



Better Fortunes

Control Your Money. Control Your Life.



NATIONAL FOUNDATION FOR
CREDIT COUNSELING

*Knowing the difference can
make all the difference.*

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CHAPTER TWO

Developing Sound Financial Habits

This chapter will help you analyze your current thinking about money and introduce sound money management habits that are critical to long-term financial health. By learning to budget and by developing these habits, you will soon have extra money available each month to expand your options. Right now, your financial horizon may be very short—you may be focused on making it to the end of the week or month on your paycheck. As you develop these habits, however, your horizon will begin to expand. You will soon see your savings grow and future financial goals become a real possibility. Following is a list of things you want to know or do as you begin to reorder your financial life. Some of them are big things, some are small things, but they all help establish the habits that will enable you to take charge of your money.

Understand how you handle money now.

As a first step to long-term, financial health, you need to take stock. Think long and hard about the choices you may have made in the past and the choices you would like to make in the future. You need to be honest with yourself.

If you are a person who has a hard time denying yourself something you want—like the latest electronic gadget or the most expensive new athletic shoes—you need to find a way to remove the temptation. That might mean giving up the credit cards that appear to make things easy to buy. Or, if you can't control an ATM habit, you might need to get rid of your ATM card.

On the other hand, you may be responsible in these areas but have had setbacks because of a job loss or health problems. In that case, you still need to work out a strategy to bounce back. A nationally certified credit counselor can help by acting as your financial “coach.” The good ones cost very little. In fact, the best ones will help you even if you can't afford to pay them.

To help with your self-assessment of your attitude about money, read each of the topics below and choose the answer, or any combination of answers, that you believe represents the best financial habit or habits. If you have other ideas, write your own choice in the blank slot.

_____ **1. Spending:**

- A. You know where your money is being spent.
- B. You know where most of your money is being spent.
- C. You have no idea where your money is going.
- D.

_____ **2. Credit cards:**

- A. You should not use credit cards.
- B. You should be able to pay off all of your credit card bills each month.
- C. If you can't pay them off, you should pay more than the minimum amount due each month.
- D. You need only pay the minimum amount due each month.
- E. Transferring balances to delay payments is okay.
- F.

_____ **3. Credit cards:**

- A. You should have as many cards as you want. Many cards mean you can afford to have them.
- B. You should have no more than two or three cards of any kind.
- C. Department store cards and bank cards are the same thing.
- D. You can have many cards as long as you pay them all off each month.
- E.

_____ **4. Credit cards:**

- A. You should always make your payments by the due date.
- B. It is okay if your payments are sometimes late because of your pay cycle.
- C. Your interest rate will stay the same whether your payment is late or not.
- D. Late payment penalties are not that bad.
- E.

_____ **5. Housing:**

- A. Owning a home is better than renting.
- B. Renting is better than owning a home.
- C. Your rent or house payment should not be more than 30 percent of your take-home pay.
- D. Sharing rent with a roommate is a sign of failure.
- E.

_____ **6. Savings:**

- A. It is okay to use savings for day-to-day living expenses.
- B. It is okay to use savings to pay monthly bills.
- C. You should have 1-3 months of living expenses saved.
- D. You should have 3-6 months of living expenses saved.
- E. Savings are a nice thing to have, unless you can't afford to save.
- F.

_____ **7. Savings:**

- A. You should keep your savings at home.
- B. You should keep your savings in your checking account.
- C. You should keep your savings in a savings account at a bank or credit union.
- D. You should keep your savings in a money market account or fund.
- E. You should keep your savings in 6 or 12 month certificates of deposit (CDs).
- F. You should keep your savings in U.S. Government savings bonds.
- G.

_____ **8. Transportation:**

- A. You drive your car until it no longer runs.
- B. You buy a new car, SUV, or truck every few years.
- C. You lease your vehicles.
- D. You rely on public transportation.
- E. You carpool.
- F.

_____ **9. Transportation:**

- A. You like to pay cash for vehicles.
- B. You should make a down payment of 20-50 percent of the cost of the vehicle.
- C. You should make a down payment of less than 20 percent of the cost of the vehicle.
- D. Making a down payment is not important.
- E.

_____ **10. Transportation:**

- A. You should finance a vehicle for 6 to 8 years.
- B. You should finance a vehicle for 4 or 5 years.
- C. You should finance a vehicle for 2 or 3 years.
- D. You should lease a vehicle rather than buy.
- E.

CHAPTER THREE

My Current Budget: How Did I Get Here?

Financial experts agree that developing and sticking to a budget are the keys to good money management, yet many people resist the idea of living within a budget. If you or your family have been struggling with financial problems, it's time to stop resisting. Before you can begin to create a budget, however, you need two important pieces of information. You need to know what you have been doing with your money and also what financial goals you want to achieve. In this chapter, we'll find out what you've been doing with your money.

Developing Sound Budgeting Skills

We will start with five basic budgeting skills you should learn to achieve long-term financial wellness. These skills and habits will, in turn, enable you to ultimately achieve your short- and long-term financial goals. Chances are, if you're like most people, at least some of your financial habits can be improved.

First, let's take a look at the five basic budgeting skills we want you to develop and use. We also ask you to commit to improve these essential skills and to practice them for the rest of your life. Take a few moments to answer the following questions honestly. A "yes" answer is a sound budgeting skill you've already developed. A "no" represents a skill you need to develop to achieve your goals. If you check "no" in any box, resolve here and now to develop that skill. At the end of

the next chapter, you will be able to write a specific plan based on these skills which will help you achieve your goals—a plan called a workable budget.

1. Do I have a written budget that addresses my income and spending?

YES NO (I **will** create a written budget by _____ and live by it!)

2. Have I stopped adding to my debts and developed a plan to pay them off?

YES NO (I **will** stop adding to my debts and create a plan to pay them off!)

3. Do I save for periodic expenses such as car insurance, car repairs, vacations, and gifts?

YES NO (I **will** save money for periodic expenses and pay cash!)

4. Have I set up an emergency savings plan to cover my living expenses for 3-6 months if I become unemployed?

YES NO (I **will** save money for emergencies to cover 3-6 months of living expenses!)

5. Have I created a plan to save for my retirement and major expenses?

YES NO (I **will** save for my retirement and major expenses!)

Monthly Fixed Expenses

Monthly Fixed Expenses	Current Monthly Spending	Necessary Changes	Planned Budget
Mortgage #1			
Mortgage #2			
Auto Loan/Lease #1			
Auto Loan / Lease #2			
RV Loan			
<i>Home Equity Loan</i>			
Debt Consolidation/Other Loan(s)			
Student Loan(s)			
Rent			
Condo or Homeowner Association Fees			
Electricity			
Oil or Gas			
Water			
Garbage Collection			
Sewer			
Phone (land line)			
Cell Phone, Pager, PDA			
Cable/Satellite TV/TiVo Boxes			
Internet Access			
Car Insurance			
Health Insurance (if it isn't deducted from your paycheck)			
Long-Term Care Insurance			
Child Support			
Alimony			
Medical/Dental Payments			
Retirement Savings			
Emergency Fund Savings			
Other			
Total Monthly Fixed Expenses			

CHAPTER FIVE

Understanding and Using Credit

Introduction

While you may have decided at some point in your life never to use credit again, it is very likely that at some point in your future, you will choose to rely on credit to purchase goods or services you need. For this reason, it's important to understand the basics of using credit wisely. Used properly, credit and credit cards offer genuine convenience for everyone in our society. Used without enough care, they can create a financial nightmare. Additionally, your children will almost certainly have access to easy credit while they are still teenagers. You will want to help them learn to use credit wisely. Understanding and using credit prudently is an essential money management skill.

There are some significant advantages to using credit. Major acquisitions such as a car or a house would not be possible for most people without borrowing. Other expensive assets such as furniture or computers may also require the use of credit. Credit cards offer convenience, are safer than carrying large amounts of cash, and can be used almost anywhere in the world. They also make it easier to conduct transactions online, which may enable you to acquire goods at lower prices or more conveniently than going to a physical store.

But unwise or excessive use of credit can lead to substantial financial problems. Using a credit card often does not “feel” like really spending money, which makes it easy to forget exactly how much you have charged. It can also encourage a shopping spree that can leave a long-term financial hangover. The ease of using a credit card can lead to impulse spending and deprive you of money that should be used to build wealth through savings and investment. Unless you can pay off credit card bills in full at the end of each month, credit cards make your purchases more expensive in the long run because of interest charges and other fees.

Credit trouble is a serious problem in the United States (most recent data available):

- In 2003, total average household credit card debt in the U.S. was \$9,205; in the 1990's, it was \$2,966¹;
- In the fourth quarter of 2003, credit card delinquencies hit an all-time high²;
- In 2003, total national debt grew by more than 8 percent; 42 percent of that was household debt³;
- Estimated 2003 interest payments paid by consumers: \$80 Billion⁴; and
- Total credit card fees paid by consumers in 2003: \$31 Billion⁵.

¹ CardWeb.com, Feb. 2004

² CBS Marketwatch.com, April 2004

³ U.S. Federal Reserve Web site

⁴ CBS Marketwatch.com, April 2004

⁵ CBS Marketwatch.com, April 2004

CHAPTER SIX

Credit Reports and Credit Scores

In Chapter Seven we will look at how to rebuild your credit, but first you should understand how lenders decide whether or not to offer credit and on what terms they will offer it. You should also understand some of the tools you can use to affect your credit score.

Remember, lenders are in business to make a profit. They lend you money and collect interest on the loans. To do this successfully, they have to minimize their risks by limiting the number of “bad loans” that don’t get repaid. When you apply for a loan, lenders examine your credit history and assess the risk that you won’t repay the loan. Borrowers with the best credit records, higher incomes, and job stability tend to get the best terms because they are less likely to default on the loan. Higher risk borrowers will typically be charged higher interest rates or fees. And, if your credit record suggests too much risk, lenders may simply refuse to offer credit.

What Is Your Credit Report?

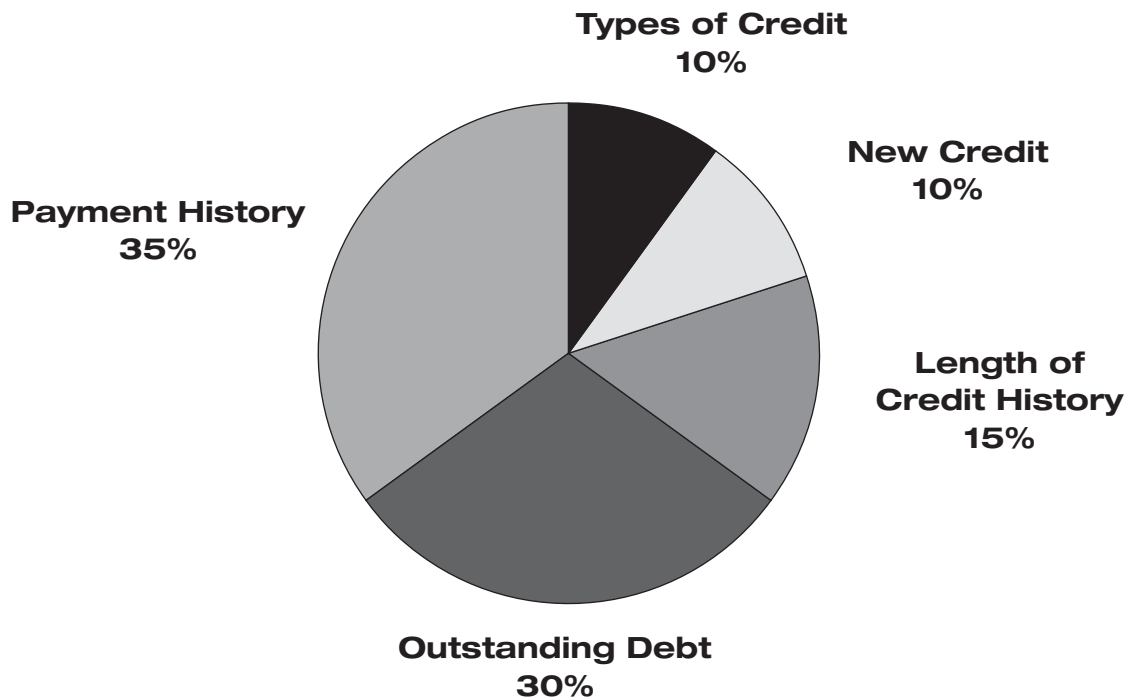
Your credit report is a compilation of data about you that has been gathered by credit reporting agencies or “credit bureaus.” The credit reporting agencies sell this information to lenders and other companies and organizations with a legitimate business need to know how you manage credit. How you handle credit today will affect your access to credit later, because lenders review your credit history when deciding whether to lend you money.

The information included in your credit report includes:

- **Identifying information** – including Social Security number, address and date of birth. This information is used to ensure that the credit report information is accurate and matched with the right person. It can also help detect and prevent identity fraud.
- **Employment history** – where you’ve worked and for how long.
- **Credit history** – account records with creditors.
- **Inquiries** – a list of who has requested your credit report.
- **Public records** – including collections accounts, bankruptcies, and late child support payments.

Most lenders use a mathematical formula to generate a “score” to help them determine if you are a good credit risk. This is called a “credit score” and the most frequently used version is the FICO score created by Fair Isaac and Company. A FICO score is a snapshot of your credit risk picture at a particular point in time. FICO scores range between 300 and 850 with higher values indicating a lower risk to lenders. To get the most from this exercise you must discuss the specific factors that caused your financial problems with your certified credit counselor. Some factors, like a period of unemployment, may have been beyond your control, but you also may have made bad choices. Whatever the specific circumstances of your bankruptcy, taking control of your future financial life requires an honest and thorough review of your pre-bankruptcy budget and a recognition of problem areas that need to be addressed.

Monthly Fixed Expenses



As you can see in Figure 6.1, your credit score is determined by five factors: payment history, outstanding debt, length of credit history, recent inquiries, and types of credit in use. Each of these factors is weighted differently to determine your score:

- **Payment History (35%)** - late payments, judgments, bankruptcy, and tax liens can lower your score.
- **Outstanding Debt (30%)** - maxing out your credit cards can lower your score.
- **Length of Credit History (15%)** - long relationships with banks and credit unions have a positive influence on your score.
- **Recent Inquiries (10%)** - too many inquiries in response to applications for credit within a short period of time can lower your score because it suggests you are frantic for credit and/or may soon be overexposed.
- **Types of Credit in Use (10%)** - too many open lines of credit (i.e. credit cards, retail accounts, installment loans, mortgage accounts) can lower your score. Loans from finance companies generally lower your score, especially when there are no other types of credit reported.

Get a Free Copy of Your Credit Report

A recent amendment to the federal Fair Credit Reporting Act (FCRA) requires each of the nationwide consumer reporting companies to provide you with a free copy of your credit report, at your request, once every 12 months, from each of the three major credit bureaus. A credit report reflects the history of your borrowing and payment practices for a seven-to-ten-year period.

To order your free credit report,

- Click on www.annualcreditreport.com, or
- Call 877-322-8228, or
- Send a request to:
Annual Credit Report Request Service
P.O. Box 105281
Atlanta, GA 30348-5281.

CHAPTER SEVEN

Rebuilding Your Credit

Developing Good Credit Habits

Whatever your personal financial situation, this chapter will outline successful strategies for rebuilding or improving your credit worthiness if it's been damaged. The chapter will also provide helpful information about shopping around for credit and managing credit card accounts.

So what do you need to do to improve or restore your credit? Here are some good credit habits that can help.

Manage Your Credit Card(s) Well

This is a big one and includes many important items:

- Check your credit report, as discussed in the previous chapter. Make sure that there are no errors on your report, and, if there are, report them immediately. Also check for missing information on accounts that are current because this information can boost your FICO score. Make sure that your credit report is accurate regarding your employment, current residence, and personal contact information. It does not have to include this information, but often will.
- If you still have open credit card accounts, keep at least one of them open (preferably an older credit card account). Consumers who use credit accounts moderately—charging low balances and repaying on time—are considered a better risk than those who do not use credit at all.

- If for some reason your credit card accounts have been closed, do not rush to apply for new cards. While it will help your FICO score to have a credit payment history, it will not help you to apply for a credit card before you are financially ready. Make sure that you are able to stick to your budget and start off small, perhaps with a gas station or department store card that you use for small purchases each month and pay off in full.
- You might find that you cannot get a traditional credit card account on your own; you need a co-signer or must apply for a secured credit card. A *secured* credit card requires you to deposit money into an account as collateral. Your line of credit is determined by the amount of your deposit. In effect, this is a convenience card that enables you to more easily conduct transactions without carrying a large amount

Pay Bills on Time

This goes with sticking to your budget—you should pay all of your bills on time to avoid late fees or increases in your interest rates from missed payments. This includes credit card payments, debts that you reaffirmed in bankruptcy, utilities, car loans, and rent or mortgage payments. Remember, all lenders will be looking at your payment habits to determine if you are practicing good financial behavior following your bankruptcy.

CHAPTER EIGHT

Predatory Lending and Identity Theft

In years past, an individual who had serious credit problems would have had few, if any, offers of credit. Recently, however, many lenders have developed specialized businesses that seek out and lend to individuals who have a history of credit problems. If you have had such problems, it is likely that you will begin receiving such offers in the mail or by phone. These offers may sound very much like the offers you received before your earlier credit problems began. **They are not!** Typically, they will involve much higher interest rates or other unfavorable terms. They will also come with much stiffer penalties for late payments or if you don't comply with complex loan requirements.

Lending to people with credit problems is a legitimate business. But some of these offers may come from “predatory lenders” who charge high rates and count on you to ultimately default. These predatory lenders then walk away with the profits from your payments and also repossess the items you bought with the loan.

Once you are back in the market for credit, you should know how to assess these offers. Following is a list of items to watch for when considering an offer of new credit. Most of the items listed below are legal but costly. A few, such as providing false information, are clearly wrong. If you believe a potential lender may be engaging in fraudulent or dishonest behavior, report it immediately to your local consumer affairs agency and end your contact with that lender.

Identity Theft

Identity theft is when someone uses your personal information (name, Social Security number, credit card information, etc.) without your consent to commit fraud and/or other crimes. The United States Office of Consumer Affairs reports that it received more than 685,000 consumer fraud and identity theft complaints in 2005. Consumers reported losses from fraud of over \$680 million.⁴

How Do Identity Thieves Get Your Personal Information?

- From businesses and other institutions by:
 - Stealing records while on the job
 - Bribing employees who have access to records
 - Hacking records
 - Conning information out of employees
- Stealing mail from your mailbox.
- “Dumpster diving” – rummaging through your trash, the trash of businesses, or public trash dumps.
- “Phishing” – stealing personal information through an email or phone in which they pose as a legitimate company and claim that you have a problem with your account.
- “Skimming” – stealing credit or debit card numbers by capturing the information in a data storage device that they have attached to an ATM or credit card machine.
- “Shoulder surfing” – looking over your shoulder for passwords and PIN numbers at ATM machines and stores.

⁴ Federal Trade Commission Report, “National and State Trends In Fraud & Identity Theft, January – December 2005.

Warnings Signs of Costly or Potentially Damaging Loans

Fees and Interest Rates

- High interest rates as calculated by the Annual Percentage Rate (APR)
- Unusual variable interest rate terms that can go up significantly on short notice. This includes “teaser” or introductory rates
- High fees and closing costs
- Significant prepayment penalties if you pay off the loan ahead of schedule
- Balloon payments (large amounts over and above your monthly payment at a future date, often to close out the loan)
- Negative amortization (your monthly payment will not keep pace with interest charged, so the amount of money you owe goes up even when you are making all of your required payments)

Other Loan Terms

- Credit insurance required as part of the loan
- Mandatory co-signers

Loan Purpose

- Suggestions by a lender that you refinance a recent loan it made to you. (Referred to as “flipping,” the practice of frequent refinancing generates substantial fees for the lender and growing expenses for the borrower.)
- Unnecessary debt consolidation

Documentation and Other Issues

- Post-dating documents
- Large loan broker fees or kickbacks
- Making unaffordable loans based on the value of your property
- Forged signatures
- Inaccurate income listed by the lender on loan applications
- Unrealistic (inflated) appraisals of your home’s value
- Terms at closing different from what you were promised
- Rush, rush, rush to close the deal

These are just a few of the more obvious warning signs. When in doubt, ask your certified credit counselor.

What Can Identity Thieves Do With Your Personal Information?

- They may open new credit card accounts in your name.
- They may change the address on your existing credit card accounts.
- They may open a bank account in your name and write bad checks on that account.
- They may file for bankruptcy under your name.
- They may take out a mortgage, auto loans, or establish phone or wireless service in your name.
- They may get a job or file fraudulent tax returns in your name.
- They may give your name to the police during an arrest. If they don't show up for their court date, a warrant for their arrest is issued in your name.

What Do You Do If You Think Your Identity Has Been Stolen?

- Contact the fraud departments of any one of the three major credit bureaus to place a fraud alert on your credit file. The fraud alert asks creditors to contact you before opening any new accounts or making changes to your existing accounts. As soon as one of the credit bureaus confirms your fraud alert, the other two credit bureaus will be automatically notified to place fraud alerts on your accounts as well. Credit reports from all three bureaus will be sent to you free of charge.

Equifax **1-800-685-1111;**
www.equifax.com

Experian **1-800-397-3742;**
www.experian.com

TransUnion **1-800-888-4213;**
www.transunion.com

- Close the accounts that you know or believe to have been tampered with or opened fraudulently.
- File a police report. Get a copy of the report to submit to your creditors and others who may require proof of the crime.
- File a complaint with the Federal Trade Commission (FTC). The FTC maintains a database of identity theft cases. That database is used to learn more about identity theft and how to prevent future cases. It is also used by law enforcement agencies for investigations.
FTC 1-877-438-4338 or
www.consumer.gov/idtheft
- Consult an attorney to determine legal action to take against creditors and/or credit bureaus if they are not cooperative in removing fraudulent entries from your credit report.
- Contact the local Office of the United States Trustee if a bankruptcy case has been filed fraudulently in your name.

CHAPTER NINE

What is Insurance For? Protecting Yourself from Financial Losses

All choices involve risk. For example, driving a car involves the risk of an accident. You can reduce that risk by limiting the amount of time you drive your car, walking, or by taking public transportation whenever possible. Or, you might take a defensive driving course to enhance your chances of avoiding accidents caused by somebody else's mistakes.

Similarly, insurance is about reducing financial risk. Auto insurance won't reduce your chances of being involved in an accident, but it will protect you from financial loss due to the car repairs, medical costs, or lawsuits that result from an accident. Buying health insurance reduces the risk that medical bills from a serious illness or injury will wipe out your savings or push you into deep debt. Homeowner's insurance won't prevent a fire, but it means you will likely be able to afford a new place to live if your home burns down.

Protecting yourself against sudden financial catastrophe is as much a part of good money management as paying your bills and accumulating wealth. Often, people look only at the cost of buying insurance and decide not to buy it because they don't receive anything tangible in return. But that's like saying seat belts are useless because they don't matter unless you become involved in an accident.

Does it really make sense to jeopardize all the hard work you've put in to build long-term, financial health by refusing to pay insurance premiums? Real financial wellness means protecting yourself against the financial impact of events such as illness or accidents that you can't control.

You may not be able to afford all of the insurance that you would like. You will have to make choices. For this reason, it is important to understand the types of insurance protections available, the cost of such insurance, and the ways to decide how much insurance is needed. This knowledge will enable you to make informed decisions.

When choosing insurance coverage, the best rule is to *"insure only what you cannot afford to lose."* In other words, if the loss would create a crippling economic burden and cause you major financial harm, then you should have insurance for that loss. This will create monthly or periodic expenses for the insurance, so make sure you include the cost in your budget. Paying for any type of insurance in the aftermath of financial hardship may be difficult, but not having insurance can lead to an even worse financial outcome. In fact, it's possible that inadequate insurance coverage is contributing to your financial problems. Part of the process of rebuilding your financial life involves spending a relatively small amount each month to protect yourself from a catastrophic loss. That's what insurance is for. But you also want to avoid buying more insurance than you need.

Cost of Insurance

Generally, you can buy insurance to cover any loss. However, the more insurance you have, the more it costs. Buying insurance is always a trade-off and depends upon how much risk you are willing to assume and how much risk you want an insurance company to take on. For example, most life insurance companies offer both term and whole-life insurance.

Types of Insurance

Type	Purpose	Examples of Coverage
Automobile	<ul style="list-style-type: none"> Provides financial protection from losses due to an auto accident or other damage to a car. Most states require licensed drivers to have automobile insurance 	<p>Collision: Provides for the repair or replacement of the policy owner's car damage in an accident</p> <p>Liability: Covers the cost of property damage or injuries to others caused by the policy owner.</p> <p>Comprehensive: Covers the cost of damage to an auto as a result of fire, theft, or natural disaster.</p>
Health	<ul style="list-style-type: none"> Provides payment of certain health care costs. 	<p>Basic: Covers office visits, laboratory, hospital costs, and routine care.</p> <p>Major Medical: Protects against large bills caused by catastrophic illness or injury.</p> <p>Dental and Vision: Covers some of the cost of routine exams and specific services.</p>
Renter's	<ul style="list-style-type: none"> Provides financial protection in case of loss of personal possessions in a rental unit. 	<p>Reimburses policy owner for loss of possessions in a rental unit due to fire, theft, water damage, etc.</p>
Homeowner's	<ul style="list-style-type: none"> Protects against financial loss from damage to your home or its contents, as well as injury to others on the property Most financial institutions require homeowner's insurance for mortgages 	<p>Physical Damage: Reimburses for fire or water damage to house or other structures on the property.</p> <p>Loss or Theft: Reimburses for personal property damage or stolen.</p> <p>Liability: Protects against loss from a lawsuit for injuries to people on your property.</p>
Life	<ul style="list-style-type: none"> Provides financial protection to the dependents of the policy owner when the policy owner dies. 	<p>Term Life: Offers protection for a specified period of time</p> <p>Whole Life: Offers protection that remains in effect during the lifetime of the insured and acquires a cash value.</p>
Disability	<ul style="list-style-type: none"> Provides income over a specified period when a person is ill or unable to work. 	<p>Policy owner selects a replacement income for lost wages if an illness or accident prevents the person from working.</p>
Long-Term Care	<ul style="list-style-type: none"> Pays for the daily care of the elderly or permanently ill. Care can range from occasional home visits to assisted living to full-time nursing care. 	<p>Policy owner determines a daily benefit amount and benefit duration. Additional features such as inflation protection can be added to the policy.</p>