

What's UP with Gap Insurance?

If you have a car loan and your car gets stolen or totaled in an accident, gap insurance, also called “totaled insurance” pays the difference between what you collect from an insurance company for the value of the car and the amount you still owe on the loan. Gap insurance, (which stands for “guaranteed auto protection”) is a debt-cancellation agreement.

Should I buy Gap Insurance?

If you've financed the purchase of a car with little or no money down, or if you've chosen a long (4 year) payoff period, gap insurance can be valuable protection. Cars depreciate quickly – faster than some people pay down their loans. A new car depreciates @ 11% when you drive it off the lot, and 20% each year after that. So it's fairly common for a financed car to be worth substantially less at the time of an accident or theft than the balance left on the loan.

Example: You buy a car for \$25,000 and put \$5,000 down. You finance \$20,000 over 5 years. A year after you buy it, you total the car. An insurer values it at \$15,000 and issues a check payable to you and the finance company. The check gets applied to the loan amount, leaving a \$1,000 balance. If you have gap insurance, it will pay off that balance so you don't have to pay the \$1,000 out of pocket.

If you've made a large down payment or opted for a short payoff term, and if the lender doesn't require you to buy gap insurance, you may be fine without it.

Things to consider

You can buy gap insurance in one of two ways: Through the lender that finances your loan, or through your car insurance company, (if they sell it – not all insurers do). If you buy gap insurance through a lender, it will cost a flat up-front fee of \$500-\$700. It will be much cheaper buying it through your car insurer, in most cases, and less painful because the cost gets added to your regular premium. If you buy it through the dealer/lender and the gap insurance cost gets added to your loan, also be paying interest on that cost. Get quotes and compare to find the better option.

Gap insurance doesn't cover missed or late payment fees, repossessions, extended warranty costs or car repairs...just loan balances.

How long to keep Gap Insurance

If you buy gap insurance by adding it to your car insurance policy, drop/cancel it when your loan balance drops below the value of the car. You can check the value of your car online via Edmunds.com or Kelly Blue Book.

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