

The auto gap insurance dilemma at the dealership: Take the coverage or leave it?

Bankrate

While you're signing a stack of paperwork in the dealer's office and eyeing the set of keys to your brand-new ride, your salesman asks if you'd like to add another \$500 to your final tab for something you've never heard of called "auto gap insurance."

It's easy enough to say "no thanks." But don't floor it for the door just yet.

This coverage takes care of the potential gap between what you owe and the value of your car — if, say, the car is totaled after you drive it off the lot.

"The longer your loan term, the more valuable gap coverage would be," says Amy Bach, executive director of United Policyholders, an insurance consumer group in San Francisco.

Plus, you may be able to get the coverage for substantially less than \$500. Here's how to evaluate whether to say "yes" or "no."

Who sells auto gap insurance?

You have two options for purchasing gap insurance, says Bob Passmore, senior director of personal lines for the Chicago-based Property Casualty Insurers Association of America.

"The lenders often will have something they'd be happy to sell you, and so will your insurance company," he says.

If you decide to buy the coverage through your insurer, it may add about \$20 to your annual premium, according to the Insurance Information Institute, a New York-based trade group.

But expect to pay between and \$500 and \$700 for gap insurance through an auto lender, United Policyholders says. The coverage costs even more when you factor in the interest rate attached to your car loan.

If you're purchasing gap insurance through your lender, you should expect that you'll need to have the money available upfront, says J. Robert Hunter, director of insurance for the Consumer Federation of America in Washington, D.C. So, the cost of the coverage would likely be added to the balance of your loan.

When you might say 'yes' to gap coverage

It makes the most sense to carry gap insurance when you buy or lease a new vehicle, says Loretta Worters, spokeswoman for the Insurance Information Institute.

The institute says other times to give it serious consideration are when your down payment was less than 20 percent, or:

Your loan term is five years or longer.

You transferred negative equity from an older car loan into your new loan.

Your vehicle's value depreciates more quickly than that of most others.

The average car loses about 65 percent of its value over five years, according to Consumer Reports. The cars that depreciate at a faster rate do so because of limited appeal, oversupply or rebates on newer models that are similar.

When it easiest to say 'no'

You really don't need gap insurance if you own your car in the clear, Hunter says.

"Even if you don't own it outright, you don't have to get it," he says. You have to consider the costs involved and the likelihood that you'll have a total loss.

And, if you can afford the gap between what you owe on your car loan and how much it's worth, then gap coverage may not be for you.

Products such as auto gap insurance "tend to have a lot of fine print," so it pays to weigh the benefits and drawbacks, Bach cautions.

Weighing the value of a policy

"They have very low loss ratios, meaning that insurers tend to make a lot of money on them," Bach says. "They have restrictions that can make it tricky for the policyholder to collect."

Coverage can be priced relatively high and may not be the best value for consumers. "The consumer has to figure out how much it's going to cost over the life of the loan to keep the gap coverage in place," she says.

And, whether you pay a lot or a relatively small amount of money for auto gap insurance, you could find yourself buying the coverage and never needing to use it. Total-loss claims are rare, Hunter says.

"You have to have an accident pretty quick, in the first couple of years, to collect anything," he says.

People typically have collisions once every 10 years, and the chances of a car being totaled are much slimmer, he adds.