Understanding Insurance

Some types of insurance you have to take out by law such as motor insurance if you drive a vehicle; some you may need as a condition of a contract such as buildings insurance as a requirement of your mortgage; and others are sensible to take out such as life insurance.

While it is a good idea to make sure you are not paying for insurance that you don't need, you should always think about what would happen if the worst should happen and you didn't have cover to protect you.

How insurance works

At its most basic level, an insurance policy is the contract that you take out with an insurer to protect you against specific risks under agreed terms.

When you buy a policy you make regular payments, known as premiums, to the insurer. If you make a claim your insurer will pay out for the loss that is covered under the policy.

If you don't make a claim, you won't get your money back; instead it is pooled with the premiums of other policyholders who have taken out insurance with the same insurance company. If you make a claim the money comes from the pool of policyholders' premiums.

How premiums are calculated

Insurers use risk data to calculate the likelihood of the event you are insuring against happening. This information is used to work out the cost of your premium. The more likely the event you are insuring against is to occur, the higher the risk to the insurer and, as a result, the higher the cost of your premium.

An insurer will take two important factors into account when working out the premium they will charge.

1. How likely is it in general terms that someone will need to make a claim?
2. Is the person who wants to take out a policy a bigger or smaller risk than the 'average' policyholder?

Choosing the right insurance

Insurance provides peace of mind to businesses and families across the UK. General insurance products are designed to safeguard against the risk of loss, damage or theft, for example because your house floods or because your dog unexpectedly needs major surgery. This guide is going to focus on 3 specific types on insurance: income protection insurance, life cover and critical illness insurance.

Income protection

Income Protection Insurance helps support you financially if you have time off work and suffer a loss of earnings because of injury or illness. This type of insurance covers most illnesses that leave you unable to work. For example, it may cover you if you're unable to work due to a stress-related illness, mental health or a physical health condition. Income Protection Insurance only covers you if you're unable to work due to illness or injury – it does not pay out if you are made redundant.

Having an income protection policy will mean that you can continue to pay your bills, rent or mortgage if you are unable to work.

How income protection works

There are different types of income protection insurance, but most are either Individual Income Protection Insurance (often called IP) and Employer Provided Income Protection Insurance (known as Group Income Protection or GIP).

- Individual Income Protection is taken out by a person seeking to independently protect their income in the event of being unable to work due to illness or injury.
- Employer Provided Income Protection Insurance is a policy taken out by your employer to protect your income if you are unable to work due to illness or injury.

If you or your employer buy an income protection policy, you will be paid a monthly income if you find yourself unable to work. You or your employer will pay a monthly premium to your insurer for your chosen policy which will pay out after a pre-agreed waiting period. This is also known as the 'deferred' period. The waiting period is the time between being unable to work and the time at which you will begin receiving payments.

Individual income protection

You can apply for income protection if:

- You work in full time employment
- You work in part time employment
- You are self employed

You can also apply if you have a pre-existing medical condition, however depending on how serious your condition is, insurers may charge you more, or they may apply a specific exclusion to your policy.

Here are some of the things you might want to consider when looking at whether Income Protection is right for you:

- What would happen if you became ill and couldn't afford to pay the bills?
- If you're employed, do you have sick pay to fall back on and how long is this paid for?
- If you're self-employed, what would you do if you couldn't work for any reason?
- Do you have enough savings to cover any personal loan or debt repayments?
- Do you have any dependents, and will you have enough savings to cover you and your dependants if you are unable to work?

The cost of an Individual Income Protection Insurance product will be determined by the type of policy you want to buy, and your individual circumstances.

Factors that affect the amount you pay are:

- Type of job
- Your age
- The percentage of income you want covered
- Your health, including any pre-existing conditions
- When you want your policy to end

Employer provided income protection

Employer provided income protection, or Group Income Protection is insurance cover that employees can only get through their employer. This usually forms part of an employee benefits package.

Group Income Protection allows employers to choose a policy that fits their business needs and budget. Businesses can pick and choose how long a policy runs for, whether it'll be fully-funded by the company or part-funded by the employee, what percentage of salary it pays out, which employees get it and how long they must be off work before the income benefit kicks in.

Key benefits of employer provided income protection

No medical underwriting, which means that individuals with pre-existing health conditions do not have to worry about exclusions related to their conditions and they are also able to receive additional support for these conditions.

Financial peace of mind at an uncertain time, as policies pay a regular income if you are unable to work

Access to dedicated support from your insurer though Employee Assistance Programmes and access to professionals such as mental health specialists and physiotherapists.

Expert case manager to assist employees to recover and return to work as soon as possible.

A specific focus on wellbeing with access to preventative support services and tools, helping to empower employees with maintaining their health and wellbeing.

Income protection support services

While the financial benefits are usually the main reason why people choose to protect their income, income protection products frequently come with a wide range of added value support. This type of support - for both the employer and employee - usually comes as part of the policy and doesn't cost anything extra.

Some of these support services can include rapid access to assessment for a range of health issues, use of a dedicated Employee Assistance Programmes which provide access to support services 24 hours a day and rehabilitation services.

What is Life Cover?

Life cover is a term used to describe life insurance or death cover which can provide a cash lump sum in the event of your death, or if you become diagnosed with a critical illness. You can include critical illness cover as part of your life cover or take it out as a separate policy.

By paying a monthly premium or a lump sum to your insurer for life cover, you can safeguard your loved ones from financial hardship if you die or suffer from one of a list of illnesses. The money can be put towards funeral costs, payment of a mortgage, debts, or your family's living expenses.

Things to think about to decide if you might need cover:

- what would happen if you died or were ill for a long time
- who are your financial dependents: your husband or wife, children, brother, sister, or parents
- what kind of financial support does your family have now
- what kind financial support your family will need in the future
- what kind of costs will need to be covered such as household bills, living expenses, mortgage payments, education costs, debts or loans, funeral costs
- whether you can afford to pay regular premiums or a lump sum
- what factors might affect your premiums – many life cover policies look at your age, occupation, lifestyle, pre-existing and family medical history
- whether you would need to include critical illness cover because of your family medical history

If you have loved ones, such as children, a partner, or other relatives, who depend on your income to cover debts, bills, or living expenses, then it may be worth considering taking out life cover. It will help to provide some financial support to your family if you die.

However, you may already be covered by a group life scheme (often known as death in service benefit) through your employer.

Life cover is important if you are:

- just married
- a young couple just starting out
- new parents raising a young family
- a mature family starting to think about the future
- a retiree who may survive their partner and need financial support

And you might want to consider life cover if you are:

- getting married
- buying a house
- starting a new job
- applying for a mortgage or loan
- the birth of a child

Types of life cover

There are different types of policies which can give you lump sum payments, or a regular monthly income (if you have family income benefit). To decide on which cover you need, think about the questions and your reasons for choosing one of these policies.

Term insurance	gives you life cover during a pre-agreed period of time
Group life cover	gives you life cover through your employer
Critical illness	gives you cover for specific medical conditions
Over-50 plans	gives you cover towards funeral costs, paying debts or if you want to leave some money to loved ones if you die
Whole of life plans (also known as life assurance)	gives you cover for your entire life; it can meet your debts or be left to a loved one when you die

Critical illness insurance

Critical illness cover gives you financial protection against certain illnesses and medical conditions of a specific severity.

Your cover will provide you with a tax-free lump sum cash payment which can be used to help you and your family. For example, it could help you pay off your mortgage, pay for treatment to help you recover or pay your household bills.

All critical illness policies cover cancer, heart attack and stroke, providing they are of a certain severity.

Covers varies between insurers and some policies include additional medical conditions, so check the details of your policy with your insurer.

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