Inaccurate Notions about Insurance

- Majority investors have a notion that insurance is meant for tax saving. It is being widely used for tax saving purposes. Investors are unaware about the objective of life insurance. Insurance insures event risk. The risk in case of life insurance means possibility of loss to the family due to death of the person insured since the income will no longer exist to support the family. It has a sole objective of securing the future of the dependants in case of an adverse event. The tax benefit under Section 80C is just an added advantage and ideally should not be the sole objective to buy insurance.

- Many people buy insurance policies in the name of their wife, kids who are not earning members and are dependants. Insurance must be bought in the name of the earning member of the family who is supporting the dependants. The earning member should always ask himself 'What will happen if something happens to him? Who will take care of the dependants (non-earning members like wife, kids and parents)?' Policy should be taken in the name of the earning member so that if something happens to him the dependants will be the beneficiaries of the insurance claim. While if the policy is taken in the name of dependants and if something happens to the earning member of the family the dependants will not get anything. So, it is clear that the earning members should insure themselves, not the dependants.

- Investors feel that if they do not have any dependants so they do not need life insurance. In this case, it is right. But they will need Mediclaim or Health Insurance. If one gets admitted to a hospital for a surgery or for any other reason the costs are huge. This will impact the savings by a significant extent. Mediclaim or Health Insurance pays off the hospital bills in case the person insured is admitted to the hospital.

- Many policyholders buy multiple insurance policies and feel that they have taken adequate insurance cover. Instead of buying multiple policies a term plan provides the required cover at a very low cost. Policyholders usually buy multiple policies thereby refusing to buy a term plan and often remain under insured.

- Most people generally avoid taking insurance cover since they already have a group insurance from their employer. This group cover is just temporary since it will only cover you till you are associated with the employer. What if you change the job after some years of working or lose your job or start a business then you will be left without adequate insurance cover and end up being under insured. It is always ideal to have a term insurance along with the group insurance cover since if you buy the cover after a few years i.e. when you change or lose your job or start a business, the premium at that point of time will be very high due to increased age and health conditions.

- Investors buy insurance policies with a view that on maturity they will get a bonus. But in order to give bonus, the companies collect an extra amount which is already included in the premium. This means the premium has a bonus loading which is built in. It has been seen that the investors think they are getting a bonus for free which is clearly not the case. There is no free lunch. Nothing comes for free in the world of finance. Due to the investment component and bonus loading both built in, the premium for policies (excluding term plans) is very high.

- As far as term plan is concerned which is the only pure life insurance policy, people often expect to get money back at the end of the policy term. So, they do not prefer term plan. Insurance is a service offered by the company which is not tangible i.e. investors have a psychology that they do not prefer those things that they cannot touch it and since they do not get the money back in a term plan nor they are getting a product (which they can touch it) in return of the premium paid, they do not prefer term plan. It is just like paying for a burger, eating it and then asking for money back. Due to this mentality it has been seen that the investors remain under insured. Insurance is not an investment to get something back on maturity. Investors fail to understand that in return of the premium that they are paying to the insurance company for a term plan, they are getting insurance. Pure insurance should not be confused with investments and investors should not expect to get money back on maturity (since they are getting insurance cover in return of the premium paid). The detailed explanation of this aspect is mentioned in the articles 'Investing Mistakes' and 'Insurance Goof-Up' under our 'Articles' section. Do not forget to read it.