Lesson 7.3: Managing Risk

Adapted from Lesson 10B: Is Insurance Worth Buying?:
https://www.federalreserveeducation.org/teaching-resources/personal-finance/managing-risk/is-insurance-worth-buying-lesson-10b

Standards and Benchmarks

See pages 5-6.

Lesson Description

Students learn about insurance options and possible risks. They play a game where they first choose levels of insurance coverage and then face random events. Students track the cost of their insurance choices and the benefit of their choices based on each event. Finally, students determine whether the insurance choices they made were financially beneficial or not and why insurance may be a good idea.

Concepts

Financial risk
Insurance
Opportunity Cost
Premium
Risk

Objectives

Students will be able to:

- define insurance, premium, deductible, copay, and liability.
- describe the benefits of insurance (loss reduction).
- describe the costs of insurance (premiums plus other opportunity costs).
- explain why buying insurance may be a good idea even if the costs exceed the benefits over a given period.

Compelling Question

How can consumers reduce their risk of financial loss?

Time Required

60-75 minutes

Materials

- Managing Risk Lesson 7.3 Slides, one copy for teacher to display
- Materials from Lesson 10B: Is Insurance Worth Buying?

- Visual 10.1: Risks, one copy for teacher
- Handout 10B.1: Managing Risk, one copy for each student (NOTE: for ease of use, copy as separate pages, not back-to-back)
- Handout 10B.1: Managing Risk – Answer Key, Part B: My Life Events, one copy for teacher
- Handout 10B.2: Assessment, one copy for each student
- Handout 10B.2: Assessment – Answer Key, one copy for teacher

- Additional Materials
  - One regular deck of (52) cards
  - Calculators (optional)

Procedure

1. Ask students “Would you rather have health insurance and never use it or not have health insurance and need medical care?”.

    a. Raise your hand if you prefer to have the health insurance.

    b. Raise your hand if you prefer to not have the health insurance.

2. Display Slide 2. Discuss the following with students:

    a. What is **risk**? (*Risk is the chance of loss.*)

    b. What actions have you taken today that involve some kind of risk? (*Answers will vary. Students will likely suggest actions that involve a moderate to high degree of risk but many of the actions they take involve some degree of risk. Loss does not need to be monetary.*)

    c. Did you do anything to reduce the risk? (*Answers will vary based on student responses. Students might have looked both ways before crossing the street, tied their shoes, or placed money in a wallet rather than keeping it unsecured.*)

3. Display Slide 3. Tell students that you will determine how much risk they would be comfortable with through a series of questions. Ask them to raise their hands if they would do the following:

    - Ride in a car without a seatbelt?

    - Stay out past curfew?

    - Swim in the ocean with a lifeguard?

    - Visit a friend with the flu?

    - Leave your house unlocked while you go to the gym?

4. Display Slide 4. Tell students one type of risk is **financial risk**. Define financial risk as the possibility of monetary loss. However, there are ways to manage financial risk.

5. Display Slide 5. Explain the four ways of managing financial risk using each definition and example provided.

   a. Avoid

      - Definition: Choosing not to engage in activities or investments that could lead to financial loss.

      - Example: Do not drive.

   b. Reduce

      - Definition: Taking steps to lower the chance of loss.

      - Example: Obey traffic laws and maintain your vehicle.

   c. Retain

      - Definition: Accepting potential financial loss instead of transferring it.

      - Example: Accept any financial loss associated with getting into an accident.

   d. Transfer

      - Definition: Shifting financial risk to another party.

      - Example: Buy automobile insurance.

6. Ask students:

   a. Do you think any of these strategies are better than others? (*No. It is dependent on the situation.*)

   b. How would you decide which risk management strategy would be the optimal choice? (*Answers will vary. Have students justify their answers using examples. For situations that result in greater financial loss and have a greater chance of occurring, the less likely retaining would be the optimal choice.*)

7. Complete procedure steps 1-13 on pages 244-249 from Lesson 10B: Is Insurance Worth Buying?

   Note: Rather than a physical deck of cards, you can use the Playing Card Shuffler found here: https://www.random.org/playing-cards/.

Closure

8. Review the important points of the lesson by asking the discussion questions in the closure section on page 249 (procedure step 14).

Assessment

9. Complete assessment on page 249 of the lesson.

Standards and Benchmarks

National Standards for Personal Financial Education

Standard 6: Managing Risk

People are exposed to personal risks that can result in lost income, assets, health, life, or identity. They can choose to manage those risks by accepting, reducing, or transferring them to others. When people transfer risk by buying insurance, they pay money now in return for the insurer covering some or all financial losses that may occur in the future. Common types of insurance include health insurance, life insurance, and homeowner's or renter's insurance. The cost of insurance is related to the size of the potential loss, the likelihood that the loss event will happen, and the risk characteristics of the asset or person being insured. Identity theft is a growing concern for consumers and businesses. Stolen personal information can result in financial losses and fraudulent credit charges. The risk of identity theft can be minimized by carefully guarding personal financial information.

Benchmarks: Grade 12

1. People vary with respect to their willingness to accept risk and in how much they are willing to pay for insurance that will allow them to minimize future financial loss.
2. The decision to buy insurance depends on perceived risk exposure, the price of insurance coverage, and individual characteristics such as risk attitudes, age, occupation, lifestyle, and financial profile.
3. Some types of insurance coverage are mandatory.
4. Insurance premiums are lower for people who take actions to reduce the likelihood and/or financial cost of losses and for those who buy policies with larger deductibles or copayments.
5. Health insurance provides coverage for medically necessary health care and may also cover some preventive care. It is sometimes offered as an employee benefit with the employer paying some or all of the premium cost.
6. Disability insurance replaces income lost when a person is unable to earn their regular income due to injury or illness. In addition to privately purchased policies, some government programs provide disability protection.

7. Auto, homeowner's and renter's insurance reimburse policyholders for financial losses to their covered property and the costs of legal liability for their damages to other people or property.

8. Life insurance provides funds for beneficiaries in the event of an insured person's death. Policy proceeds are intended to replace the insured's lost wages and/or to fund their dependents' future financial needs.