How to Make a Proper Insurance Plan

By Eng Tiang Chuan

A Protection Portfolio is an important part of financial planning. Be sure you don't get caught with inadequate coverage.

The common answer to the question of whether the typical Singaporean has enough insurance is "yes and plenty of it". On further examination, most policy holders will not know what his or her policy covers. Many people are still clueless about what they are covered for despite having bought numerous policies. This could easily result in unnecessary duplication or worse, not getting the correct protection despite paying high premiums.

Consumers are used to the product selling instead of needs based selling approach. A typical experience is that of being approached by agents promoting certain products at bus interchanges or MRT stations. While there is nothing wrong in this approach, it has to be done in the context of enhancing value for the consumer and not in the hope of doing a quick sale.

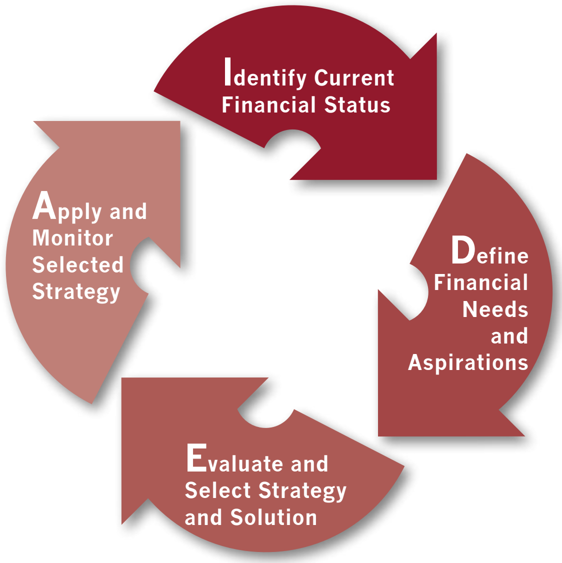
To ensure that we have the right protection, knowledge of what and how to construct a proper Protection Portfolio is a must. This series of articles will focus on how to carry out a Proper Protection Planning.

A well known classification of financial planning, known as the *4Ws*, is often used as a guide to achieve financial well–being. The *4Ws* are:

Wealth Protection
Wealth Accumulation
Wealth Preservation
Wealth Distribution

Wealth Protection, or Protection Planning, stands as the very first step of a proper financial planning process. It employs the concept of Risk Transfer through insurance whereby the financial risks are transferred to an insurance company through a contract.

Protection planning can be represented by the I.D.E.A diagram:



1. Identify Current Financial Status
2. Define Financial Needs and Aspirations
3. Evaluate and Select Strategy and Solution
4. Apply and Monitor Selected Strategy

Planning shouldn't stop just after going through one cycle but should be continuous. Periodic review should be done to cater to the changes in a person's lifecycle. What is enough now may not be adequate in the future. Consumers should not go straight to selecting or buying insurance products without first going through the first three steps. Just like building the jigsaw puzzle, one may never be able build a beautiful jigsaw puzzle simply by picking up random pieces and trying to fit into each other. Similarly, getting a insurance plan without the proper considerations may result in an ill–fitting plan.

In real life, an incomplete jigsaw will not cause much distress except maybe a few days of disappointment. An improper Protection Plan may cause dire financial consequences and a lifetime of regret.

CARRYING OUT THE PLANNING PROCESS

To Identify the Current Financial Status, an Assets and Liabilities and Cash Flow Analysis should be carried out. Assets and Liabilities Analysis would deduct all liabilities including mortgages, loans, bills etc, and deduct from the assets including property, stock holdings, CPF savings etc. The result is the Net Worth. Cash Flow measures the monthly/yearly spending/saving habits and shows a positive or negative result. Positive indicates there is excess income/savings while a negative would point to overspending. Creating a Budget would be a tremendous help in generating a positive Cash Flow. An Assets and Liabilities and Cash Flow Analysis can be easily done by the reader or with the assistance of a competent adviser and shall not be discussed in detail here.

Consumers are often overwhelmed and confused when faced with the vast variety of insurance products available in the market. The products fall into different classes and are meant to protect different aspects in your protection plan. Policy holders may get an unsuitable product if they do not know what the policy covers. Other than getting a product without knowing what it covers, consumers may be lured by some seemingly good features of a policy and overlook the more important areas. Such instances could easily cause financial difficulties when an unfortunate event strikes. To avoid such circumstances, the consumer should know what areas they want protected. This would help consumers in Step 2 of a Proper Protection Planning – Define his/her Financial Needs and Aspirations.

HOSPITALIZATION EXPENSES

Protection against hospitalization expenses is the most basic coverage one should get, for both children and adults. Hospitalization expenses could cause a great outflow of financial resources which could be crippling to one's financial health. In the Sunday Times article "40 years of his Medisave wiped out in 3 months" published on November 4, 2007, it was reported that the savings in Mr Mohammad's Medisave account, which took him over 40 years to build up, was used up in 3 months after his daughter was diagnosed with ovarian cancer. Unfortunately, his daughter must still go for further treatment. Unlike expenses for death, hospitalization expenses can be recurring and prolonged. And with advances in medical science, the chances of more expensive treatments and prolonged life despite being diagnosed with illnesses can only increase.

DEATH

The main reason for getting Death coverage is to provide for one's liabilities – dependents, debts, funeral expenses etc. The death payout would enable the dependents (eg, spouse, children and parents) to continue their current lifestyle and continue their various plans like funding education. In addition, some people would like to provide a donation to their church, temple or charity in the event of death. If you have adequate death coverage, then you would be able to do that.

TOTAL PERMANENT DISABILITY (TPD)

Similar to Death coverage, when the insured suffers from TPD, the payout can cover for needs of dependents and debts. However, unlike Death, TPD care can be prolonged and no one knows for sure how long the insured will suffer before passing away. Additional expenses like paying for a domestic helper, miscellaneous medical apparatus like wheelchairs and beds are also needed. Disability Income (DI – refer to below) can be used to meet the needs of such recurring expenses. TPD coverage normally ends at age 65. Thus, for pre–age 65 (pre–retirement), DI should be used to cover for

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the monthly expenses. Post age 65 (during retirement) disability coverage should be covered using a Long Term Care plan (see below). The monthly expenses projected for Retirement Planning can be used to supplement the monthly expenses.

CRITICAL ILLNESS (CI)

CI coverage provides a payout if the life assured is diagnosed with a pre–defined illness. Similar to TPD, CI care can also be prolonged with miscellaneous expenses needed. Although a good Hospitalization and Surgical (H&S) plan will cover a big portion of the hospitalization expenses, it is important to know that not all cancer drugs are covered by the MediShield plan. Such cancer drugs can be very costly. The annual cost of new treatment such as Erbitux (colorectal cancer) is at US$120,000, Nexavar (kidney cancer), Herceptin (breast cancer) and Avastin (colon cancer) at US$50,000[1]. Such cost can be financed by having a CI coverage. In addition, the CI payout can also be used for alternative treatment such as Traditional Chinese Medicine (TCM) or treatments in foreign countries if one wishes. As with TPD, DI should be used to cover for monthly expenses should one lose the ability to work due to CI.

DISABILITY INCOME (DI)

For those who rely on a source of income for living expenses, losing the ability to generate this income stream due to disability or illness would be financially disastrous. Having a DI coverage would help to protect against such a scenario and offer the insured a chance to continue his/her life plans. It also offers a source of regular income to offset the regular expenses such as employing a domestic helper if such needs arise. It was reported in the January 25, 2008 issue of The Straits Times, titled "Families flock to get maid levy rebate for disabled", that 1200 families applied for government schemes introduced in September 15 last year to help families cope with the cost of caring for the disabled family member. 800 of the applications were for maid levy rebate. This class of insurance can help address the loophole of losing one's ability to generate an income due to disability or illness yet unable to claim due to failure to meet the definitions needed for various payouts. Disability Income covers to a max age of 65.

PERSONAL ACCIDENT (PA)

Accidents can result in Disability, Death or Partial Dismemberment (eg loss of fingers, limbs, sight in one eye etc). Such coverage only extends to the above scenarios due to accidents ONLY. Thus, Partial Dismemberment should be the main consideration for getting coverage for PA as Death and Disability coverage should not be limited to accidental causes only. The premium for PA coverage is much lower than others due to the low probability of claim.

LONG TERM CARE (LTC)

LTC coverage means getting a monthly payout if one is disabled and is unable to perform a certain number of Activities of Daily Living (ADL). ADL includes Washing, Dressing, Feeding, Toileting, Mobility and Transferring. Disability coverage post age 65 would be the most useful aspect of this coverage as TPD and DI coverage normally ends at age 65. A report titled "Singaporeans live longer but suffer 8 years of poor health" on The Straits Times on December 5, 2007 highlighted that although the average life expectancy has increased, many still suffer from disability in old age. Having a LTC plan can help relieve some of the burden of old age disability.

With the knowledge of the main areas to consider when conducting Protection Planning in mind, we shall look into the common insurance plans available in Singapore and the common mistakes/misconception made in our next article.

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Reference:
1. Speech by Minster for Health, Mr Khaw Boon Wan at the American Association for Cancer Research Asia Centennial Conference on 4th Nov 2007
–– http://www.moh.gov.sg/mohcorp/speeches.aspx?id=17730