the person may file a lawsuit against you.
- Report the accident to your insurance agent or company as soon as possible.
- Take the name and number of any witnesses to the accident, even if you don’t think you may need them.
- If you have a camera, take photos of the scenes and the vehicles.

Washington Administrative Code (WAC) states that an insurer (insurance company) shall complete its investigation within thirty days after notification of a claim, unless such investigation cannot reasonably be completed within that time. If they can't complete the investigation within 30 days they are required to keep you updated on the progress of their investigation.

A traffic citation is not a determination of legal liability. The company is obligated to investigate claims made according to WAC and their policy language. It is possible that there may be more than one person at fault and the liability could be shared. Washington State uses the theory of comparative negligence, in which parties to an accident can be found to share the fault. Each party's duty is to avoid an accident and
their failure to perform those duties must be considered. Simply being “in the wrong place at the wrong time” isn’t proof of negligence.

There is no definition of “full coverage” in the law, so there are often misunderstandings between policy holders and their insurance companies. Read the declarations page you get from you company at renewal time and see what coverages are listed that have a price beside them. Those are the coverages that you have. Towing, rental, and extended coverage for special stereo or other equipment are additional coverage’s you must request.

If the other party’s insurance is accepting liability, you are entitled to be compensated for the loss of use of your vehicle for a reasonable length of time while it is under repairs or not drivable. If your vehicle is considered a total loss, most companies will provide a reasonable amount for loss of use. If your company is handling the damages you must have rental coverage on your policy to obtain a rental car.

A property damage claim includes the cost to repair or replace the vehicle and compensation for loss of use of that vehicle. Insurance policies define this property damage as to amount they will pay on behalf of their insured. There is no doubt that any accident is an inconvenience for everyone involved, however, the insured person’s policy probably won’t compensate you for time or lost wages under a property damage claim. Currently there is no law or case law that addresses this issue. This matter is often settled through Small Claims Court.

You are free to choose the auto body shop you want the work to be done. If you choose to take your vehicle to a repair facility in which the overall cost for a satisfactory repair is higher than the insurer’s estimate, you may be liable for any additional amount above their estimate. The insurer must provide you with the names of reputable repair shops reasonably close to you that can satisfactorily complete the repairs for the amount of their estimate. The repair shop generally works with the adjuster to handle any "supplement" (additional costs) that occur due to hidden damage or parts price differences. If the company and the shop can't agree, it is the responsibility of the company to provide the name of a repair shop that will repair your vehicle for the amount of the estimate. The repair shop that the insurance company suggests must not be an unreasonable distance from where you live.

The insurer owes you repair or replacement with like kind and quality parts, but not necessarily new parts. If the parts and repairs are guaranteed by the repair shop, and are in the same condition as the parts damaged, they conform to the repair requirements. If you insist on certain parts you may have to pay the additional cost.

Insurance companies have different policies regarding payment procedures. Your company may have rules about whether it is necessary to repair your vehicle. It might pay to a lien holder or a body shop and the owner. If the other party’s insurance is paying they are required to pay either the registered owner or the lien holder, or both. A direct payment to the owner who doesn't repair the car right away may not allow for any other payments for undetected, additional damage.

If the vehicle is declared a total loss, the company owes you the actual cash value of a comparable vehicle in your local area. You can determine this amount by using dealer quotes and/or newspaper ads or other auto sales publications of vehicles comparable to yours in mileage, condition, options, etc. In addition they will pay you sales tax on the value of your vehicle, and pay the unused portion of your registration fees. You may have the option of keeping your car. If you do, the company will subtract the value of the salvage from the final settlement.
Insuring Your Property

Renters policy

When starting out, most people don't give much thought to insuring their property. After all, most people starting out don't own much. But, renter's insurance is a very important risk management tool to use. If you don't own much, you probably have very little money to replace the things that you need to live from day to day. Renter's insurance provides protection for personal possessions and personal liability when you rent an apartment or house. A 2006 Insurance Research Council poll found that 96% of homeowners have insurance while only 43% of renters have insurance. The average premium for renters in Washington state in 2004 was $177.

Renters insurance (also called tenant insurance) offers coverage similar to homeowner insurance for people who rent living space including an apartment, condominium, single-family home or multi-family home, such as a duplex. Renters insurance is normally a special "package" that combines coverage for:

- Personal liability (protection against claims someone else makes against you)
- Premises medical coverage (pays the medical expenses of others accidentally injured on the property you rent)
- Additional living expense (pays for your living expenses if the living space you rent is deemed unlivable)
- Personal property (contents) coverage. Be aware that standard renter policies only cover the actual cash value at the time of the loss.
- It does not cover the building, but it may cover any renter improvements (such as built-in book shelves or room partitions you add).

The following is a sample list of items in a renters’ policy that typically include a specific dollar limit: money, securities (such as stocks and bonds), watercraft, trailers, jewelry, silverware, gold-ware, pewter-ware and business property. Prepare a list of your personal property with their values and talk to your agent about items with specific limitations. The limits in your policy may be less than the value of your property, so you may want to buy a special rider or endorsement to cover it. You can also add coverage for volunteer activities that you engage in.

Renters insurance for college students

If you are a college student who rents an off-campus apartment or house while away at school, you should think about buying renters insurance. Landlords only buy insurance to cover their building and property. You need coverage to protect your personal property if it gets damaged, destroyed or stolen, such as your computer, television, stereo, bicycle or furniture. Even if you are a dependent under your parent’s insurance, your personal property, in many cases, is not covered if you live off campus. Your parents should check their policy or contact their insurance agent to see if their homeowner insurance will protect you while you are away at school.

Assignment – Auto insurance

Determine what coverage you want for auto insurance. List the amounts for each of the categories below. Identify three auto insurance companies. Research their financial ratings, claims rating, and complaints. Which company would you choose? Using the auto coverage above, go to the following sites and get a quote for auto insurance for yourself. Were the rates different?

www.esurance.com
www.geico.com
List all people to be insured and all people in your household:

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Liability coverage required. Required 25/50/20. Typical is 50/100/25.

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Personal Injury Protection (May not be necessary if you have other coverage.)

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Uninsured motorist bodily injury coverage (per person and per accident)

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Uninsured motorist property damage coverage

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Deductible

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Collision coverage

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Comprehensive coverage

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Other coverage: Emergency Road Service Rental Reimbursement Medical payments

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Discounts Anti-Lock Brakes Air bags Car alarm Professional group Low risk occupation

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Claims record

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Complaint record

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AM Best Rating Standard and Poor Rating

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Other Ratings

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Licensed to do business in Washington.

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Activity – Discussion about auto claims
Only to the extent that you are comfortable, share your experiences or those of people you know with auto claims. What was covered? What was not?

Activity – Calculate your credit score

Calculate your credit score.

Activity – How does your choice in cars impact your insurance costs?

Go through the exercise of buying a car. How does your choice of car impact your insurance costs?

**Unit 3: Risk Management in Your 20s to 30s**

**Healthcare Insurance**

**Healthcare Insurance Summary**
1. Write down all your current and anticipated health needs.
2. Use the Health Plan Evaluation Form to compare health plans offered to you.
3. Consider setting up a flexible spending account to cover expenses your health plan doesn’t reimburse.
4. Keep good records of all health care spending for reimbursement and filing taxes.
5. If you have a high deductible health plan, consider setting up a Health Savings Account.
6. Follow instructions and ask questions of your health care provider.
7. Stay healthy by establishing good eating, exercise and other wellness habits.

Healthcare benefits are meant to protect workers from financial loss that may result from serious illness or injury. Benefits include medical, dental, prescription drugs, and vision coverage. Companies find that promoting health leads to increased productivity because workers aren’t preoccupied with health issues and have fewer sick days. Companies also believe that this is a good way to recruit workers.

Who is covered? About 101.5 millions workers covered by employment-based health benefits. Of these workers, 76% are covered through own employer and 24% are covered through a family member. There are also 14.9 million nonworking adults and 42.9 million children covered under these plans.

Larger companies tend to offer healthcare. In 2005, 100% of employers with 200 or more employees offered health benefits. 61% of employers with 3 to 199 workers offer health benefits.
Medical care for a “typical” insured family of four in the U.S. cost about $13,382 in 2006, a 9.6% increase from 2005, according to the second annual Milliman Medical Index. The study estimates that in any given year, a typical family of four will be responsible for about 38% of their total annual medical costs, including $2,210 in out-of-pocket spending and $2,810 in payroll deductions. Employers will cover 62%, or $8,362, of the total costs.

If you have a job with a medium-sized or large employer, your employer will provide your medical coverage through a group insurance plan for their employees. If you don’t have access to a group insurance plan, you will need to find individual health insurance coverage. The Office of the Insurance Commissioner has a list of insurers.

Most people buying individual health insurance in Washington state will need to complete a standardized health screen questionnaire. This questionnaire identifies your eligibility through the Washington State Health Insurance Pool (WSHIP). Premiums for WSHIP coverage are higher than commercial health plans. However, WSHIP offers some high deductible plan options with lower premiums. For more information, contact WSHIP directly at 1-800-877-5187 or visit their Web site at www.wship.org.

Insurance plans will screen for pre-existing conditions or medical conditions in which you received advice or treatment during the previous six months. They may require a waiting period or a period of time before you can seek treatment for these pre-existing conditions. Individual plans may require a nine-month waiting period. If your prior plan is equal or better than the new plan, the insurance company must credit your enrollment time in that plan toward the waiting period for the pre-existing condition. For example, if you had nine months of coverage under your prior plan, the insurance company would waive your waiting period. If you had four months coverage, you would have to wait five months for the new insurance to cover a pre-existing condition. Insurers may not impose a pre-existing condition waiting period on your coverage if you have 18 months of creditable coverage; and qualify as an “eligible individual” under federal law.

Certain applicants are not required to fill out the health screen questionnaire when applying for individual insurance. They include applicants who will exhaust their COBRA coverage, have 24 months of continuous coverage through an employer with 20 or less employees, have moved out of their existing...
plans’ service area within Washington state, continue to receive care from a primary care doctor who left their existing plan, have received a notice regarding the discontinuation of their conversion plan (a limited benefit policy that an individual may have a right to convert to after their group insurance ends).

**Low cost or free options**

Before you buy health insurance in the individual market, consider your eligibility for less expensive options. Some options include:

- Basic Health Plan – administered by the Washington State Health Care Authority
- Indian Health Services or a tribal health clinic Community Health Centers (federally funded) – offers health care on a sliding fee scale
- Breast and Cervical Health Program – available through your local health department Children’s Health Insurance Plan (CHIP)
- Veterans Administration Medicaid and Healthy Options plans – administered by the Washington State Department of Social and Health Services

For more information, contact the Insurance Consumer Hotline at 1-800-562-6900.

**Health Plan Structure**

Health plans are usually described as either fee-for-service (also called indemnity) or managed care. There is a basic premium, which is split between you or your employer, and paid monthly, to buy the health coverage. In addition, there are often other payments you must make including deductibles, coinsurance and co-pay. These will vary by plan. In considering any plan, you should try to figure out its total cost to you and your family, especially if someone in the family has a chronic or serious health condition.

Most plans cover: medical expenses for hospital and doctor fees, surgical expenses, anesthesia, x-rays, laboratory fees, emergency care, and maternity care. Some plans cover: physical exams, preventive care, health screenings, chemical dependency treatment, prescription drugs, dental, vision, mental health or psychiatric care, home health, nursing home and hospice care. Identify your health care needs and ask your health plan whether they provide coverage.

All plans limit payment for any given treatment and require employees to share in the cost. A deductible (typically $100 to $500) requires employee to cover the first dollars used in a year. For example, if it is January and you have a deductible of $100, and you just had a doctor visit for $120. Your medical coverage would only reimburse $20. The deductible was applied to the expense. Some younger, healthier employees who don’t have many health needs, choose a higher deductible to reduce premiums and fund a Health Saving Account for their medical needs.

Coinsurance (typically 20%) is another way companies require employees to pay a portion of expenses. If coinsurance is 20% and your medical expense is $100, you would have to pay $20 and your medical coverage would pay $80. Some plans have the employee pay fixed fee per visit, for example $10 every time you make a visit to the clinic.

Out-of-pocket limit (usually $3000 - $3300) is the maximum amount of money you cover. Once employee has reached the out-of-pocket limit, the rest of expenses will be covered by the medical plan. For example, if your medical plan has $3000 out-of-pocket limit for the year and you have accumulated $3200 in deductibles and coinsurance, the $200 in excess of $3000 will be paid by the plan.

A lifetime limit (typically $1 million) is the maximum amount that the plan will cover for one employee. If the employee has a serious illness that runs up medical bills to $1,000,000, then the plan will no longer cover any expenses.
Most plans require that the treatment be medically necessary. For example, plastic surgery to look better will typically not be covered. There are restrictions on how much the plan will pay for certain kinds of care. The plan will also require pre-certification before hospitalization, that you will have to submit for the medical procedure for pre-approval.

A pre-existing condition is a health or physical condition that existed before you joined the plan. Prior to 1993, insurance coverage was denied or significantly delayed on the basis of pre-existing conditions. In Washington state, however, employers cannot use health screening to reject applications, and the only waiting periods allowed may be no more than nine months for a condition treated in the previous six months.

**Choices in Plans**

Indemnity plans pay their share of the costs of a service only after they receive a bill for you. Typically you choose your health care provider, you may pay the bill of the provider will send it to the indemnity plan and then you are reimbursed by your indemnity plan (if you paid the bill) or the indemnity plan pays the provider. Usually, you have a deductible—such as $200—to pay each year before the insurer starts paying. Once you meet the deductible, most indemnity plans pay a percentage of what they consider the "Usual, Customary and Reasonable" charge for covered services. The insurer generally pays 80 percent of the costs and you pay the other 20 percent, which is known as coinsurance. If the provider charges more than the Usual, Customary and Reasonable rates, you will have to pay both the coinsurance and the difference.

Managed care plans have agreements with certain doctors, hospitals, and health care providers to give services to plan members at reduced cost. In general, you will have less paperwork and lower out-of-pocket costs if you select a managed care type plan and a broader choice of health care providers if you select an indemnity-type plan.

There are basically three types of managed care plans: PPOs, HMOs, and POS plans.

**Preferred Provider Organization (PPO).** A PPO has arrangements with doctors, hospitals, and other providers of care who have agreed to accept lower fees from the insurer for their services. In addition to the PPO doctors making referrals, plan members can refer themselves to other doctors, including ones outside the plan.

If you go to a doctor within the PPO network, you will pay a copayment (a set amount—say $10 for a doctor or $5 for a prescription). Your coinsurance will be based on lower charges for using the "preferred" provider. If you choose to go outside the network, you will have to meet the deductible and pay coinsurance based on higher charges. In addition, you may have to pay the difference between what the provider charges and what the plan will pay. It’s important that you look over the list of providers and make sure that the doctors you want to go to are part of the list. Otherwise you will be paying more to use those providers.

**Health Maintenance Organization (HMO).** HMOs offer members a range of health benefits, including preventive care, for a set monthly fee. There are many kinds of HMOs. If doctors are employees of the health plan and you visit them at central medical offices or clinics, it is a staff or group model HMO. Other HMOs contract with physician groups or individual doctors who have private offices. These are called individual practice associations (IPAs) or networks.

HMOs will give you a list of doctors from which to choose a primary care doctor. You are restricted to the doctors in the HMO and if they change, you will have to choose from whomever is hired. This doctor coordinates your care, which means that generally you must contact him or her to be referred to a
specialist. With HMOs there may be a copayment, like $5 or $10, for various services. If you belong to an HMO, the plan only covers the cost of charges for doctors in that HMO. If you go outside the HMO, you will pay the bill. This is not the case with point-of-service plans.

**Point-of-Service (POS) Plan.** Many HMOs offer an indemnity-type option known as a POS plan. The primary care doctors in a POS plan usually make referrals to other providers in the plan. But in a POS plan, members can refer themselves outside the plan and still get some coverage.

If the doctor makes a referral out of the network, the plan pays all or most of the bill. If you refer yourself to a provider outside the network and the service is covered by the plan, you will have to pay coinsurance.

The distinctions between these kinds of plans have begun to blur as health plans compete in the marketplace. Some indemnity plans offer managed care-type options, and some managed care plans offer members the opportunity to use providers who are "outside" the plan.

**Choosing a Plan**

There is not one health plan that is best for everyone. Younger people with less health care needs will choose a different plan than elderly people with chronic illnesses. The first step in choosing a health plan is to write down all your current and anticipated health care needs. For example, if you have back problems and need the services of a chiropractor, you need to note this down. If you are planning to have a child, you need to write down that you will have maternity health care needs.

Usually the trade-off is between how many services will be covered versus how much premium and other costs you will pay. Most plans provide coverage for physical exams and health screenings, care by specialists for medically necessary services, hospitalization and emergency care and prescription drugs. You might want to check on care and counseling for mental health, services for drug and alcohol abuse, obstetrical-gynecological care and family planning services, ongoing care for chronic (long-term) diseases, conditions, or disabilities, physical therapy and other rehabilitative care, home health, nursing home, and hospice care, chiropractic or alternative health care, such as acupuncture and any experimental treatments you are considering.

Additionally, look at preventive care, such as shots for children, women health screenings, and help to quit smoking, etc. Check to see if the plan specifically excludes a treatment that you may need.

**Quality of Plan**

Many managed care plans are regulated by Federal and State agencies. Indemnity plans are regulated by State insurance commissions. The Washington State Insurance Commissioner keeps track of complaints by plan.

You can also find out if the managed care plan you are interested in has been “accredited,” meaning that it meets certain standards of independent organizations. Some States require accreditation if plans serve special groups, such as people in Medicaid. Some employers will only contract with plans that are accredited. Several national organizations review and accredit plans and institutions (click on [http://www.ahrq.gov/consumer/hlthpln2.htm#sources](http://www.ahrq.gov/consumer/hlthpln2.htm#sources) and go to “Additional Sources of Information). You can contact these organizations to see if a plan you are considering is accredited.

Another approach is to ask the plan how it ensures good medical care. Does the plan review the qualifications of doctors before they are added to the plan? Plans are supposed to review the care that is given by their doctors and hospitals. How does the plan review its own services, and has it made changes?
to correct problems? How does the plan resolve member complaints? Some managed care plans survey members about their health care experiences. They may produce a report card that includes satisfaction and other measures of quality including how many people stay or leave the plan, how many doctors are board certified, and how long you have to wait for an appointment. Ask the plan for these reports for consumers, businesses and the community. Keep any eye out for magazine articles that rate health plans.

Talk to current members of the plan. Ask how they feel about their experiences, such as waiting times for appointments, the helpfulness of medical staff, the services offered, and the care received. If there are programs for your particular condition, how are the patients in it doing?

You can also check how many complaints have been filed against the plan at https://fortress.wa.gov/oic/complaints/health.aspx?Year=2005.

**Doctor Qualifications**

With many of the managed care plans, you will be working with a primary care doctor to make most of the medical decisions. In many plans, care by specialists is only paid for if you are referred by your primary care doctor. Review the list of primary care doctors and check out their credentials. Ask other plan members who they use as a doctor. You must feel comfortable and trust the primary care doctor as he or she may be guiding you through some perilous times.

Then check the specialists that you will be using. You can ask doctors you know, medical societies, friends, family, and coworkers to recommend doctors. You may also contact hospitals and referral services about doctors in your area.

- Ask plans and medical offices for information on their doctors' training and experience.
- Look up basic information about doctors in the Directory of Medical Specialists, available at your local library. This reference has up-to-date professional and biographic information on about 400,000 practicing physicians.
- Use "AMA Physician Select," which is the American Medical Association's free service on the Internet for information about physicians (http://www.ama-assn.org/aps/amahg.htm).
- Is the doctor board certified? Although all doctors must be licensed to practice medicine, some also are board certified. This means the doctor has completed several years of training in a specialty and passed an exam. Call the American Board of Medical Specialties at 800-776-2378 for more information.
- Have complaints been registered or disciplinary actions taken against the doctor? To find out, contact the Washington State Medical Licensing Board https://fortress.wa.gov/doh/hpqa1/hps5/Medical/default.htm.
- If you can, arrange to interview the doctor to see what experience they have with your health condition.

**Health Plan Evaluation Check List**

| My (self, spouse and dependents) special health concerns: |  |
Chronic illness

Preventive

Other

Health concerns that I anticipate in the future:

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Ask other members

Doctor Quality
Doctor selection good?
Board certified
Years experience
Complaints?
Personal references?

Convenience
Location
Hours of operation
Off-hour support
Recordkeeping required

Other

Note: Check to see if care and counseling for mental health, services for drug and alcohol abuse, obstetrical-gynecological care and family planning services, ongoing care for chronic (long-term) diseases, conditions, or disabilities, physical therapy and other rehabilitative care, home health, nursing home, and hospice care, chiropractic or alternative health care, such as acupuncture and any experimental treatments are covered.

Source: Much of the information on how to choose a plan was adapted from the Agency of Healthcare Research and Quality [http://www.ahrq.gov/consumer/hlthpln1.htm](http://www.ahrq.gov/consumer/hlthpln1.htm).

Health Savings Accounts (HSAs)
Health Savings Accounts (HSAs) were created by The Medicare Prescription Drug Improvement and Modernization Act of 2003 to allow you to pay for your current health care expenses and to save for future qualified medical and retiree health expenses on a tax-free basis. You, your family members, and your employer can make tax-deductible contributions to your account. To open up an HSA account, you must have a High Deductible Health Plan (HDHP). A health plan qualifies as an HDHP if it has an annual deductible of at least $1,050 for an individual’s coverage or $2,100 for family coverage.

You can use your HSA to pay the deductible on your HDHP and any other qualified expenses your plan does not cover, such as vision and dental fees, and over-the-counter drugs. You make the decisions on how to spend the money in your account for qualified health expenses. You don’t rely on a third party or a health insurer for approval of your health decisions. Your unused account balances roll over from year to year.

Any individual covered under a qualified high deductible health plan may establish an HSA. However, if you are on Medicare or you receive benefits from the Department of Veterans Affairs, you cannot set up an HSA. For 2006, the maximum amount you can deposit into an HSA is: $2,700 for single coverage
$5,450 for family coverage

If you are age 55 or older, you can deposit additional money (also referred to as “catchup” contributions) into your HSA account of $700 for 2006, $800 for 2007, $900 for 2008 and $1000 thereafter.

The HDHP maximum annual out-of-pocket expense is $5,250 for self-only coverage and $10,500 for family coverage. HDHPs in Washington state must comply with state insurance laws. If you have questions about a HDHP and whether it’s a valid plan, call our Insurance Consumer Hotline at 1-800-562-6900.

Funds contributed to an HSA belong to the account beneficiary. If you change employers or leave the work force, they stay with you. Money can accumulate in the account every year. Unused amounts remain available in later years. Financial institutions or life insurance companies usually administer HSAs.

The Internal Revenue Service Web site at http://www.irs.gov/publications/p969/ar02.html#d0e1691 provides information on HSAs and other medical spending accounts that might apply to you. To determine what medical costs qualify see Internal Revenue publication 502, Medical and Dental Expenses http://www.irs.gov/taxtopics/tc502.html. The Washington State Insurance Consumer Hotline at 1-800-562-6900 also has information on plans.

COBRA

The federal government created the Consolidated Omnibus Budget Reconciliation Act (COBRA) in 1985 to guarantee that working Americans who lost their jobs did not lose their health insurance. Prior to 1985, terminated employees or employees whose hours were cut back often found themselves without health insurance. COBRA provides some measure of protection for employees, retirees, spouses, and dependent children. For a detailed look at the COBRA law and procedures, you can visit the Department of Labor’s Web site on pension and welfare benefits at http://www.dol.gov/ebsa/faqs/faq_consumer_cobra.html.

Under COBRA, employees who lose their employer-provided health insurance and their eligible dependents may apply for and purchase coverage at group rates at their own expense. COBRA most commonly guarantees extension of health insurance for up to 18 months, although spouses and children may qualify for extensions of up to 36 month when they lose their dependent status. Employers must notify employees about their COBRA rights. Once notified of their eligibility, employees have 60 days to accept coverage. However, COBRA does not apply to everyone. There are several important exceptions and criteria. The law generally applies only to employers who had 20 or more workers in the previous year, although seasonal-type operations may or may not qualify.

State and local governments fall under COBRA, but the law does not apply to federal plans or to certain religious organizations. (Federal employees do have some similar rights under another law and should ask their personnel division for more information.) Also, COBRA generally does not apply to employees who are terminated for “gross misconduct.” Health insurance through COBRA is often expensive. Because the law only guarantees the right to purchase coverage “at the group rate,” a COBRA purchaser will pick up the employer’s share of premiums and any future increase in premiums that the group is charged.

Washington's Patient Bill of Rights

INTENT: The Legislature intends that patients covered by health plans receive quality care, designed to maintain and improve their health, including sufficient and timely access and adequate choice of health-care providers:

The Bill of Rights (2SSB6199) outlines procedures to ensure that patients:
• Are assured that health-care decisions are made based on appropriate medical standards;
• Have better access to information regarding their health insurance plans;
• Have access to a quick and impartial process for appealing denials of coverage;
• Have the right to independent third-party reviews of denials;
• Are protected from unneeded invasions of their privacy.
• Can seek redress for damages that result when managed care carriers withhold or deny appropriate care.

These provisions took effect on July 1, 2001.

Privacy Guarantees
A health carrier is prohibited from releasing personally identifiable health information unless it is authorized in writing, unless it is required to control sexually transmitted diseases, or unless it is covered by existing privacy laws applying to health information. The Insurance Commissioner adopted rules to implement these requirements on January 9, 2001. These rules took effect on July 1, 2001 with benefits effective on the policy renewal date.

Disclosure of Health Plan Benefits, including Exclusions
A listing of covered benefits, including prescription-drug coverage, must be disclosed prior to purchase of any health plan. This disclosure must include any exclusion, limitation or reduction in coverage, including any coverage criteria which may be applied when determining what is covered. Other items to be disclosed prior to purchase are the carrier's policies to protect confidentiality, premium, and other enrollee costs, a summary of grievance procedures, an explanation of the amount you need to pay for services (i.e. Copays, deductibles or coinsurance) and a convenient means of obtaining a list of participating providers. Additional information describing the plan and its operations must be made available upon the request of a prospective enrollee or a current enrollee.

Grievance Procedures
Each health carrier must implement a grievance process under which an enrollee can appeal any denial of coverage. The process must meet standards established by the Insurance Commissioner, as well as meet timelines, notice and due process requirements established in the law. The process must be prompt, fair and impartial, providing timely notice of its results to the enrollee together with notice of other options for alternative treatment, further appeal or independent third party review.

Independent Third-Party Review of Appeals
An enrollee whose health coverage has been denied may seek an independent, third-party review, and insurers must develop a process to allow it. The results of this review are binding on the carrier. The Department of Health has adopted rules for certification of review organizations. The Insurance Commissioner has adopted rules for the selection and operation of independent organizations to perform these reviews. The commissioner is responsible for designating organizations meeting these standards, charging health carriers' fees as needed to fund these organizations, and providing ongoing oversight of the review boards.

Redress for Damages that Result from Denial of Care
Health carriers and their employees and agents must follow accepted standards of care when making health care treatment decisions. In the event they fail to follow accepted standards of care, consumers can sue for damages in some cases, depending upon the type of coverage they have. Generally speaking, consumers covered by individually purchased health plans can sue under Washington law, but enrollees in group employee benefit plans are often subject to other laws that restrict their ability to sue. (For more information on carrier liability and group health plans, contact either the Office of the Washington State Insurance Commissioner at (800) 562-6900 or the U.S. Department of Labor at (866) 444-3272.) Consumers must exercise the opportunity for independent review prior to suing their carrier, unless they have already been hurt or an independent review is deemed not beneficial to the enrollee.
Access to Providers
Health carriers must allow subscribers to choose a primary health care provider from a list of participating providers and allow them to change providers. Carriers must provide prompt and appropriate referrals to specialists. When chiropractic care is covered, subscribers must be allowed direct access to chiropractic care. Subscribers with complex or serious conditions may even receive a standing referral to a specialist.

Terminology Worksheet
Define the following and give an example:
- Deductible
- HMO
- PPO
- PSO
- Indemnity plan
- Coinsurance
- Out-of-pocket limit
- Lifetime limit
- Medically necessary
- Pre-existing condition

Assignment – Evaluate a Health Plan
Outline your health care requirements.

Select three health plans from the list. Do research on the health plans and fill out the Health Plan Evaluation Checklist (you may not be able to assess doctor quality). Which one would you purchase? http://www.insurance.wa.gov/publications/health/Consumers-Guide-PDFS/All_Health_Plans.pdf

Health Plan Evaluation Check List
My (self, spouse and dependents) special health concerns:

- Chronic illness
- Preventive
- Other

Health concerns that I anticipate in the future:
<table>
<thead>
<tr>
<th>Basics</th>
<th>Premium</th>
<th>Deductible</th>
<th>Coinsurance</th>
<th>Copay</th>
<th>Out of pocket limit</th>
<th>Maximum lifetime limit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Coverage</td>
<td>What does the plan cover?</td>
<td>Preventive coverage?</td>
<td>Alternate medicine coverage?</td>
<td>Exclusions?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Plan Quality</td>
<td>Accredited?</td>
<td>Patient satisfaction surveys</td>
<td>Report cards</td>
<td>Ask other members</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Doctor Quality</td>
<td>Doctor selection good?</td>
<td>Board certified</td>
<td>Years experience</td>
<td>Complaints?</td>
<td>Personal references?</td>
<td></td>
</tr>
<tr>
<td>Convenience</td>
<td>Location</td>
<td>Hours of operation</td>
<td>Off-hour support</td>
<td>Recordkeeping required</td>
<td>Other</td>
<td></td>
</tr>
</tbody>
</table>

Financial Education at BCC
Investing in Washington’s Future
2009 Page 67
Source: Much of the information on how to choose a plan was adapted from the Agency of Healthcare Research and Quality [http://www.ahrq.gov/consumer/hlthpln1.htm](http://www.ahrq.gov/consumer/hlthpln1.htm).

Activity - Discussion

What are the most common illnesses? What percent of the population gets them? How much do they cost? [http://www.fpnotebook.com/Prevent/Epi/MrtltStstcs.htm](http://www.fpnotebook.com/Prevent/Epi/MrtltStstcs.htm)


Activity – How would you choose a doctor?

How do you choose a doctor? Choose a doctor from the Seattle Magazine best doctor list. How would you check the credentials of the doctor?

- Ask plans and medical offices for information on their doctors' training and experience.
- Look up basic information about doctors in the Directory of Medical Specialists, available at your local library. This reference has up-to-date professional and biographic information on about 400,000 practicing physicians.
- Use "AMA Physician Select," which is the American Medical Association’s free service on the Internet for information about physicians ([http://www.ama-assn.org/aps/amahg.htm](http://www.ama-assn.org/aps/amahg.htm)).
- Is the doctor board certified? Although all doctors must be licensed to practice medicine, some also are board certified. This means the doctor has completed several years of training in a specialty and passed an exam. Call the American Board of Medical Specialties at 800-776-2378 for more information.
- Have complaints been registered or disciplinary actions taken against the doctor? To find out, contact the Washington State Medical Licensing Board [https://fortress.wa.gov/doh/hpqq1/hps5/Medical/default.htm](https://fortress.wa.gov/doh/hpqq1/hps5/Medical/default.htm).
- If you can, arrange to interview the doctor to see what experience they have with your health condition.

List other sources of information on how to choose doctors.

Assignment - Evaluate health plans.

Here is the table for 2005:

<table>
<thead>
<tr>
<th>Company Name</th>
<th># of Complaints</th>
<th>Complaint Index</th>
<th>Market Share</th>
<th>Premium</th>
</tr>
</thead>
<tbody>
<tr>
<td>MOLINA HEALTHCARE OF WASHINGTON INC</td>
<td>4</td>
<td>0.2</td>
<td>6.96%</td>
<td>$594,216,710</td>
</tr>
<tr>
<td>COMMUNITY HEALTH PLAN OF WASHINGTON</td>
<td>5</td>
<td>0.2</td>
<td>5.29%</td>
<td>$451,714,471</td>
</tr>
<tr>
<td>Health Plan</td>
<td>Unit</td>
<td>Risk Management in Your 30s</td>
<td></td>
<td></td>
</tr>
<tr>
<td>-------------------------------------------------</td>
<td>------</td>
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<td></td>
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</tr>
<tr>
<td>Kaiser Foundation Health Plan of the Northwest</td>
<td>3</td>
<td>Homeowner Insurance</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Group Health Cooperative</td>
<td>34</td>
<td>A homeowner policy is a protection package that provides coverage for your property. This insurance covers damage or destruction, medical payments for others who may be hurt while on your property and protection against claims someone else makes against you. This is available for primary residence home that you live in. According to the National Association of Insurance Commissioners, homeowners suffered $41.9 billion in losses in 2005. Every year about 7% of insured homeowners have a loss that results in a claim. The average homeowner's insurance premium for Washington state in 2004 was $590.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Washington Dental Service</td>
<td>12</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Asuris Northwest Health</td>
<td>3</td>
<td></td>
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<tr>
<td>Group Health Options Inc</td>
<td>17</td>
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<tr>
<td>Regence Blue Shield</td>
<td>94</td>
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<tr>
<td>Pacificare of Washington Inc</td>
<td>31</td>
<td></td>
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<tr>
<td>Kps Health Plans</td>
<td>10</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Premera Blue Cross</td>
<td>158</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Willamette Dental of Washington Inc</td>
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<tr>
<td>Vision Service Plan</td>
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<tr>
<td>Regence Bluecross BlueShield of Oregon</td>
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<td></td>
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</tr>
<tr>
<td>Aetna Health Inc</td>
<td>7</td>
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<tr>
<td>Lifewise Health Plan of Washington</td>
<td>42</td>
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</tr>
<tr>
<td>Dental Health Services Inc</td>
<td>1</td>
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<td></td>
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<tr>
<td>Great West Healthcare of Washington Inc</td>
<td>1</td>
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<tr>
<td>RegenceCare</td>
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<td></td>
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<tr>
<td>RegenceCare</td>
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</tr>
</tbody>
</table>

**Unit 4: Risk Management in Your 30s**

**Homeowner Insurance**

A homeowner policy is a protection package that provides coverage for your property. This insurance covers damage or destruction, medical payments for others who may be hurt while on your property and protection against claims someone else makes against you. This is available for primary residence home that you live in. According to the National Association of Insurance Commissioners, homeowners suffered $41.9 billion in losses in 2005. Every year about 7% of insured homeowners have a loss that results in a claim. The average homeowner's insurance premium for Washington state in 2004 was $590.
The National Association of Insurance Commissioners (NAIC) survey revealed major homeowner misunderstandings about what is covered by standard homeowner's insurance policies. The NAIC survey revealed another type of potential consumer misunderstanding. Twenty-four percent of respondents indicated their policies insured their homes for the actual cash value, while 64 percent said their policies covered the replacement cost of their homes in the event of a catastrophe. Another 12 percent said they did not know which type of coverage (actual cash value or replacement cost) they purchased.

This is what you may be covered for:

**Dwelling coverage.** This coverage provides money for the repair or rebuilding of your damaged or destroyed home and attached structures, such as a garage or deck up to the limit defined in the policy. You should not get coverage for the value of the land—only the building. This coverage can be for “actual cash value,” “replacement value,” “extended replacement value” or “guaranteed replacement value.” It is
better to choose replacement value because actual cash value may cover only a portion of what it costs you to replace the damage. Extended replacement value will cover 20% to 30% of your limit and guaranteed replacement value will cover the full cost of replacing the damage. You will have to pay for the extra coverage. The insurance industry estimates that most homeowners undervalue their property by 21% on average.

Usually water damage and earthquakes are not covered under this. You may to get an endorsement for earthquakes or buy other insurance. Check with the federal government at www.floodsmart.gov to find out more about flood insurance. Think very carefully about what the limit of this coverage should be. Talk to your agent or broker and ask questions about what will happen under various scenarios.

**Coverage for other structures.** This coverage provides for the repair or replacement of other permanent, separate, unattached structures on your property. The limit is typically 10 percent of the dwelling coverage. This coverage protects against a loss to a detached garage or personal workshop. It usually will not provide coverage for other buildings on your property that renters occupy, or buildings you use for business. If you have an unusually large detached garage or several outbuildings on your property, you may need to buy additional coverage.

**Personal property coverage.** This coverage provides for repair or replacement of your furnishings and personal items, such as your TV, stereo, clothing, dishes, etc. This is usually set at 70 percent of the dwelling coverage. It’s advisable to do an inventory of your personal property to see if you need more coverage. Often insurance companies will have limits on valuable items in your home such as jewelry. If you have items that exceed that limit you need to purchase extra insurance. In replacing your items, your insurance company will initially pay you for the used value of your item. After you buy the replacement item, your insurance company will pay you the difference between the used value and the actual replacement cost.

This coverage extends worldwide, but usually provides only up to 10 percent of the personal property coverage limit for property you take with you when you travel. Insurance companies usually offer personal property coverage on a named peril basis. This means that the policy will specify and list the perils that are covered by insurance. Commonly covered perils include fire, lightning, windstorm, hail, explosion, riot or civil commotion, aircraft, vehicles, smoke, vandalism and malicious mischief, theft, and damage caused by falling objects. Insurance policies always exclude certain events. An “Act of God” which is an extraordinary and unexpected event such as a tornado or hurricane might not be covered in your policy. It’s important that you sit down with your agent and broker and go through what you think might happen to see if you are covered.

**Coverage for loss of use or additional living expenses.** This coverage pays for your living expenses if you can’t live in your house. However, your normal expenses, such as your house mortgage payment or utility bills, are not covered. Your policy usually will include the loss of use or additional living expense coverage at 20 percent of your dwelling coverage limit without additional premium.

**Medical payments coverage.** This coverage pays the medical expenses of others when they are accidentally injured on your property. Most policies include at least $1,000 of coverage, but higher limits may be available. Generally, this coverage is limited to any non-resident on your property with your permission. The insurance company does not need to determine negligence to pay the injured person or their provider. This coverage also is called “good neighbor” coverage.

**Personal liability coverage.** This coverage pays expenses for bodily injury and property damage sustained by others when you are legally liable. For example, if you knew you had a broken walkway and someone tripped and fell, you would be liable. Most policies include at least $100,000 of coverage, but higher limits may be available. When deciding how much coverage to buy, think about the value of your total assets, and how much you might lose if someone successfully sued you for damages. Personal liability coverage extends beyond your property limits. If an incident occurs involving family members who
live with you (as defined in your policy) at other locations, it will cover the liability of your family members. Don’t forget that you could be sued and may have to pay out of future earnings. Many families will purchase umbrella coverage (discussed later) for up to $2 million to protect themselves for large law suits. For example, it may provide coverage if your minor child damages a neighbor’s property. This type of coverage generally provides for debris removal, damage to trees, plants and shrubs.

You can get other kinds of coverage your insurance company offers by purchasing an endorsement. Endorsements include protection against losses from sewer or sump pump backing-up, coverage for a second home, coverage for your small sailboats and motor boats, broader theft coverage (to include auto and boat), and credit card and check forgery protection.

The following chart from the National Association of Insurance Commissioners shows the typical homeowner policies and what they cover. The most popular form is the HO3 Special.

### Loss Chart

<table>
<thead>
<tr>
<th>Kind of Policy</th>
<th>Losses Covered</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Dwelling</td>
</tr>
<tr>
<td>D-1</td>
<td></td>
</tr>
<tr>
<td>HO-1 Basic</td>
<td></td>
</tr>
<tr>
<td>HO-2 Broad</td>
<td></td>
</tr>
<tr>
<td>HO-3 Special</td>
<td></td>
</tr>
<tr>
<td>HO-4 &amp; 45-50</td>
<td></td>
</tr>
<tr>
<td>COMB</td>
<td></td>
</tr>
<tr>
<td>HO-8</td>
<td></td>
</tr>
</tbody>
</table>

- Fire or lightning
- Loss of property removed from premises endangered by fire or other perils
- Windstorm or hail
- Explosion
- Riot or civil commotion
- Aircraft
- Vehicles
- Smoke
- Vandalism and malicious mischief
- Theft
- Breakage of glass constituting a part of the building
- Falling objects
- Weight of ice, snow, sleet
- Collapse of building or any part thereof
- Sudden and accidental tearing, apart, cracking, burning or bursting of a stream or hot water heating system or of applicances for heating water
- Accidental discharge, leakage or overflow of water or steam from within a plumbing, heating or air conditioning system or domestic appliance
- Freezing of plumbing, heating and air conditioning systems and domestic applicances
- Sudden and accidental damage from artificially generated currents to electrical appliances, devices, fixtures and wiring (TV and radio tubes not included)
- All perils except flood, earthquake, war, nuclear accident and others specified in your policy. Check your policy for a complete listing of perils not covered

Source: National Association of Insurance Commissioners- Consumer Guide to Homeowners Insurance

### House Insurance

**Summary for House Insurance**

1. Do an audit of your house and install safety features.
2. Do an inventory of your personal property. Get appraisals as necessary. Most policies have a limit on jewelry, cameras, guns, and other high priced items. It may be necessary to get additional coverage if you exceed the limit.
3. Do research on how much it will cost to replace your home.
4. Consider your assets in determining your personal liability coverage.
5. Make a list of all the coverage you want using the worksheet shown later.
6. Pull your credit report and correct any errors.
7. Have a history of your house insurance claims.
8. Check rating services such as Consumer Reports. Check the Washington state Insurance Commissioner for complaints. Check for financial stability at AM Best or Standard and Poors.
9. Call the agent or broker for the insurance company you want to check out.
10. Get the quote in writing.
11. Compare all quotes and choose the best for you. Don't be rushed or let the agent or broker use persuasive tactics to rush you.

Go through your house and put in features that might lower your insurance costs. This includes smoke detectors, deadbolt locks, an alarm system, reinforcing your house for earthquakes, getting fire resistant roofing, strapping your hot water heater and securing all bookshelves. Attend a community session on earthquake readiness and get other tips. Ask your local fire department for ideas of how to make your house safer. Remove any potential hazards.

Insure only the value of the house, not value of the land. Make a list of the structures and coverage you will need. Newer homes with newer equipment should warrant lower premiums. Construction materials which make your house safer will also result in lower premiums. Make sure that you let your agent or broker know if your house has these safety features.

Typically we use the assessed value or the market value of our home to determine what it is worth. When you determine the replacement cost for insurance purposes it may be different from your local government’s assessed value for tax purposes or what another buyer will pay for it. They use different criteria to establish those values. Remember, the cost to actually rebuild your home may exceed its current market value or sales price. Talk to your agent to find out if you have an adequate amount of coverage. Keep in mind, if you do not insure at least 80% of the replacement value of your home, your insurer will prorate your claim by the amount that you are short.

Once you establish the appropriate coverage amount for your home, you should review this information annually. This will ensure your coverage keeps pace with inflation and other changes that affect the cost to repair or replace any damage to your home. Most policies automatically adjust your dwelling limit at renewal, so you may want to review it to make sure you have adequate coverage. Whenever you make changes to your home, such as additions or major improvements, notify your insurance company. The renovation can affect the amount of coverage you need to maintain full replacement cost coverage. Talk to your agent before you make major improvements or renovations.

Check out the insurance company thoroughly. Make sure that it is financially stable by checking its AM Best (www.ambest.com), Standard and Poor’s (www.standardandpoors.com/ratings) ratings, Duff and Phelps Inc. www.insure.com/ratings, or Moody’s Investor Services www.moodys.com. These also can be obtained at your local library. Check how the insurance company fares on processing claims for its customers. Consumer Reports (also available at your local library) publishes information on that. Go the Washington state Insurance Commissioner’s website and check on its complaint record: https://fortress.wa.gov/oic/complaints/home.aspx?Year=2005. Make sure the company you’re considering is licensed to do business in Washington. If you have questions about a company, call the Washington state Insurance Consumer Hotline at 800-562-6900.

The amount of the deductible you select will affect your premium. The higher the deductible, the less expensive the insurance premium. But don't forget that, in the event of a loss, you'll have to pay the amount of your deductible from your own money before your insurance pays for any damages. Don't take a deductible that will be too much for you to pay. If you have personal property stolen from your rental car during your vacation, you could make a claim against your insurance. Filing claims in a short period of
time, even if they are small claims, can result in your homeowner’s policy being cancelled, or your rates going up.

Buying your house and auto insurance from the same company will save you premiums. Staying with an insurer for a long time will also reduce your premiums. Be sure to ask for these when you talk to your agent or broker.

If you are 55 years of age or older, you can save on premiums.

Ask your agent or company if they offer any special discounts for professional groups or employers.

### Homeowner Insurance Evaluation Form

<table>
<thead>
<tr>
<th>Company Name:</th>
<th>Company Name:</th>
<th>Company Name:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contact Information</td>
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<tr>
<td>Dwelling Coverage Limits</td>
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<tr>
<td>Personal Property Coverage Limits</td>
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<tr>
<td>Personal Liability Coverage Limits</td>
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<tr>
<td>Loss of Use</td>
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<tr>
<td>Medical Payments</td>
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</tr>
<tr>
<td>Deductible</td>
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<td></td>
</tr>
<tr>
<td>Method of valuation:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Actual Cash Value,</td>
<td></td>
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</tr>
<tr>
<td>2. Replacement cost,</td>
<td></td>
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</tr>
<tr>
<td>3. Extended replacement cost</td>
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<tr>
<td>4. Guaranteed replacement cost</td>
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</tr>
<tr>
<td>Earthquake (deductible?)</td>
<td></td>
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</tr>
<tr>
<td>Other coverage needed:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Note flood insurance is provided by government)</td>
<td></td>
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</tr>
<tr>
<td>Claims rating</td>
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<tr>
<td>Complaint record</td>
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<tr>
<td>AM Best Rating</td>
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<tr>
<td>Standard and Poor Rating</td>
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</tr>
<tr>
<td>Other Ratings</td>
<td></td>
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</tr>
</tbody>
</table>

(Note flood insurance is provided by government)
Earthquake Insurance

Earthquake insurance provides coverage if your home is damaged by an earthquake. A standard homeowner and renter’s policy will not cover earthquake damage. It can be purchased as an endorsement to some policies or you may have to find another insurance company. An earthquake endorsement generally excludes damages or losses from floods and tidal waves even if it was caused or compounded by an earthquake.

Earthquake insurance is designed to cover catastrophic damage. Insurers will set deductibles high at 10 to 25 percent of the structure’s policy limit. The insurance only pays for damages that exceed the deductible. You may have a separate deduction for the contents of your home, the house itself and unattached structures. Check the details before you purchase.

Some insurers may require an inspection of your property before they will agree to issue a policy. They may check to see that your home is bolted to its foundation, the bracing of interior walls, strapping the water heater and the mounting of shelves. Many of these improvements are not expensive and you might want to install them to save aggravation in the event of a minor earthquake.

Make sure your water heater, gas appliances, and other such fixtures are fastened securely. Teach all family members how to shut off gas to the house. Ensure bookcases, wall hangings, and hanging plants are secure and fastened to walls and ceilings. Make sure you have an emergency plan and all family members know what they should do if an earthquake occurs. Designate a meeting place outside the home where family members can gather once the danger has passed.

Designate a distant relative or friend who can serve as a point of contact and communication for you and your family members if you get separated. Create an earthquake kit that can be easily accessible outside of the house. This would include flashlights, batteries, candles, a portable radio, water and food for a week.

Train all members of your family what to do when an earthquake strikes. These procedures can be used to other emergency readiness as well:

1. If you are inside when an earthquake hits, stay inside and get under a heavy table or desk. Stay away from windows. Do not evacuate the building unless emergency personnel direct you to leave.
2. If you are outside, get away from buildings and power lines, and remember that stone and masonry facings can break loose and fall away from upper parts of buildings.
3. If an earthquake occurs, watch for items that might break and fall, especially glass items. Broken glass on the floor causes many of the injuries people suffer in the aftermath of an earthquake, and glass-filled carpet is hazardous long after the danger of an earthquake passes.
4. If you are in a car, stop safely away from structures, large trees, power lines, and other hazards. Stay inside the vehicle.
5. Don't use candles until gas lines are checked. Also, check all areas of your home before you use certain utilities, such as water and electric, sewage connections, and even chimneys.
6. Don't tie up phone lines except to report emergencies.
7. Be prepared. Remember that you will need food and water, even for the short term. Keep your family together and stay alert for aftershocks.

Factors that affect your premium
All insurance companies set guidelines to determine whether they should accept you for coverage and how much they should charge you. These factors include:

**Property information**
This includes your street address, the year your house was built, number of living units, type of construction material, type of foundation, living space square footage, number of rooms, age of the roof, floor plan, roofing materials, and the age of heating, plumbing, and electrical systems.

**Community fire protection**
These factors include the distance from your home to the nearest fire department and fire hydrant, and the fire department’s response time.

**Prior insurance**
Insurance companies look at your prior insurance history. For example, if you own an uninsured property for several years, and then decide to insure it, you will have a more difficult time getting insurance. Insurance companies believe this shows a lack of responsibility by the homeowner.

**Claims and occurrence history**
Your insurance company may ask you to disclose both claims and occurrences from the past. A claim is a loss you reported to the company for coverage. An occurrence is either a loss you did not report, or if you did report it, it did not result in an opened or processed claim. Insurance companies believe this represents the potential for loss, and may ask you about such events.

**Your history**
Under federal law (Fair Credit Reporting Act), insurance companies can use credit history as one factor that impacts your homeowner rate. They may assign you an insurance score based on your credit history. They use your score as one factor to decide whether to accept or decline your coverage, or how much to charge you. However, Washington state has further restrictions on how insurance companies can use credit. You can review this in the auto insurance section. Some companies may charge you more based on the number of claims you have filed. They may even cancel your coverage if you made several claims. Your insurance company will ask you for information, such as your occupation and how long you have worked for your current employer to determine how stable you are.

**Submitting a claim**
Insurance is something you hope that you will never have to use, but if you should ever need to file a claim after experiencing a loss, the following suggestions to prepare yourself before any loss can make the process easier:

1. Create and annually update a written inventory of your personal property.
2. Videotape or photograph the contents of your home, and the exterior from different viewpoints and angles.
3. Engrave or mark larger possessions to show ownership.
4. Have someone appraise your jewelry, antiques, stamps, coins, and other valuable collectibles.
5. Keep your insurance policy, home inventory, appraisals, photos and video records in a secure secondary location (such as your office or a safety deposit box).

You should make an inventory of your household goods and have it on file. If a disaster occurs and you need to file an insurance claim, a household inventory of your personal property is one of the most helpful things you can do to make the claims process easier. A household inventory is a list of all your personal items in your home that includes where you bought each item, how much you paid, and any identifying
information, such as model or serial numbers. It can save you time and prevent disagreements with your insurance company.

Many homeowners discover after a loss that they don’t have enough personal property coverage or they are unable to document their lost or destroyed items. A complete and current inventory can help you and your insurance company prevent either of these possibilities. Don’t wait for disaster to strike before you sit down and figure out what your possessions are worth.

Building a household inventory is easy to do. First, make a list of all the rooms in your house. Then go room-to-room and list your possessions. Jot down supporting information. At a minimum, the list should contain a complete description of each item, the estimated value of each item, the price you paid for the item and where you bought it, the age of the item, and any other details that will help you document its worth. You should always separately itemize expensive items, such as large appliances, televisions, stereos, jewelry, camera equipment, computers, etc.

Be specific. Cite serial numbers, brand names, or model numbers whenever you can. Be honest. If you no longer have receipts, stick to your best memory of purchase costs. Remember that an adjuster’s question about one item on your list might raise questions about other items. When you buy expensive items, such as an appliance, computer, or a HDTV, make sure you keep the receipt with your records in a safe place and log it into your inventory.

Back up your inventory with photos or video. Photograph or video each room and its contents, leaving closet and cabinet doors open. If possible, record the inventory on a computer disc and store at least one copy with your photos or video tape.

Store those photos or video tapes and a copy of your inventory in a safe place outside your home, such as with a trusted friend, at your office, or in a safe-deposit box. Keep one copy of the inventory at home – and remember to update it at least once a year. Use a specific date as a reminder, like the start of Daylight Savings Time or right after taxes are filed. If your loss exceeds the coverage you have for personal property, you can itemize that amount on your 1040 Schedule A income tax form.

If you experience a loss

1. Notify your agent or insurance company and ask what documents, forms, and other data you need to get your claim processed.
2. Review your policy and ask your agent or insurance company for an explanation of what is covered.
3. Protect your property from further damage. Save the receipts for temporary repairs and submit them to the insurance company for reimbursement. You should not make permanent repairs until after your insurance company has inspected the damaged property.
4. If you are unable to live in your home, tell your agent or insurance company where they can reach you.
5. Itemize your losses and include copies of receipts for larger items, such as large appliances, furniture, expensive cameras, and computer equipment. If the loss is due to a criminal act, such as burglary or theft, notify your local law enforcement agency.
6. You must prove your loss with receipts. If you don’t have receipts, then photos of the damaged or missing items may help document the loss. If your insurance company requires you to submit a "proof of loss" form, complete and submit it in a timely and accurate manner. This will help prevent claim processing delays.
What is covered by your standard home insurance policy?
flood damages
Items are stolen from your home
vehicles such as cars, boats and motorcycles stolen from or damaged on their property
a person falls off your deck and sues
a break in the water line on their property supplying water to their home
a fire in your house
damages due to a break in the sewer line on their property that connects to their municipal sewer system
damages from earthquakes
damages from mold
damages from termites or other infestation
your windows are shattered by a windstorm
pets stolen from or injured on their property

Answer
flood damages N
Items are stolen from your home Y
vehicles such as cars, boats and motorcycles stolen from or damaged on their property N
a person falls off your deck and sues Y
a break in the water line on their property supplying water to their home N
a fire in your house Y
damages due to a break in the sewer line on their property that connects to their municipal sewer system N
damages from earthquakes N
damages from mold N
damages from termites or other infestation N
your windows are shattered by a windstorm Y
pets stolen from or injured on their property N

Umbrella Insurance
Some individuals may purchase liability insurance to cover for law suits that may be filed against them requesting large settlements. Many experts say most of us would do well to carry at least $1 million worth of coverage, even if we don’t have a net worth that high. After all, someone might still sue you, expecting to garnish your future wages if he or she wins. This coverage is relatively inexpensive ($1 million policy can run you $200 a year or even less) and provide protection for your assets. Umbrella insurance would sit on top of the liability limits in your auto and homeowner insurance. It will cover liability in excess of what your limits for each of those are. It can also cover slander and libel which is not covered in your standard homeowner policy.

Question:
Explain why you would want to have Umbrella Insurance.
Assignment – House insurance

If you have a house, determine what coverage you want.

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<thead>
<tr>
<th>Contact Information</th>
<th>Company</th>
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<th>Company</th>
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<tbody>
<tr>
<td>Dwelling Coverage Limits</td>
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<td>Personal Property Coverage Limits</td>
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<td>Personal Liability Coverage Limits</td>
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<td>Loss of Use</td>
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<td>Medical Payments</td>
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<tr>
<td>Deductible</td>
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<td>Actual Cash Value, Replacement cost, Extended replacement cost, or Guaranteed replacement cost</td>
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<td>Earthquake (deductible?)</td>
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<td>Other coverage needed:</td>
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<td>Claims rating</td>
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<td>Complaint record</td>
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<td>AM Best Rating Standard and Poor Rating</td>
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<tr>
<td>Other Ratings</td>
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<tr>
<td>Licensed to do business in Washington.</td>
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<tr>
<td>Premium</td>
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Activity – Discuss the following:
What factors are important in buying a house?
Share your experiences with property insurance claims.
What can you do to reduce risk on your home?

Activity - Recordkeeping
Create an inventory of your possessions with pictures and lists.
Activity — Determine how much life insurance you need.
Answer the following questions and determine how much life insurance you need.
How much do I provide for my dependents for how many years? This includes children, parents and others who depend on you for financial support.
Do my children have college tuition needs that I have to provide for?
Are there family members or organizations that I want to leave money to?
Will there be estate taxes that have to be paid when I die?
Will there be funeral arrangements that have to be paid when I die?
Total up your assets and other sources of death benefits such as social security and life insurance provided by your employer. This will give you an indication of how much life insurance you need.

Unit 5: Risk Management in Your 40’s

Prior to the 1900s, life expectancies were much shorter and people had less mobility. Individuals relied on their families to provide for them in their old age. In 1935, social security was introduced to provide income security for individuals over 65 who, it was assumed, could no longer work.

Many have come to think of age 65 as the age when individuals get to retire and to enjoy their sunset years. Now some people set the financial goal of retiring before 65—they want to retire at age 55 or earlier. Other people enjoy working and work past 65. For example, Alan Greenspan retired as the high-powered Chairman of the Federal Reserve at age 78. Others are working into their 90s. Some retirees take a reduced work schedule and others pursue new challenges such as starting a business. As life expectancies increase and the nature of work changes, there is no doubt that the concept of retirement will also change.

Retirement benefits are given to employees in three ways:
- Defined benefit plans or traditional pension plans were more prevalent with larger companies and provided lifetime income for the retiree. Investing to provide the retirement income is up to the employer.
- Defined contribution plans (401Ks, IRAs, profit sharing plans, and more) typically work as retirement accounts where the employee and/or the employer contributes. When the employee leaves the company, the account would follow. Retirement income would depend on what the employee contributed and often the employee is responsible for investment decisions.
- Social security is core to all employers. However, it provides a smaller and smaller portion of retirement benefits.

About 60% of all workers have access to retirement benefits and 51% of all workers participate. 69% of white-collar workers (office workers) and 62% of blue-collar (manufacturing) workers have these benefits but only 34% of the faster-growing service occupations are covered. Total retirement assets—which include both employer and individual accounts—have been growing and now total about $10 trillion.
By looking at the chart on the next page, it is evident that IRAs and defined contribution plans, where employees are responsible for contributing to their own retirement, are growing while other types are shrinking or staying the same. This means that it’s up to you and not your employer to take care of your retirement.

**Defined Benefit**

**Summary of Retirement Benefits**
1. Retirement benefits are given to employees in three ways, (1) Defined benefit plans, (2) Defined contribution plans, (3) Social Security.
2. Defined benefit plans provide a lifetime income for the retiree, it is an annuity. The employee is not required to contribute to the plan.
3. Defined contribution plans are primarily the contributions of the employee, with a portion of the contribution matched by the employer.

4. Defined contribution plans are becoming more prevalent than Defined benefit plans.

5. Defined contribution plans include 401Ks, IRAs, profit sharing plans, etc…

6. There are $10 trillion dollars in retirement assets, with at least 60% of workers having access to retirement benefits.

Only 20% of all workers participate in a defined benefit plan or traditional pension plan. 22% of white-collar workers and 25% of blue-collar workers have them while only 7% of service occupations are covered. To participate in this type of plan, the employee typically has to have worked for the company for a number of years. The retirement income that a person gets depends on how many years she has worked for the company and what her highest average salary was over a period of years. If the retirement benefit is paid for the rest of the retiree's life, it is a lifetime annuity.

Most defined benefit plans have vesting requirements, meaning you have to work for the company for a number of years (5 is the most common) before you are vested or are entitled to any retirement benefits. Some are cliff vested meaning you need to have worked the full number of years to qualify, or you receive nothing when you retire. For example, you have to be with the company 5 years to qualify for pension benefits. If you leave at 4½ years, you're not eligible. Other plans vest a portion based on the number of years you work; for example, 40% when you’ve worked 5 years, 60% when you’ve worked 6 years, and so on.

The benefits from these plans are based on salary and the number of years you work for the company. The most common formula is $1.5\% \times \text{the number of years} \times \text{the average of your highest 5 years of salary}$. Say your highest 5 years of salary are $50,000, $52,000, $54,000, $56,000, and $58,000 and you worked for the company for 20 years. Total the salaries and divide by 5—you get $54,000. Take $1.5\% \times 20\text{ years} \times$ $54,000$, and your pension at retirement is $16,200. Most people expect this type of plan will cover only 1/3 of retirement needs.

This type of pension plan tends to favor employees who have been with the company for a long time and who make a relatively high salary. In the majority of cases, there is an offset or deduction in the benefit for social security. Unfortunately, the average employee stays only four years in a job before she leaves for another one either because she quits or is laid off. This means the average employee would not qualify for this type of benefit. Additionally, employees who stay the 20 to 30 years that it takes to get sufficient retirement income are rare.

Defined benefit plans are attractive in that they will provide the retiree with lifetime income. Additionally, it is up to the employer to ensure that the money is there. The bad news with defined benefit plans is that people have to work for a company for a long time to get sufficient income. They are expensive for employers to maintain so more employers are getting rid of lifetime income retirement plans. Another disadvantage is that when you die (unless it is a joint plan or a survivor is selected), the monetary payments stop. No one has any right to it. The other disadvantage is the employer may not be in business, or may default, or change the original agreement at retirement. We have witnessed this with the airlines failures in the past 20 years.

There are other considerations with defined benefit plans. You may elect a joint and survivor annuity, meaning the benefits could be paid over you and your spouse’s lifetime. The annuity or annual payment is reduced to reflect the longer joint lifespan, but you get peace of mind.

Most companies have a social security offset and deduct from your retirement income if you are also entitled to social security. This allows the company to take into consideration what it paid in social security taxes. Some plans have increases in inflation built in. Some give these increases when they want. As with social security, early retirement results in reduced retirement income. The company usually
doesn’t allow you to take early retirement before a certain age (most typical is 55) and won’t give you full benefits before a certain age (62 is the most common). Plans generally pay full benefits if the employee becomes disabled but disability benefits may be tied to age and/or years of service. Very rarely can you take these assets into another retirement arrangement if you leave the company.

If you’ve worked for a number of companies, you need to track all your pension plans. Make sure the companies have current contact information for you. Otherwise, the company can lose track of previous employees. This has resulted in thousands of dollars have become lost to the employees and becoming “unclaimed property” on the corporate books.

**Defined Contribution Plans**

**Summary of Defined Benefits**

1. The lifetime retirement income is dependent on the how many years the employee has worked for the company and a percentage of salary.
2. A common formula is Highest average salary X Years of Service X 1.5%
3. There are vesting requirements before you are entitled to retirement benefits.
4. Vesting can be a percentage each year, or cliff vested. If it is cliff vested, you must work the vesting period, or you receive nothing.
5. Most people expect this type of plan will cover only 1/3 of retirement needs.
6. These plans favor employees who have been with the company for a long time and who make a relatively high salary.
7. These plans are being phased out by employers.
8. The annuity normally stops at the death of the retiree, unless a survivor option is in place. If a survivor option is elected, then the annuity is reduced to reflect the longer joint lifespan.
9. Most companies have a social security offset and deduct from your retirement income if you are also entitled to social security.
10. Plans may pay benefits, tied to age and/or years of service, if the employee becomes total disabled.
11. Very rarely can you take these assets into another retirement arrangement.
12. Be sure and keep track of all your pension plans as you work for different companies and make sure the companies have your current address.

According to the 2006 National Compensation Survey, about 54% of workers have access to defined contribution plans and 43% participate. As with defined benefit plans, more white collar workers, (53%) are covered than blue collar workers (40%) and less workers (20%) in service occupations.

Defined Contribution Plans are different from defined benefit plans in that employees make contributions to their own retirement savings accounts. Employers may or may not match contributions up to a certain amount. When the employee leaves the company, the money goes with him or her, that is, contributions are portable. Retirement income depends on how much the employee contributes and the returns on the retirement account. Some of the funds the employer contributes can also be portable depending on the vesting schedule. This is discussed in the next section.

**Savings and Thrift Plan - 401K Plans**

Many folks save for retirement through company-sponsored plans. Most of these are structured as 401K (named after the IRS code that established them in 1981) company plans where employees can make pretax contributions to their own account. According to the Investment Company Institute, in 2006 there were 43 million participants in 457,830 plans with $2.1 trillion in assets. Depending on the plan, employees may also make after-tax contributions where tax on the investment income is deferred until retirement.
If you contribute to a 401K, your money is deposited before taxes, that means your salary is reduced for tax purposes in the current year. To encourage saving, some plans will automatically make you a participant, contributing 3% of your salary unless you opt out. The maximum contribution is $15,000 (2007) with an additional catch-up of $5000 for those over 50 years old. About 82% of employees contribute and on average participants put in 6.8% of salary.

Employers may match all or part of this contribution. This means that they will put in some money for each dollar that you put in. About 91% of employers will match up to 3.3% of your salary in 2006. This means that for every dollar you put in, on average most employers will put in 50 cents. If your employer matches your contribution, the 401K is the great way to save for your retirement. If your employer matches any of your contribution, and you do not participate, it is essentially "turning down a raise" or "leaving money on the table" from the employer.

Many employers require that an employee work for a certain period of time to earn the right to keep the employer match. This is called a "vesting" schedule. Let's say you make $50,000 a year and contribute 3% or $1500 to your 401K every year. Your employer contributes $750 a year, contributing $750 a year. There is a five year vesting schedule, at 20% a year.

<table>
<thead>
<tr>
<th>Year</th>
<th>Cumulative contribution at $1500 a year</th>
<th>Cumulative Employer Match at $750 a year</th>
<th>Vested</th>
<th>Employer match that you can take with you if you leave</th>
</tr>
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<tbody>
<tr>
<td>1</td>
<td>1500</td>
<td>750</td>
<td>20%</td>
<td>150</td>
</tr>
<tr>
<td>2</td>
<td>3000</td>
<td>1500</td>
<td>40%</td>
<td>600</td>
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<tr>
<td>5</td>
<td>7500</td>
<td>3750</td>
<td>100%</td>
<td>3750</td>
</tr>
</tbody>
</table>

If you leave after two years, you would only be 40% vested meaning you could only take 40% of the total company match of $1500. You could, of course, take your contribution of $3000 for a total of $3600. If you leave after 4 years, you could take 80% of the total employer match of $3000. This with your contribution of $6000 would total to $8400. Sometimes the "vesting schedule" is based on the number of hours worked, or a calendar date, or an anniversary of hire date. Employees should be knowledgeable about their plans vesting schedule. Each plan can be different. During your employee orientation, or your first year of employment, be sure you understand the schedule. Some small business owners (family-owned, doctors, dentists, attorneys, etc.) might need to direct you to their 401K plan administrator to answer all your questions. The IRS has looked at these plans closely because of prior abuse. Make sure your questions are fully answered.

Most 401Ks allow employees to make their own decisions among investment selections. Companies offer 10 or more selections. Most allow changes at any time and the rest allow at least 4 changes a year.

About 82% of plans allow loans to the employee. Depending on the company plan, employees may borrow up to a maximum of 50% of the account balance or $50,000. Where permitted, about 25% of participants have loans for an average balance of about $6000. The loan must be repaid with after-tax payroll deductions. Most plans have restrictions on what you can borrow for. Home purchase, education, and medical expenses top the list. You might be required to repay the loan if you leave the company, and hence the retirement plan, for new employment. Take this into consideration before obtaining a loan. Review your loan covenants carefully.

You can start withdrawing money when you hit age 59½ and no later than age 70½. You can withdraw before age 59½, but only for "hardship" reasons defined by the government, and you may still have to pay 10% penalty tax on these withdrawals. If you quit your job and your account is more than $5000, you can...
leave your money with the company plan. You also have the option of moving your money to your new company’s plan or moving your money into a “Rollover IRA.” Even though you have 60 days to decide, it’s best to make these arrangements ahead of time. If the check is made out to you for a later decision, 20% will be withheld for taxes (which you don’t get back until you file your return). There is a 10% penalty for withdrawing before age 59 ½ and you have to pay taxes on your withdrawal on top of that.

Here is an example of how a 401K works. Jill is single and makes $30,000 a year gross salary. She usually pays about 15% tax on her salary. Her employer will match her 401K contributions by 50 cents for every dollar that she puts in up to a maximum of 6%. Jill puts in $1800 or 6% of her salary. Her employer matches 50 cents on her dollar so it puts in $900. Her salary for tax purposes has been reduced to $28,200 so if she stays at the same tax rate, she would save an additional $270 in taxes (15% of $1800). If her employers continue to contribute in the same way and she receives an 8% return over 30 years, her employers’ contribution is over $100,000 that she would not have otherwise. In actual case, Jill’s salary will increase and so will her employer’s contributions so the amount could be substantially more.

**One key point to make about 401Ks; the taxes do not disappear.** They are deferred meaning when you take the money out at retirement, you will have to pay taxes on the distributions. Also, another disadvantage is that you will pay taxes at ordinary income tax rates which would be higher than the capital gains tax rate that may be applicable to some of your investments. However, you compound your return on the amount you would have paid in taxes in the current year.

**401K Asset Allocation**

Once you are eligible for a 401K and have decided to contribute, you will be asked to decide how you want to allocate your contributions. This is a critical decision which will determine how much you will earn and have in your retirement account when you retire. About 52% of 401K plans offer 10 or more choices of investments. Here are the most commonly offered:

- **Money market funds.** These funds generally return at the short-term interest rates. Money market funds are low return and low risk. Some employees increase their allocation in money market funds when they are preparing to take cash out.

- **Equity funds.** Funds that invest in stocks. About 8000 different American companies are listed on the three major US stock exchanges. If you were to buy every single share of stock out there (pay the market value), you would spend about $20 trillion. Worldwide there are 54 stock exchanges and the total value of companies was $51 trillion as of the end of March 2007. When you own a stock, you own a piece of the company. In addition to being categorized as domestic and international, stocks can be categorized as large, medium or small. Larger plans may have selections in indexed funds, growth funds, and international funds. As compared to bonds, stocks have higher return and higher risk.

- **Bond funds.** These funds invest in bonds. The safest bonds are US Treasury bonds. Other bonds include corporate bonds or bonds issued by foreign countries. Bond funds do not behave like bonds that you buy and hold to maturity. There may be capital gains or losses if interest rates move. Bonds tend to be lower risk and lower return than stocks.

- **Lifestyle funds.** These allocate assets based on the age or risk tolerance of the investor. They may allocate more to stocks if the employee is young and more to bonds when the employee is older. For employees who don’t know how to allocate, these funds are an easy alternative.

- **Guaranteed Investment Contracts (GICs).** GICs are fixed-rate investments insurance companies sell to retirement plans. A GIC behaves almost as if you had invested your money in a bond which you are holding until maturity. These tend to be low risk if you hold them until their due date.
- Company stock. Some companies make their contributions (the employer match) in company stock. They also allow employees to choose company stock as an investment option. The danger with having too much of your account in one stock is that you could take a large drop in your portfolio if this stock does poorly.

As can be seen by the chart below, employees tend to allocate assets based on the market performance. During the recession of 2002, the allocation into equity funds fell by over 10%. This is an indication that employees are reacting to the market. Allocation into company stock has fallen from almost 20% in 1996 to about 15% in 2004. This is a good sign as too much of your account in one stock is a dangerous thing.

![Most of 401Ks are invested in stocks](chart)

Experts recommend that:
1. You asset allocate based on your time horizon.
2. Don’t put too much of your assets in any one category (30% to 40% maximum)
3. Invest in index funds for lower fees.
4. Dollar cost average
5. Rebalance or buy and sell investments in asset classes to match your asset allocation goals.

You also don’t have to determine which fund has the best manager. By paying yourself first 10%-15% out of every paycheck, you will use dollar cost averaging to buy into your 401K which is better than trying to outsmart the market. Since it’s been shown that we can’t outsmart the market, putting in regular amounts is the best tactic to take. (The vast majority of people buy high and sell low.)

Rebalance or buy and sell investments in asset classes to match your asset allocation goals. So, if stocks do really well and your stock allocation grows to 50%, you will sell stocks and buy another asset that has dropped to less than your allocation. Studies show that this is an effective way to maximize your return and take the edge off down markets.

Because assets get larger as the worker gets older, he or she relies more on investment returns to increase the value of the account. Younger workers increase the value of their accounts with contributions.
Asset allocation also changes with age. Younger participants put more of their assets in equity or stock funds. Older participants move more assets to fixed income so that there will be less risk as they near retirement and require the funds.

If you have a 401K with a company match available and don’t participate, you are losing out. About 18% to 25% of employees don’t participate or contribute to them. This is especially prevalent in younger folks as about half of those under 25 don’t contribute. If you don’t diversify your investments, you can lose out as well. A heavy allocation to company stock has hurt workers at Enron, Qwest, MCI Worldcom and other companies where the stock took a drubbing (dramatic loss in value).
When people leave company, 60% of younger folks will cash out their 401Ks instead of moving it over into a rollover IRA. This costs you a lot. Let’s say you have $6000 when you cash out. You will pay a 10% penalty of $600 plus taxes on the $6000 (at 15%) or $900. So $1500 is out the door leaving you with $4500 to spend. That’s not the entire cost. In 40 years that $6000 at 8% return would have grown to $130,000.

**401K Summary and Key Actions**
1. Try to put away 10% to 15% of your income for retirement.
2. Max out on the employer contribution. This is money that you shouldn’t leave behind.
3. Invest in index funds and save on fees.
4. Avoid taking out a loan on your 401K.
5. Determine an asset allocation that makes sense for your time horizon (your age will impact how long you have to invest and that will influence your asset selection.)
6. By setting aside your money every paycheck you will automatically be using dollar cost averaging to buy your funds.
7. Rebalance your portfolio to keep your designated asset allocation.
8. Ask about fees. You can lobby for a lower cost provider if you think that fees are too high.
9. Don’t cash out your 401K when you leave a company. It can hurt you in the future.

**Comparing 401Ks to Traditional and Roth IRAs**

401Ks are often compared to other tax-advantaged retirement saving accounts. The traditional Individual Retirement Account (IRA) was set up by the US government in 1973 for workers who did not have employment-based pensions and in 1981 extended it to all workers to encourage saving for retirement. Since that time it has gone through many changes and the current 2007 rules allow people to contribute up a maximum of $4000 ($5000 for those over 50 years old) with pretax dollars for those workers who make up to $50,000 for a single filer or Head of Household and $75,000 for a married couple filing a joint return or qualifying widow(er). These amounts change annually and they can be found in the IRS publication 590, Individual Retirement Arrangements (IRAS).


If you withdraw from your IRA before age 59½, you pay a 10% penalty. This is in addition to the regular income tax you would pay on the withdrawal. There are hardship withdrawals that are exempt from this. Check the IRS for these exceptions. You could pay extra taxes if you don’t withdraw the minimum required (according to life expectancy tables) starting age 70½. You can’t borrow from your IRA and you can’t use it as security for a loan.

For these workers who put their money in pretax, a traditional IRA is very similar to a 401K except that the contribution limit for the 401K is much higher at $15,000 and there is no company match. If the worker makes over $50,000, the IRA is still partially deductible up to $60,000 for single filers and $85,000 for married joint filers. Workers who make over these limits can still contribute to a traditional IRA. Why would they do this? The returns on investments are tax deferred until you take the money out.

Different from a traditional IRA, contributions to Roth IRAs are made after tax. Why would anyone want to contribute? Well, the distributions are tax-free. This benefits those who are young and will accumulate large returns on their accounts. The contribution limits are the same as with the traditional IRA. However, those eligible to contribute must be within the income limits of $95,000 for single filers and $150,000 for married filing jointly. There is reduced contribution up to $110,000 for single and $160,000 for married filing jointly. Roth IRAs have another advantage in that they are not subject to minimum distribution requirements. These amounts increase in 2007 and can be changed annually. See website: http://www.irs.gov/publications/p590/ch02.html#d0e8996
Roth IRAs also allow withdrawals without penalty for first-time home buying and qualified educational expenses. Financial planners think that these are winners for people with moderate incomes and low tax brackets.

To see the difference between these retirement saving accounts, let’s take an example of Jill who earns $30,000 a year and is trying to decide whether to put her 6% contribution to a traditional IRA, a Roth IRA or a 401K. Jill’s employer matches 50 cents for every dollar she puts in. Jill will be taking the money out in 30 years as retirement income. She expects an 8% return on average over the 30 years. Her tax rate is 15% right now and she expects to pay 15% in taxes when she retires.

### Comparing a Contribution of $1800

<table>
<thead>
<tr>
<th></th>
<th>Traditional IRA</th>
<th>Roth IRA</th>
<th>401K</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contribution pretax</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Tax savings now</td>
<td>$270</td>
<td>0</td>
<td>$270</td>
</tr>
<tr>
<td>Company match</td>
<td>$0</td>
<td>0</td>
<td>$900</td>
</tr>
<tr>
<td>Total in account</td>
<td>$1800</td>
<td>$1800</td>
<td>$2700</td>
</tr>
<tr>
<td>Value in 30 years at 8% per year</td>
<td>$18,113</td>
<td>$18,113</td>
<td>$27,169</td>
</tr>
<tr>
<td>Taxes due on distribution</td>
<td>$2,717</td>
<td>0</td>
<td>$4,075</td>
</tr>
<tr>
<td>Net distribution</td>
<td>$15,396</td>
<td>$18,113</td>
<td>$23,094</td>
</tr>
</tbody>
</table>

Traditional IRA: Jill’s income level is low enough (less than $50,000) to put money away pretax into a traditional IRA. Her salary for tax purposes is reduced by $1800 to $28,200 so she pays less taxes now. (Her taxes are deferred until she draws the income from the IRA.) If she is taxed at the 15% rate, she saves $270. In 30 years, at 8% return, Jill has $18,113 which will be taxed when she takes a distribution. If tax rates are 15% when she takes the distribution, she pays $2716.95 in taxes netting $15,396.

Roth IRA: Jill’s income level is low enough to put money into a Roth IRA (less than $95,000 for single). Her salary is not reduced so she has no tax savings now. In 30 years, at 8% return, Jill has $18,113 which will be not be taxed when she takes a distribution so she pays $0 taxes, netting $18,113.

401K: Her company matches up to 50 cents for every dollar the employee contributes up to 6% so she gets $900. Her salary for tax purposes is reduced by $1800 to $28,200 so she pays less taxes now. If she is taxed at the 15% rate, she saves $270. Her company matches 3% of $900 so the total contribution is $2700. In 30 years, she will have $27,169 which will be taxed when she takes it out. If her tax rate if 15% when she takes the distribution, she pays $4075 in taxes, netting $23,094.

It’s pretty obvious that If a company matches, 401K is best up to the maximum of the match. After that the Roth IRA looks pretty attractive because the distribution will not be taxed. It is especially attractive if tax rates are low now and you can put away money on an after-tax basis at lower cost. If tax rates increase in the future (as some project they may because of large deficits and the shortfall in social security, then the Roth IRA looks even more attractive. For more information about IRAs, go to the IRS website [http://www.irs.gov/taxtopics/tc451.html](http://www.irs.gov/taxtopics/tc451.html).

**Profit Sharing Plan.**

These plans allow the company to allocate a portion of profits to employee retirement plans usually according to a formula. They’re different from savings plans in that the company contribution may go up and down based on profits. If a company has a bad profit year and is strapped for money, it can contribute less to a profit sharing plan. In 1999, companies contributed about 25% of profits, which came to about 8% of salaries. Some companies contribute in stock. 401K arrangements may be part of these as well. In the Profit Sharing/401K Council of America’s 1999 survey, 53% of saving plans are 401K only.
11% are profit sharing only, while 36% are combined 401K and profit sharing. About 30% of these have immediate vesting, another 32% cliff vesting (meaning you have to have worked the full number of years) after 3, 4, or 5 years, 35% have graduated vesting from 5 to 7 years.

**Money Purchase Plan**
As of 1997, there are 108,000 money purchase plans with 5 million participants, and assets of $141 Billion. Company contributions in these plans are fixed, based on a percent of the employee’s salary. Unlike a profit sharing plan where company contributions can fluctuate, the company must put the required amount in every year.

**Employee Stock Ownership Plan (ESOP)**
This is a retirement plan in which the employer pays into a fund that invests mostly in company stock. This trust is allocated to individual employee accounts, usually based on a percent of compensation and/or years of service. Vesting can happen over a number of years.

These are most popular in closely held companies where retiring owners may be facing unpleasant options in selling or liquidating. The retiring owner can sell the shares (at least 30% of the company) to the ESOP, and there is no taxable gain to the owner. The ESOP can borrow money to buy the shares and the interest is deductible to the company.

The danger with ESOPs is that all the assets are tied up in one stock. But rules allow employees to diversify up to 25% of their account at age 55 and up to 50% at age 60. Distributions are made when you quit, are disabled, or retire.

**SIMPLE IRA**
This is a plan that small employers (including self-employed individuals) can set up for their employees. It is a written plan that allows the employer to contribute and the employee to reduce salary for tax purposes by a certain percent. There are limits on both the salary reduction and the contribution. This plan allows small employers to give retirement benefits akin to the 401K without going through the administrative costs. There are different rules for withdrawals when you retire, and these should be checked before you start a SIMPLE IRA. For more information about IRAs, go to the IRS website http://www.irs.gov/taxtopics/tc451.html.

**SEP-IRA**
An SEP allows an employer to contribute to an employee’s SEP IRA. There are limits on what can be contributed, but they are higher than on other types of IRAs. Your contributions to SEP IRAs are subject to the limits and deductibility rules of traditional IRAs unless your plan was set up before 1996. For more information about IRAs, go to the IRS website http://www.irs.gov/taxtopics/tc451.html.

**Summary Defined Contribution Plans**
1. Unlike defined benefit plans, which end when you or your spouse dies, defined contribution plans have account balances that can go to your heirs. Make sure that you designate a beneficiary for all these plans. In addition, some plans allow you to buy an annuity that will last until you die. But the amount of the annuity will be based on what you have in your account.
2. The most common plan is a 401K.
3. Some of the other plans include:
   a. Profit Sharing Plan
   b. Money Purchase Plan
   c. Employee Stock Ownership Plan (ESOP)
   d. Simple IRA
e. SEP-IRA

**Defined Benefit**

XYZ has a defined benefit plan that gives 1.5% of the highest average five years’ salary for every year of service. Employees vest after 7 years of service. Jill’s highest salary for five years prior to retirement is $45,000, $47,500, $50,000, $52,500, and $55,000.

**Question**

What retirement benefit will Jill salary be if she worked 6 years?

**Answer**

Unfortunately, it would be $0 as she would not have vested.

**Question**

What would Jill’s retirement income be if she worked 20 years?

You first have to take the last five years’ salary and average to get $50,000. Then you apply the formula: Highest average salary X years service X 1.5%. Answer: $50,000 x 20 x 1.5% = $15,000

**Question**

What would Jill’s retirement income be if she worked 10 years?

**Question**

What would Jill’s retirement income be if she worked 30 years?

Jack worked for company XYZ for 20 years. XYZ has a defined benefit plan that gives 1.5% of the highest average five years’ salary for every year of service. Employees vest after 7 years of service. Jack’s highest salary for five years prior to retirement is $345,000, $37,500, $40,000, $42,500, and $45,000.

**Question**

What will Jack’s retirement income be and how does it compare to Jill’s?
Question

What the key actions you should take with your 401K?

Unemployment Insurance

The Federal Unemployment Tax Act (FUTA) imposes a tax on wages and states may add their own tax based on turnover. This tax is used to pay cash benefits to workers who have been terminated from employment. Workers must have earned a certain amount of qualifying wages to be eligible. There is a one week waiting period. The worker must be able and available for work, actively seeking work, and free of any disqualifying event such as quitting voluntarily from a job, discharge for misconduct, refusal of suitable work or being part of labor dispute. Benefits are based on a percent of worker’s earnings over a recent 52-week period. Benefits paid for a maximum of 26 weeks and there may be additional weeks in times of high unemployment.

Discussion

If you have a 401K at work, list all the different funds you can invest in. Which ones do you think are the best?

Activity – Risk Return of Funds

Looking at risk return of asset classes at www.morningstar.com

Here are the funds in the City of Seattle voluntary deferred compensation plan. Look up the risk return of each on Morningstar. Key in the letters for the fund and check under Risk Measures. Mean is the return. Standard deviation is the risk. Draw some conclusions based on your research.

Fixed Income – Government securities LALDX
Fixed Income – Intermediate Bond – PTTRX
Balanced Specialty – VOTVX, VTXVX, VTTVX, VTTHX, VTIVX, VTINX
Large Cap Stock Value – DODGX
Large Cap Stock Blend – VINIX
Large Cap Stock – Growth – RGAEX, CVGRX, CSIEX, FCNTX
Mid Cap Stock Value – LAVLX
Activity – What should you do about retirement savings?

You started a job with a salary of $40,000. Your employer has a 401K plan with a $1 for $1 match up to 6%. What should you do?

Evaluate the difference between putting your money into a traditional IRA, Roth IRA or 401K. For future value in 30 years calculations, use: [http://www.bankrate.com/brm/cgi-bin/savings.asp](http://www.bankrate.com/brm/cgi-bin/savings.asp).

Check out some difference scenarios. What if tax rates are 15% now and 15% in 30 years? What if tax rates are 15% now and 15% in 30 years?

### Comparing a Contribution of $1800

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Activity – Select your 401K

Short Form: Your 401K offers the following options. How would you allocate between these different asset classes if you were 20 years old? How would you allocate between these different funds if you were 60 years old?

Long Form: Complete the asset allocation. Break the class into groups and assign several funds for each to research. Looking up each fund on [www.morningstar.com](http://www.morningstar.com), compare its performance to others in its category in the Category Return page. Students should then choose the best fund in each category.

Money Market Asset Class
- Vanguard Prime Money Market

Fixed Income Asset Class
- Vanguard Short-Term Bond Index
- Vanguard Intermediate-Term Bond Index
- Vanguard Instl. Total Bond Market Index
- PIMCO Total Return

Real Estate Asset Class
- Goldman Sachs Real Estate Securities

Equity Asset Class
- Vanguard Value Index
- Vanguard Institutional Index
- Vanguard Growth Index

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* Fidelity Advisor Equity Growth
* Vanguard Total Stock Market Index
* Vanguard FTSE Social Index
* American Century Equity Income
* Vanguard Mid-Cap Index
* Vanguard Extended Market Index
* Vanguard Small-Cap Value Index
* Vanguard Small-Cap Index
* Vanguard Small-Cap Growth Index

International Equity Asset Class
* Fidelity Advisor Diversified International
* Vanguard Total International Stock Index

Activity - Case Study 401K

You have just been hired at MIT to work 30 hours a week at $18 per hour. Part of your employee benefits is a 401K plan. Read the plan description [http://hrweb.mit.edu/benefits/forms/401k/401k_summary.pdf](http://hrweb.mit.edu/benefits/forms/401k/401k_summary.pdf) and review the guide to the investment options: [http://hrweb.mit.edu/benefits/forms/401k/guide.pdf](http://hrweb.mit.edu/benefits/forms/401k/guide.pdf).

Answer these questions.
Are you eligible to participate in the plan?
What is the maximum you can contribute to the plan?
You are tight on expenses but want to contribute. How much should you contribute?
Describe the main asset categories you can invest in.
How should you allocate your account between these asset categories?
How should you select the funds?

Unit 6: Risk Management in your 50s and 60s

Disability Income Insurance

Disability strikes one in four workers before age 65. The financial impact of disability can be disastrous. According to the US Department of Housing and Urban Development, 46% of conventional mortgage foreclosures were attributed to disability and only 2% to death. According to research by the U.S. Department of Education and the National Institute on Disability and Rehabilitation, the most common causes of long-term disability are heart disease, back injuries, and cancer, followed by anxiety and depression.

Disability Insurance is a form of insurance coverage that provides a portion of income lost as the result of a total or partial disability caused by either an accident or an illness. This is different from a short term illness which would be covered by sick leave. Other sources of income if you are disabled include social security and disability plans available through your employer. Before you purchase disability insurance, you should make sure that you are not covered under your employer.

Disability Income Through Employers

Disability is more prevalent than most people realize. It costs account for 6% to 12% of payroll. One out of 7 people become disabled for 5 or more years before reaching age 65. Three out of 10 workers are disabled for 90 days or more. 11.6% people aged 16-67 had a work disability. 5% have disability that prevents them for working.

Social Security Disability
Disability is defined for social security purposes means that the employee is so severely impaired, mentally or physically, that she cannot perform any substantial gainful work. It must last for continuous period. You can check on the social security website to determine if you qualify [http://www.ssa.gov/dibplan/dquality4.htm](http://www.ssa.gov/dibplan/dquality4.htm). If a worker is determined to be disabled, he or she receives a monthly benefit equal to primary insurance amount at the time disability occurred. The worker has to have 20 credits. The waiting period is five full calendar months prior to receiving any benefits. As of 2004, there were 6.2 million disabled workers and 1.8 million dependents were receiving an average month benefit of $862.

**Workers’ Compensation**
Workers compensation pays for medical care and offers cash benefits for workers who are injured on the job or who contract work-related illnesses. In 2002, $53.4 billion in workers’ compensation ($24.3 B medical care and $29.2 B cash benefits) were distributed to these folks. There is a waiting period of 3 to 7 days for these benefits.

Cost of workers’ compensation was declining between 1990 and 2000 due to better management of health care costs, stricter eligibility and better prevention.

**Short-term disability**
Short term disability can be equated to sick leave or paid time off for sickness. 70% of private employers offer short-term disability which usually covers 100% of wages for a few weeks.

**Long-term disability**
Only about 25% of private employers offer long-term disability benefits. Long-term disability provides cash benefits to cover for lost wages in the event of disability. The eligibility for long-term disability may be the same as for social security. There is typically a waiting period of 3 to 6 months. Long-term disability is generally designed to replace 60% of earnings and will be reduced by other benefits such as workers compensation and social security disability payments.

**Purchasing Disability Income Insurance**
This kind of policy can have many exclusions and limits. The insurance company will review your medical and financial histories before they offer you coverage. The older you are, the more the premium will cost. Women pay more because they are disabled at higher rates than men. If you are in a low risk occupation, you will pay less.

Disability insurance can be purchased on an individual or group basis. It is usually less expensive to purchase as part of a group. Professional associations or other groups may offer coverage. Most insurance companies will issue disability insurance coverage equal to approximately 50% to 60% of your earnings. The definition of disability is the most important aspect of a disability policy. You can be covered in the event of disability for your occupation or it can be the more restrictive definition of any occupation which you are reasonably suited to by your education, training or experience.

The renewability provision is one of the key features of an individual disability income insurance policy. This provision defines your rights when it comes to keeping your disability policy in force. If you purchase a policy that is Non-Cancellable and Guaranteed Renewable, the insurance company cannot cancel, increase your premiums, change any provisions or add restrictions to the policy -- even if the issuing company no longer offers similar policies in the future. For more information on this, check out [http://www.mdtaxes.com/disability_insurance.html](http://www.mdtaxes.com/disability_insurance.html).

**Key factors to consider**
Determine whether you want coverage for your current occupation or any occupation for which you are reasonably qualified by training, experience, and education. Some insurance companies may cover your own occupation for one to two years and then switch to any occupation.

You need to determine what percent of your earnings you want to cover with the policy. Most commonly they will pay 50% to 60%. Consider all your main monthly costs - mortgage payments/rent, food, utilities and transportation and add medical costs due to your disability. You may get disability income from other sources so you should check to see what you will get from social security. Some policies cover total disability. Others cover partial disability.

If you purchase your own policy, your disability income is not subject to income tax. If your employer pays, you will have to pay income tax.

Some policies have premiums that stay the same or that increase as you age. If you plan to keep the policy for a long period of time, a level premium policy is the better choice.

Policies have different waiting periods before you begin receiving benefits. You can choose 90 days, 6 months or longer. The longer the waiting period, the lower the premium. Check to see if you have a relapse whether you will still have a waiting period.

The period of time you receive the benefits can be a number of years or until you are 65.

You may want a cost-of-living adjustment to cover your earnings over time.

Determine whether you want noncancellable and guaranteed renewable policy where the premiums will never be increased and the policy cannot be canceled.

Make your check payable to the insurance company not the agent and get a receipt.

After purchasing the policy, you may have a “free-look” period (usually 10 days after you receive the policy) to change your mind. If you decided to cancel, the company will give you a full refund.

If you have a complaint, contact the Washington state Insurance Commissioner at www.insurance.wa.gov.

<table>
<thead>
<tr>
<th>Company Name:</th>
<th>Company Name:</th>
<th>Company Name:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contact Information</td>
<td>Definition of disability (own or any occupation)</td>
<td>Elimination period before benefits start</td>
</tr>
<tr>
<td>Length of benefit period (years or to age 65)</td>
<td>Benefits for partial disability</td>
<td>Percent of lost income replaced (typically 60%)</td>
</tr>
<tr>
<td>Return to work programs</td>
<td>Recurrent disability what happens if I return to work and then relapse</td>
<td>Cost of living</td>
</tr>
</tbody>
</table>
Question:
What is Disability Income Insurance?

Life Insurance

The classic and best reason for an individual to buy life insurance is for protection against dying too soon. The person buying life insurance should be primarily concerned with seeing that his or her survivors do not face financial hardship. Life insurance is also purchased to pay estate taxes. Business relationships often require life insurance or can benefit from it, for example. Annuities offer a secure way for consumers to make sure they don't outlive their money. Beware of anyone who tries to sell you life insurance as an “investment.” Life insurance should be purchased for the protection it will give you.

The following questions help you determine how much you need.
How much do I provide for my dependents for how many years? This includes children, parents and others who depend on you for financial support.
Do my children have college tuition needs that I have to provide for?
Are there family members or organizations that I want to leave money to?
Will there be estate taxes that have to be paid when I die?
Will there be funeral arrangements that have to be paid when I die?

Total up your assets and other sources of death benefits such as social security and life insurance provided by your employer. This will give you an indication of how much life insurance you need.

Term life insurance

Most consumer advocates feel that term insurance is the best life insurance buy. Term life insurance is different from "whole life" or "ordinary life" in that you build up no equity, or cash value. You pay each year for the cost of insurance, which typically increases annually as your chances of being alive the next year decline. Most term policies are renewable on an annual basis, and some have level premiums or a decreasing death benefit for a stated period -- one, five or ten years, or even to a specified age.
Permanent life insurance

The second type is permanent life insurance, which goes by several names, such as universal life, variable universal life and whole life. Permanent insurance may provide long-term financial protection. These policies include both a death benefit and, in some cases, cash savings. Because of the savings element, premiums tend to be higher.

A number of factors affect life insurance premiums. Of those factors under your control, you should take action to improve them if you can. Others are a function of your genetics, occupation or location. Either way, it's important for you to be educated on these issues so that you can make the best insurance decisions to fit your life.

<table>
<thead>
<tr>
<th>How it affects your premium</th>
</tr>
</thead>
<tbody>
<tr>
<td>Coverage you require</td>
</tr>
<tr>
<td>Life insurance is typically purchase to cover for those who are dependent on your income. Most consumer groups suggest that if you are single with no dependents, you don’t need life insurance.</td>
</tr>
<tr>
<td>Age</td>
</tr>
<tr>
<td>The older you are, the more expensive the premiums</td>
</tr>
<tr>
<td>Overall health</td>
</tr>
<tr>
<td>Life insurance companies typically ask you about your medical history, request access to medical records and even obtain samples for testing. Pre-existing and/or chronic health problems, such as diabetes, heart disease, cancer or sexually transmitted diseases may prevent you from getting life insurance or place you in a high-risk pool at greater cost.</td>
</tr>
<tr>
<td>Poor health habits</td>
</tr>
<tr>
<td>Poor health habits, such as smoking and excessive drinking. Be aware that insurance companies may look back and consider these behaviors for the past five years.</td>
</tr>
<tr>
<td>Dangerous sports</td>
</tr>
<tr>
<td>Engaging in dangerous sports such as skydiving, skiing or rock climbing may raiser your premiums.</td>
</tr>
<tr>
<td>Driving pattern</td>
</tr>
<tr>
<td>Your driving record, in terms of accidents can have an impact on your risk. The better your driving record, the better rates you’ll receive for your life insurance.</td>
</tr>
<tr>
<td>Geographic area</td>
</tr>
<tr>
<td>Life insurance companies have access to regional data that document mortality rates and life expectancy, and they use that data to calculate the rates they offer.</td>
</tr>
</tbody>
</table>

Shopping for Life Insurance

Life insurance is a competitive marketplace, and much of the competition focuses on price. Don't hesitate to seek premium quotes from several different companies. Determine what you need before you shop. Then you will be less susceptible to persuasive tactics. If term insurance fits, that's what you should shop for. If you want to lower your premium at all costs, you may want to consider using a direct writer, a company that cuts costs by operating without agents.

If you want to buy more complicated products such as whole life or universal life in which your benefits are dependent on stock market returns, make sure you understand how all components work. Don't buy anything you don’t understand. Most consumer advocates believe that term life is all you need to cover your needs. It gives you the most benefits for the cost. On more complicated products, consider what happens if you need to get money out for any reason. Ask the agent about what penalties there are for doing this.
Update your coverage as your circumstances change. As your children grow and go on their own, they won’t be dependent on you anymore. Don’t be misled by someone who tells you should buy additional policies for children as they are born. Children rarely have an income and seldom require life insurance. Your net worth every few years and reconsider the prospects your survivors may face if you die.

Fraud and bad advice happens when consumers buy life insurance, just as it happens with other financial products. Some life insurance policyholders in recent years have fallen victim to a practice called “churning.” Churning happens when your coverage is changed so the agent or broker gets a commission but you lose out. People with cash-value policies are persuaded to convert their coverage to another policy with a promise of better benefits. The problem is that the cash value of the original policy is raided in order to pay for the new policy. Luckless consumers may not realize until years later that they have actually lost out.

Never buy a policy you don’t understand. If your agent or company cannot explain the policy terms to your satisfaction, shop elsewhere. Make sure you understand the guarantees in your policy, any fees that are charged, and the surrender penalties if you choose to drop the policy at any time. Costs are often hidden in the policy. Ask for full disclosure of all fees. Get everything in writing and don’t depend on the agent’s promise of returns.

Essay Question:
Explain “churning” in life insurance.

Caring for Your Parents

More and more baby boomers are find that in addition to the care of their children, they may also be responsible for the care of their parents as they both age. It is estimated that about 34 million people care for their parents. According to the survey conducted by the National Alliance for Caregiving, people spend on average $5,500 out-of-pocket to take care of their parents. This sum can amount to 10% of the family’s income. In addition, folks are spending at least 5 hours a week caring for parents.

Often in cases where more care is needed, children may, if they can get it, buy long term care insurance for their parents. This prevents the children’s assets from being depleted in caring for a parent’s incapacitation.

Medicare

The federal healthcare program for elderly and disabled is Medicare. In 2006, it cost $317.7 billion and covered 35.4 million elderly and 6.3 million disabled. Workers over 65 who are eligible for Social Security and their eligible spouses are the elderly covered by the plan. A lot of information is available on Medicare at their website: www.medicare.gov. There are three parts to Medicare:

- Part A: Inpatient hospital care – paid by current workers and employers through payroll tax of 2.9% split between employee and employer.
Part B: Outpatient services – Those eligible for medicare pay a monthly premium of $206 to $375 in 2006. The balance (three fourths of the cost) is paid by the government.

Part D: Prescription drugs was made available to those eligible in 2006 for a monthly premium of $35.

You may have your choice of Medicare plans and it’s important to choose the right plan for you. The AARP has a good primer on Medicare at http://www.aarp.org/health/medicare/. It is important to note that Medicare will not cover all your healthcare needs when you retire. Experts estimate that you will need $160,000 in savings to cover your health-care needs, including insurance premiums and any out-of-pocket medical expenses if you retire at age 65. This doesn’t include any long-term care costs such as living in a nursing home. If you retire early, you'll need more.

Long Term Care Insurance

Long-term care insurance can cover medical and/or non-medical support services used during a prolonged illness, disability or loss of mental capacity. Different from Disability Income Insurance, it is not used to protect your income that would be used for mortgage or care of your family. This insurance would cover care for you when you are no longer able to perform the daily activities of living such as bathing, dressing, eating, toileting, transferring or continence. It may also include grocery shopping, laundry, meal preparation, managing medications, transportation, or various types of medical therapies.

Sometimes, family members take on the burden of caring but this can impact their financial situation if employment has to be given up to care for a loved one. Long-term care can be provided in a variety of settings including one’s own home, adult or group family homes, assisted living facilities, nursing homes and continuing care retirement or other community settings.

Often people who do not have this insurance and who have no assets to protect may qualify for low-income assistance through Medicaid to pay for such services. Individuals generally pay for long-term care services out of pocket. The monthly costs for long-term care range from a few hundred dollars for chore assistance to several thousand dollars for skilled nursing care.

In Washington and many other states, the rapid rise of the state’s senior population is expected to strain the resources of individuals, families, and government at all levels over the next 30 years. Long-Term Care insurance is gaining importance among baby boomers as an option to meet future health expenses not covered by traditional health insurance.

Most major medical health insurance policies do not cover long-term care expenses, nor does Medicare or Medicare Supplement insurance. Long-term care insurance is about the only option that allows people to protect their assets and retain more control over their health-care decisions in this late-life situations. Those who do not have this preparation often have few alternatives but to spend down their assets until they qualify for Medicaid.

As you might expect, the cost of Long-Term Care insurance varies according to the amount of coverage you buy, the options selected, and -- most of all -- your age at the time of purchase. Premiums may also increase over time.

Most people consider long-term care insurance when they are in their 50s. Long-term care insurance gets more expensive as you get older. Be sure you can afford it. You should look at all of the options, and you should beware of zealous sales representatives. If you feel you are being pressured unfairly or not being treated properly, contact the Insurance Commissioner by calling the toll-free Consumer Hotline, 1-800-562-6900.
Long term care insurance is right for you if you have assets to protect, can afford the premium, are not currently disabled, want to ensure control over your assets, don’t qualify for Medicaid and you want to protect your family from having to provide the care.

It may not be right for you if you have few assets, can’t afford the premium, are already disabled, qualify for Medicaid, have other insurance, have enough assets so you can set aside the money for care yourself or have no family or causes you want to bequeath your assets to.

In considering long term care insurance, the worst case scenario is requiring skilled nursing care in a nursing home for a long period of time. Nursing homes cost $186 per day in Washington State. Check out the AARP site to find the most recent data [http://www.aarp.org/bulletin/longterm/Articles/a2003-10-30-dailycost.html](http://www.aarp.org/bulletin/longterm/Articles/a2003-10-30-dailycost.html). That can run you close to $70,000 a year. A few years of those expenses can deplete your assets. However, long term care insurance is expensive. It can cost $3000 per year for a 50-year-old and $5000 per year for folks in their 60s. It is recommended for those who have assets over $150,000 and who make $50,000 to $75,000 a year.

When shopping for long term care insurance, the Texas Department of Insurance ([http://www.tdi.state.tx.us/](http://www.tdi.state.tx.us/)) gives this advice:

- **What types of care are covered and in what setting?** Policies can offer a full range of services, including home health care, adult day care, assisted living facility care, and nursing home care. Policies are required to cover all levels of care from custodial to intermediate to skilled care.
- **What are the benefit eligibility requirements?** Policies won’t pay until you’ve satisfied certain requirements, such as being unable to perform tasks called Activities of Daily Living or being certified as cognitively impaired. The benefit eligibility triggers may vary from policy to policy.
- **How much is the daily benefit amount for each type of benefit?** Most policies will pay a maximum daily amount for your care. You will pay the difference between the maximum daily benefit and the actual cost. It’s important that you choose your benefit amount wisely. To keep premiums down, you could plan to pay some of the cost yourself. But you have to make sure that you have the funds to cover for this.
- **How long will benefits be paid?** The chances of needing long-term care for more than five years are relatively small. For most people, a policy covering three to five years is appropriate and more cost-effective. However, if your primary concern is protection if you get Alzheimer’s disease, which can last a long time, you may want to consider the more costly option of lifetime coverage.
- **Does the policy have a pre-existing condition waiting period?** If so, how long is it? Some policies won’t cover a pre-existing medical condition until after a certain period of time has elapsed. Some policies will pay for care related to a pre-existing condition immediately if you disclosed the condition on your application.
- **What inflation protection is offered?** Inflation protection helps ensure that you have adequate coverage in the future. All companies must offer an automatic increase in benefits at the rate of 5 percent compounded annually. If you reject inflation protection, the rejection must be in writing. The company also may have other options for protecting you from inflation. Be aware that to beat inflation, you’ll either have to pay a higher premium today, or higher out-of-pocket costs later.
- **What is the nonforfeiture benefit?** All companies must offer you a nonforfeiture benefit. If you reject the nonforfeiture benefit, the rejection must be in writing. If you cancel or lapse your policy after a specified number of years, the insurance company will either return a percentage of the premiums you paid; extend benefits for a period of time equal to the premiums paid, less any claims; or provide a greatly reduced benefit.
- **Is the policy tax-qualified?** If you buy a tax-qualified policy, you can deduct part of the premiums you paid as a medical expense on your income taxes. Benefits paid from a tax-qualified policy are generally not considered taxable income. The policy must disclose if it is intended to be tax-qualified or non tax-qualified.
• Can I upgrade the policy later by purchasing more benefits? Some companies allow you to upgrade your policy after purchase. However, you will likely have to complete and submit a new medical questionnaire.
• Is the company financially sound? A company's financial rating by an independent rating service is a helpful indication of the company’s overall financial strength.
• Does the company have a good track record for customer service? The number of consumer complaints against a company is a good indication of the company's customer service record.
• Is it licensed? Licensed companies belong to a guaranty association that will pay your claim if your insurance company goes broke. If you buy from an unlicensed company and have a claim, it might go unpaid.
• Does the agent specialize in long-term care insurance? Because of the many variations in long-term care policies, having an agent with knowledge and experience can help you choose the right coverage for your needs.
• What is the company's 10-year history of rate increases? While past increases are predictor of future increases, you may want to take the rate history into consideration.

Remember, you have a 30-day “free look” period to review your long-term care policy after you receive it.

**Long Term Care Evaluation Form**

<table>
<thead>
<tr>
<th>What kind of care is covered?</th>
<th>Home health care, adult day care, assisted living care, nursing home care</th>
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<tr>
<td>Eligibility requirements?</td>
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<td>Maximum daily benefit?</td>
<td>How does it compare with daily nursing home costs in your area?</td>
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<td>How long will benefits be paid?</td>
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<td>How are pre-existing conditions dealt with?</td>
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<td>How is inflation dealt with?</td>
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<td>What is the nonforfeiture benefit? All companies must offer this.</td>
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<td>Tax benefits?</td>
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<td>Opportunity to upgrade?</td>
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<td>Financial rating of company?</td>
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<td>Complaint record?</td>
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<td>Licensed company?</td>
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<td>Experienced agent?</td>
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<td>10-year history of rate increases?</td>
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<tr>
<td>Deductible</td>
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</table>
Question:
How long do you have for a 30-day “free look” period to review your long-term care policy after you receive it?

Activity – Discuss your health care needs in retirement.
Discuss what your health care needs will be when you retire. Determine what Medicare will cover. Check out gap insurance. How much will you be paying for health care when you retire? Discuss stories of retired people you know.

Activity – What is the cost of long term care in your area?
What is the cost of long term care? Find prices in your area. Check out the AARP website: http://www.aarp.org/families/caregiving/guide_to_longterm_care.html

Activity – Discuss whether you need disability insurance.
Do you need disability income insurance? What factors should you consider?

Assignment – Long Term Care
Determine whether you want coverage for your current occupation or any occupation for which you are reasonably qualified by training, experience, and education. Some insurance companies may cover your own occupation for one to two years and then switch to any occupation.

You need to determine what percent of your earnings you want to cover with the policy. Most commonly they will pay 50% to 60%. Consider all your main monthly costs - mortgage payments/rent, food, utilities and transportation and add medical costs due to your disability. You may get disability income from other sources so you should check to see what you will get from social security. Some policies cover total disability. Others cover partial disability.

If you purchase your own policy, your disability income is not subject to income tax. If your employer pays, you will have to pay income tax.

Some policies have premiums that stay the same or that increase as you age. If you plan to keep the policy for a long period of time, a level premium policy is the better choice.

Policies have different waiting periods before you begin receiving benefit. You can choose 90 days, 6 months or longer. The longer the waiting period, the lower the premium. Check to see if you have a relapse whether you will still have a waiting period.

The period of time you receive the benefits can be a number of years or until you are 65.

You may want a cost-of-living adjustment to cover your earnings over time.

Determine whether you want noncancellable and guaranteed renewable policy where the premiums will never be increased and the policy cannot be canceled.
<table>
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<tr>
<th>(own or any occupation)</th>
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<tbody>
<tr>
<td>Elimination period</td>
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<td>before benefits start</td>
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<tr>
<td>Length of benefit period</td>
<td>(years or to age 65)</td>
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<td>Benefits for partial disability</td>
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<td>Percent of lost income replaced (typically 60%)</td>
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<td>Return to work programs</td>
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<td>Recurrent disability</td>
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<td>what happens if I return to work and then relapse</td>
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<td>Cost of living adjustment</td>
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<td>Mental health/substance abuse provisions</td>
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<tr>
<td>Noncancellable or guaranteed renewable</td>
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<tr>
<td>Exclusions or other limitations.</td>
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</tbody>
</table>


## Sources

Employee Benefit Research Institute [www.ebri.org](http://www.ebri.org)
The Health and Retirement Study [http://hrsonline.isr.umich.edu/docs/sho_ref.php?hfyle=index&xtyp=7](http://hrsonline.isr.umich.edu/docs/sho_ref.php?hfyle=index&xtyp=7)
Health Research and Educational Trust [www.hret.org](http://www.hret.org)
The Kaiser Family Foundation [www.kff.org](http://www.kff.org)
National Association of Insurance Commissioners [http://www.insureonline.org/index.htm](http://www.insureonline.org/index.htm)

## Glossary

**401(K) Plan** — A tax-deferred savings plan that allows an employer to match employee deposits into the account up to 100%. Earnings accumulate tax-deferred until they’re withdrawn.

**Actual Cash Value** — A form of insurance that pays for damages equal to the replacement value of the damaged property minus depreciation.

**Adjuster** — An individual employed by a property/casualty insurer to evaluate losses and settle policyholder claims.
Admitted Company — An insurance company authorized and licensed to do business in a given state.

Age Limits — The ages below or above which the insurance company will not issue a given policy or renew a policy in force.

Agent — Any person appointed by an insurer to receive applications for insurance on its behalf.

Annual percentage rate (APR) — Yearly interest rate charged on a credit account.

Annuity — Life insurance that pays periodic income benefits for a specific period of time or over the course of the beneficiary’s lifetime.

Appraisal – A survey to determine a property’s insurable value, or the amount of a loss.

Basic Health (BH) — This plan was created in 1987 to provide low-cost, limited benefits in high unemployment areas of the state. Under the 1993 Health Services Act, the BH was expanded to statewide and its benefits were improved.

Beneficiary — A person eligible to receive benefits under an insurance policy.

Benefit Package — Also known as a Benefit Schedule. The list of covered services offered by an HCSC, HMO or insurance plan.

Broker — An intermediary between a customer and an insurance company. Brokers typically search the market for coverage appropriate to their clients.

Cancellation — Voluntary termination of a contract by the insurance company or the insured. Cancellations must be carried out according to the terms of the contract or by mutual agreement.

Case Management — Coordination of patient care to ensure appropriate care and reductions in costs of providing services. Physician case managers coordinate such elements as referrals to consultants, specialists, hospitals, ancillary providers and services. This is intended to eliminate misutilization of facilities and resources, fragmented services and to provide continuity of services and intensity of services appropriate to the patient’s needs over time.

Cash Value — The amount that the owner of a permanent life insurance policy is entitled to receive if the policy does not remain in force until the insured’s death.

Claim — The demand for benefits as provided by the policy.

COBRA — Short for Consolidated Omnibus Budget Reconciliation Act. A federal law that requires employer-sponsored group health plans to offer continued coverage to employees who leave their jobs.

Collision Coverage — A portion of an auto insurance policy that covers the damage to the
policyholder’s car from a collision. This is a part of most automobile insurance policies.

**Commission** — Fee paid to an agent or insurance salesperson as compensation for sales, service, and distribution of insurance policies.

**Comprehensive Coverage** — That portion of an auto insurance policy that covers damage to the policyholder’s car that did not result from a collision with another car (e.g. damage from fire, explosions, earthquakes, floods, riots and theft.)

**Comprehensive Health Insurance** — Sometimes called "Comprehensive Major Medical." A form of health insurance that combines the coverage of Major Medical and Basic Medical Expense contracts into one broad contract that provides coverage for almost all types of medical expense with few internal limits, usually subject to a small deductible for some or all expenses and to a percentage participation clause (sometimes called "co-insurance") applicable to all or some of the covered expenses.

**Coordination of Benefits (COB)** — This determines the amount payable by each insurer when the claimant is covered under two or more group health plans. Total reimbursement should not exceed 100 percent of the cost of care.

**Co-Payment** — A co-payment is a patient's share of a health-care bill. It usually is a small amount - $5 or $10 per office visit. Health-care reform advocates say its primary function is to remind consumers that health care is not free - and to discourage them from seeking unnecessary care.

**Cost Sharing** — The general set of financing arrangements whereby the consumer must pay out-of-pocket to receive care, either at the time of initiating care or during the provision of services, or both. This also can occur when an insured pays a portion of the monthly premium for his health insurance.

**Coverage** — Scope of the protection provided under a contract of insurance.

**Deductible** — The part of the insured's expenses or loss that must be paid before insurance coverage begins.

**Deferred Annuity** — An annuity whose benefits begin at some designated future date (as contrasted to an annuity where benefits begin at once, called an IMMEDIATE annuity).

**Defined Benefit Plan**—A pension plan that provides the retiree with a lifetime of income.

**Defined Contribution Plan**—A health benefit plan that allows employees to make contributions to their own retirement savings accounts. Employers may or may not match contributions.

**Direct Writer** — An insurance company which sells its policies through salaried employees (licensed agents) who represent it exclusively, rather than through independent local agents, who represent more than one company.

**Disability Income Insurance** — A form of health insurance that provides periodic payments to replace
income lost when the insured is unable to work as a result of sickness or injury.

**Elimination Period** — A loosely-used term sometimes designating the "waiting period" and sometimes the "probationary period."

**Endorsement** — A written form attached to an insurance policy that changes the policy’s coverage, terms to fit special circumstances.

**ERISA** — The Employee Retirement Income Security Act of 1974. This law, which dealt primarily with pensions and retirement plans, includes a section exempting self-funded employer and union health plans from state regulation. Washington’s health-care reform law - the Health Services Act of 1993 - required a congressional waiver of this law so that the state could mandate employer-provided health coverage. The waiver did not pass, and the state law was subsequently changed.

**Exclusion** — A provision in an insurance policy that eliminates coverage for certain risks, people, property classes, or locations. Clauses in a health insurance contract that deny coverage for certain conditions, treatments, supplies or risks, such as acts of war. In property and casualty contracts, certain events or circumstances also may be excluded from coverage.

**Exclusive Provider Organization** (EPO) — A managed care organization similar to PPOs in that physicians do not receive capitated payments, but members may only choose medical care from network providers. A patient seeking care outside the EPO network would not be reimbursed for the cost of that treatment. See also Group Model HMO.

**Experience** — The loss record of an insured, a class of coverage, or of an insurance company.

**Fee** — A charge or price for professional services.

**Fee-for-Service** — The traditional payment method in U.S. health care, when patients pay doctors, hospitals and other providers for the services rendered at the time of that service, and then seek reimbursement for those costs from their private insurers or the government, if eligible for such a program (e.g. Medicare). The patient is charged according to a fee schedule set for each service and or procedure provided.

**GAP Insurance** – An automobile insurance option that covers the difference between a car’s actual cash value when it is stolen or wrecked and the amount the consumer owes the leasing or finance company. Mainly used for leased cars.

**Grace Period** — A period of time (commonly 30-31 days) after premium-due date during which a policy remains in force without penalty even though the premium due has not been paid.

**Group Insurance** — Insurance policy or health services contract covering a group of employees (and often their dependents) under a single contract issued to an employer or other group by an HCSC, HMO or other insurer.

**Group Model HMO** — There are two types: closed panel and the contract model. Closed panel HMO
deliver medical services in the HMO's health center or clinics by providers who belong to a legally separate medical group paid a negotiated monthly capitation fee. Its providers are salaried and generally prohibited from carrying on any fee-for-service practice. In the second type, the HMO contracts with an existing independent group of physicians to deliver medical care at their facilities to HMO members for a prepaid fee. Such a medical group may also offer health services on a fee-for-service basis. The medical group generally contracts with more than one HMO.

Guaranty Fund — The way that insurers ensure that some of the policyholder and third-party claims against failed or bankrupt insurance companies are paid.

Health Care Financing Administration (HCFA) — The U.S. Department of Health and Human Services (DHHS) agency renamed to the Centers for Medicare and Medicaid Services (CMS) that administers federal health financing and related regulatory programs, principally Medicare, Medicaid, and Peer Review Organization programs. The contracting agency for HMOs that provide Medicare managed care plans.

Health Insurance — Insurance against loss by sickness or bodily injury.

Health Maintenance Organization (HMO) — A legal entity in Washington state that provides health care in a geographic area, and which accepts responsibility to provide directly or by contract an agreed-upon set of health services to a defined, voluntarily-enrolled group of individuals. HMOs are reimbursed through a pre-determined, fixed, periodic prepayment made by or on behalf of each subscriber without regard to the amount of actual services provided. (In other states, HMOs are regarded as synonymous with "managed care." However, in Washington state other kinds of health carriers also may employ managed care.)

Health Plan — A generic term referring to a specific benefit package offered by an insurer.

High Risk Pool — A non-profit entity called the Washington State Health Insurance Pool, created by state law in 1987, to provide access to health insurance to all residents of Washington who are denied adequate health insurance for any reason. (RCW 48.41) The premium is limited 150 percent of the average group premium charged in the marketplace or 125 percent of the average group premium if the health plan is managed care. An assessment on health insurers operating in the state, based on the number of individuals each carrier covers, provides any subsidy needed.

Homeowner Policy — A "package" or multi-line policy providing the protection needed by most homeowners. The policy provides property insurance, including theft, with very broad coverage on both the building and the contents. Liability insurance is also provided.

Hospital Benefits — Benefits payable when an insured is hospitalized.

Indemnify — To restore the victim of a loss, in whole or in part, by payment, repair, or replacement. (To this definition, the Commission on Terminology adds the following comment: "To the extent that the obligation of the insurer is to do other than make good losses, the insurance contract is not one of indemnity. The term indemnity or indemnify should not be used to apply to an obligation other than to make good loss.")
**Individual Market** — The portion of the health insurance industry consisting of individuals and their dependents who purchase coverage directly from a carrier - approximately five percent of the entire market. Those in the individual market usually buy their own coverage because they are not eligible for employee-sponsored or government coverage, such as Medicare, Medicaid or the Children's Health Insurance Program (CHIP).

**Insurance Commissioner** — The elected state official with the authority to enforce the provisions of the state's insurance code and to make reasonable rules and regulations to implement provisions of the code; to conduct investigations, examinations and hearings related to those enforcement activities.

**Insurance Policy** — Broadly, the entire written contract of insurance. More narrowly, the basic written or printed document, as distinguished from the forms and endorsements added thereto.

**Insured** — The party to an insurance agreement to whom, or on behalf of whom, the insurance company agrees to indemnify for losses, provide benefits, or render service. (To this definition the Commission on Terminology adds the comment: "Like Insurer, the term Insured is functional and unmistakable. Therefore, it is preferred to such terms as Policyholder.") In pre-paid hospital service plans, the insured is called the subscriber.

**Joint Life Policy** — Pays the insurance when the first of two or more covered persons die.

**Lapse** — The termination of an insurance policy because a renewal premium is not paid by the end of the grace period.

**Liability Insurance** — Insurance for what the policyholder is legally obligated to pay because of bodily injury or property damage caused to another person.

**Liability Limits** — The sum or sums beyond which a liability insurance company does not protect the insured on a particular policy, similar to limit of liability.

**Life Insurance** — Insurance on human lives including endowment benefits, additional benefits in event of death or dismemberment by accident or accidental means, additional benefits for disability, and annuities.

**Limitations** — Exclusions, exceptions, or reductions of coverage contained in an insurance policy.

**Limits** — (1) Maximum amount of benefit payable for a given situation or occurrence. (2) Ages below or above which the insurance company will not issue new policy or above which it will not continue a policy in force.

**Long-Term Care Insurance** — Long-term care insurance pays for services to help individuals who are unable to perform certain activities of daily living without assistance, or require supervision due to a cognitive impairment such as Alzheimer’s disease.
**Long-Term Disability** — (1) A disability having a duration longer than a short-term disability, the exact duration being variable and a matter of reference; more commonly anything longer than 90 days. (2) A form of group disability insurance paying benefits for more than the customary 13 to 26 weeks; more commonly, benefits of five years’ duration or more, but again depending on terms of reference.

**Loss** — A reduction in the quality or value of a property, or a legal liability. Loss can also refer to payments made on behalf of the insured.

**Major Hospitalization Policy or Insurance** — A type of health insurance that provides benefits for most of the costs of hospitalization up to a high limit, subject to a large deductible. Such policies may contain internal maximum limits and percentage participation clauses. They are distinguished from major medical by the fact that they pay only in event of hospitalization.

**Major Medical Insurance** — A type of health insurance that provides benefits for most types of medical expenses incurred up to a high limit, subject to a large deductible. Such contracts may contain internal limits and a percentage participation clause (sometimes called co-insurance clause). A major medical policy pays expenses both in and out of the hospital.

**Managed Care** — Managed care is a philosophy of health care coverage that streamlines health services and creates a health-care system that includes both the financing and delivery of services to the consumer. It also takes more responsibility for maintaining subscribers' health, not just curing them once they are sick. It lowers costs by matching the patient with appropriate care as efficiently as possible. Different insurance carriers use different kinds of managed care. Although the philosophy is popularly associated with Health Maintenance Organizations (HMOs), other kinds of carriers also employ it.

**Mandated Benefits** — Washington state law requires certain benefits be included in any major medical coverage. These include mammograms, automatic coverage of newborn or adopted children, home/hospice treatment options, and others as required by the Legislature.

**Market Share** — That part of the market potential a company has captured, usually expressed as a percentage of the market potential.

**Maturity** — The date at which the face amount of a life insurance policy comes due either by reason of death or endowment.

**Maximum Allowable Charge** — The amount set by the insurer as the highest amount to be charged for a particular medical service.

**Medically Necessary** — Covered services required to preserve and maintain the health status of a member or eligible person in accordance with the area's standards of medical practice.

**Medicare Supplement** — Voluntary private insurance coverage purchased by Medicare enrollees covering the cost of services not reimbursed by Medicare.

**Medicare** — The federal healthcare program for the elderly and disabled. Workers over 65 (and their
spouses) who are eligible for social security benefits are covered by the program.

**Member** — Enrollee, beneficiary, insured. Includes those enrolled or subscribed to a health insurance plan and their eligible dependents.

**Nonforfeiture Benefit** — The various ways in which a contract owner may apply the cash value of an insurance or an annuity contract if the contract lapses.

**Open Enrollment** — A period of time when eligible subscribers may enroll in, or transfer between available programs providing health care coverage. Federal HMO regulations require that HMOs which meet certain criteria conduct annual open enrollments for periods of not less than 30 days.

**Ordinary Life** — (1) All life insurance policies not classifiable as Industrial or Group. (2) A continuous premium, whole life policy (also sometimes called Straight Life).

**Out-of-Area Services** — Services received by insurance plan enrollees when they are outside their plan's established geographic area of service as defined in the contract and service agreement. Usually not covered unless a delay would adversely affect the member's health.

**Outpatient Services** — Medical and other services provided by a hospital or other qualified facility, such as a mental health clinic, rural health clinic, mobile X-ray unit or free-standing dialysis unit. Those services include physical therapy, diagnostic X-ray and laboratory tests.

**Participating Provider** — A provider who has contracted with a health care service contractor, HMO, PPO, IPA or other managed care organization to provide health care.

**Personal Injury Protection (PIP)** — Portion of an auto insurance policy that covers the treatment of injuries to the driver and passengers of the policyholder's car. It provides coverage for bodily injury, loss of wages, burial expenses and for household services expenses.

**Point-of-Service Plan (POS)** — Incorporates features of both HMOs and PPOs, encouraging but not requiring members to choose a primary care physician. As in HMOs, primary care physicians act as "gatekeepers" to other health care services. However, members may visit non-network providers, but pay higher deductibles and co-payments.

**Policyholder** — Literally, the person who has possession of the policy. Thus the term is non-functional as commonly used. (See comment under INSURED.)

**Pooling** — Combining risk.

**Preadmission Review** — Review of claims for inpatient admission prior to hospital admission in order to assure medical necessity.

**Preauthorization** — A method to monitor and control utilization of a medical service by evaluating need prior to it being performed.
Pre-Existing Condition — A condition of health or physical condition that existed before the policy was issued. Prior to 1993, insurance coverage was denied or significantly delayed on the basis of pre-existing conditions. In Washington state, however, carriers cannot use health screening to reject applications, and the only waiting periods allowed may be no more than nine months for a condition treated in the previous six months.

Preferred Provider Organization (PPO) — A health care arrangement between purchasers of care such as employers and insurance companies and providers offering benefits at a reasonable cost using incentives, such as lower deductibles and copays to get members to use providers within a network. Use of non-preferred physicians would involve a higher cost. Preferred providers must agree to specified fee schedules and are required to comply with certain utilization and review guidelines.

Preferred Risk — An insurance classification indicating a risk that is superior to the average risk on which the rate has been calculated. They are usually eligible for a reduced rate.

Premium — The price of an insurance policy, typically charged annually or semiannually.

Pre-Paid Hospital Service Plan — The common name for Health Maintenance Organization plan (HMO). It provides comprehensive health care, usually by salaried personnel, for members who pay a flat fee for the services, whether out-patient or hospital treatment is needed.

Prescription Benefit Managers (PBMs) — Monitor prescription claims for managed care organizations, tracking the drugs and volumes of pharmaceuticals are prescribed by the plan's participating physicians.

Primary Care — Primary Care is the first care a patient receives. It is often a family physician, although patients also may receive Primary Care from a nurse, a paramedic, or other types of health-care providers, depending on the situation. Managed care systems try to resolve as many health problems as possible at this level.

Prior Authorization — Managed care procedure to control utilization of services by review and approval of a medical service. See also preauthorization.

Pro Rata — (1) Distribution of the amount of insurance in one policy, among the several objects or places covered, in proportion to their value or to the amounts shown. (2) The distribution of liability among the several insurance companies having policies on the risk.

Proof of Loss — A formal statement made by the insured to the insurance company regarding a loss. The purpose of the proof of loss is to place before the company sufficient information concerning the loss to enable it to determine its liability under the policy or bond.

Providers — Institutions and individuals licensed to provide health care services (e.g. hospitals, physicians, naturopaths, medical health clinicians, pharmacists, etc.)

Rebate — Giving to the policy owner some part of the agent's commission (or something of value) as in inducement to buy. This is an illegal action.
Reinsurance — Insurance bought by insurers. A re-insurer assumes part of the risk and part of the premium originally taken by the insurer, known as the primary company. Reinsurance effectively increases an insurer's capital and therefore its capacity to sell more coverage.

Renter's Insurance — A form of insurance that covers a policyholder’s belongings against perils such as fire, theft, windstorm, hail, explosion, vandalism, riots, and others. It also provides personal liability coverage for damage the policyholder or dependents cause to third parties. It also provides additional living expenses, known as loss-of-use coverage, if a policyholder must move while his or her dwelling is repaired.

Replacement Cost — Insurance that pays the dollar amount needed to replace damaged personal property or dwelling property without deducting for depreciation but limited by the maximum dollar amount shown on the declarations page of the policy.

Risk — The chance of loss of the person or entity that is insured.

Self-insurance — The practice of an employer or organization assuming responsibility for the health care losses of its employees. Usually a fund is established against which claims payments are drawn. Claims processing is often handled through and administrative services contract with an independent organization, usually an insurer.

Short-Term Disability — Paid time off in case of sickness. Short-term disability usually covers 100% of an employee’s wages for a few weeks.

Single Payer — This system of health coverage would enroll all Americans in a government-run program financed by taxes. This plan was scrapped when overall health-care reforms were considered at the federal level in the early 1990s, but bills that would implement a single-payer system remain alive in Congress.

Social Security — A comprehensive federal benefit program that provides workers and their dependents with retirement income, disability income, and other payments.

Subrogation — Requires an insured person to assign any rights to recover damages to his insurer.

Term Life Insurance — A form of life insurance that covers the insured person for a certain period of time, or the “term” that is specified in the policy. It pays a benefit to a designated beneficiary only when the insured dies within that specified period.

Third-Party Administrator (TPA) — An individual or company contracting with employers who want to pay the cost of providing healthcare for their employees. TPAs develop and coordinate self-insurance programs, process and pay claims, may help locate stop loss insurance for the employer. They also can analyze the effectiveness of the plan and utilization of its benefits.

Umbrella Policy — Coverage for losses above the limit of an underlying policy or policies such as homeowners and auto insurance. While it applies to losses over the dollar amount in the underlying
policies, terms of coverage are sometimes broader than those of underlying policies.

**Underinsured Motorist Coverage (UIM)** – This coverage protects an insured driver from losses that should have been the responsibility of another driver, but which are not covered at all, or not fully covered by the other driver’s insurance.

**Underwriting** – Examining, accepting, or rejecting insurance risks and classifying the ones that are accepted, in order to charge appropriate premiums for them.

**Unemployment Insurance**—Cash benefits paid to workers who have been terminated from employment.

**Usual, Customary and Reasonable (UCR)** — Health insurance plans pay a physician's full charge if it is deemed reasonable and does not exceed his or her usual charges and amount customarily charged by other physicians practicing in the area for the service.

**Waiting Period** — A period of time between the beginning of a disability and the date benefits begin. In Washington state, health insurance waiting periods are limited to 90 days.

**Waiver** — (1) A rider waiving (excluding) liability for a stated cause of accident or (especially) sickness. (2) Provision or rider agreeing to waive (forego) premium payment during a period of disability. (3) The giving up or surrender of a right or privilege that is known to exist. It may be effected by the agent, adjuster, or insurance company employee or official orally or in writing.

**Whole Life** — A life insurance policy that runs for the whole life - that is, until death

**Worker’s Compensation**—A benefit that pays for medical care and/or gives cash payments to workers who are injured on the job or who contract work-related illnesses.

**Write** — In insurance terms, to insure. It also means, to underwrite or to sell.

This glossary was adapted from the Washington State Insurance Commissioner website.