Why Self-Insurance Isn't Always the Right Choice

"Self-insurance" refers to the choice to refrain from purchasing insurance and, instead, assume all risk of loss and pay for any associated costs yourself. Essentially, you set aside money *just in case* and assume the role of your own insurance company. With self-insurance, you would pay for a medical procedure or the costs of repairing a burst pipe out of pocket instead of filing a claim and being reimbursed by an insurance company.

In some cases, self-insurance isn't allowed by law. For example, many states require vehicle owners to maintain a minimum amount of car insurance in case of an accident. Mortgage companies may require that homeowners purchase an insurance policy to protect against property damage. However, some individuals may choose to forego health insurance or disability insurance and pay for any medical costs that do arise from their personal savings. Many people choose to skip valuable personal property insurance for their electronics and buy new models when the old ones stop working instead – which is in essence, a form of self-insurance.

When it comes to life insurance, many people provide for their final expenses in their estate plans – this can be a form of self-insurance. It's important not to underestimate final expenses though. Burial and funeral expenses can amount to thousands of dollars, even for veterans who plan to be buried in a VA cemetery – the VA will not pay for caskets, cremation, the preparation of a body, or funeral director services, among other costs – so having funds set aside for final expenses is important regardless of veteran status. For individuals who need medical, chronic illness, or hospice care in their final months, final expenses can amount to much more than an estimated $10,000 in burial and funeral costs. Unless funds are set aside for final expenses, these bills can be passed to family members or beneficiaries who are then liable for the payments.

If you underestimate your final expenses, your loved ones may end up paying more than you saved by choosing not to purchase a life insurance policy.

When it comes to life insurance, self-insurance generally works the best for individuals who have no dependents and have little to no debt *and* a large nest egg that can be tapped into to pay for any expenses that come up. Self-insurance works less well for individuals who have dependents, significant debts, and/or fewer assets. Why? Dependents may need financial support after one's death – especially if they are young, need individualized care, or don't have significant income of their own. Further, debt accumulated over the course of one's life is generally *not* forgiven upon death. Credit card balances, mortgages, vehicle loans, etc., still need to be repaid and that burden may fall to survivors. A large nest egg could be used to pay for any debts that remain upon death, final taxes that are due, and funeral and burial expenses.

If you are the primary breadwinner for your family and decide not to purchase insurance on your own life, you are essentially putting faith in your family's ability to "figure it out" if you pass away and hoping that you have enough money in reserve to cover any expenses you leave behind. Depending on the timing of your death – especially if something happens when you are relatively young – you could leave your family with little to work with. That said, if you live a long and productive life, you may leave more assets behind. The choice to self-insure comes down to assessing the probability that your assets will be sufficient to provide for your final expenses (and leaving an estate to your family, if desired), your personal risk tolerance, and the risk tolerance of the loved ones who rely on you for financial support.

What are the pros of self-insurance?

- If you're not spending the money on an insurance policy, you can invest the funds that you would otherwise be spending on premiums however you'd like. In theory, this can help you make money (depending on market conditions). If your estate is sufficient to meet your financial goals, you will have never needed these funds for insurance purposes and you will technically have "saved" money that you would have spent on premiums.
  - Note, however, that term life insurance is quite inexpensive, especially if you purchase a policy when you are relatively young and healthy. For example, paying $45 a month over the life of a 30-year policy amounts to $16,200 – but could provide your beneficiaries with $500,000 if you pass away during the term. This is a significant return on investment that can benefit your loved ones.
- There are no limits to the amount you can self-insure. For example, life insurance policies may have a cap of $1 million. However, if you choose to self-insure, and have the means, there is no limit to how much money you can save to leave to your loved ones.

What are the cons of self-insurance?

- Depending on the timing of your death, you may not have had enough time to save the funds necessary to cover your final expenses and adequately set your family up to enjoy a financially secure future. Invested funds take time to grow, and earnings potential decreases each time a withdrawal is made from your accounts.
- You can pass along your remaining financial obligations to your dependents, who may have to sell your property and move to a cheaper home, decrease their standard of living, go into debt of their own, or pick up extra work to cover your final expenses. At the same time, they may have their own financial obligations that must be met. Without a plan and proper savings, your family may struggle after you are gone.

Consider:

- How much money do you want to leave behind?
- Is self-insurance even feasible with your current salary and expenses? If, for example, you care for someone with a lifelong disability, self-insurance probably won't allow you to provide for that person's needs after you are gone.
- How much debt do you have? To avoid burdening your loved ones, you need to save enough money to pay for funeral, burial, and final medical expenses, replace your salary, and pay off outstanding debts. This can amount to a lot of money and the potential exists for large out-of-pocket expenses to arise that may be unpayable. Life insurance can cover your financial obligations where self-insurance would not.

Navy Mutual provides affordable term life insurance policies to current and former servicemembers and their families. Our policies are tailored to your needs and your goals – and offer up to $1.5 million in coverage that can protect your loved ones in the future. Get a quote today.