

Dear John,

I wanted to take this opportunity to explain the credit scoring system to you since I feel credit scores are much more important than most people realize. On average, even a 10 point increase in your credit score will save you in excess of \$100,000 over the life of a \$250,000 30-year fixed loan.

Although seemingly complex and often confusing, your credit score is essentially based on five key factors, the first and most important being payment history.

35% of the score is based on how you handle your debt obligations.

- Pay all bills on time and try to avoid getting a tax lien or a judgment entered against you because those also affect your payment history in a negative way.
- Please note that paying a past due balance on a collection or charged-off account does NOT increase your credit score (due to flaws in the credit scoring software) and may even have the opposite effect more times than not. I do not suggest paying these types of accounts or even contacting these creditors when you are planning to apply for a home loan in the next six (6) months. Please let me clarify that I am not suggesting that you not pay these accounts, but that you consider waiting until after the loan closes to pay them since it can reduce your score and hurt your chances of getting loan approval. However, since not paying them can lead to a lawsuit being filed or the debt being sold to several collection agencies in the future - both of which will damage your credit even more in the long run -- one excellent solution would be to negotiate to pay or settle these accounts either concurrent with the loan closing or shortly after. An alternative would be to settle these types of accounts for deletion with payment if you are able to get the creditor to agree to do so. Just paying a collection will not get it deleted from your credit, it will only get it to show as a paid collection which still hurts the credit score.

30% of the credit score is derived from your revolving balances carried on accounts as they pertain to your debt utilization ratio.

- Revolving credit cards make up a very significant portion of what ultimately determines your credit score. Your total revolving credit utilization ratio is calculated as follows: Divide your Total Open Revolving Credit Card Debt into your Total Open Revolving Credit Card Limits gives you your Credit Card Utilization Ratio.

Example: \$15,000 of open credit balances divided into \$75,000 of available credit card limits =

20% Credit Card Utilization Ratio (debt ratio for short)

The closer to zero your Credit Card Utilization Ratio is, the better your credit score.

- Having a 0% debt ratio is ideal, so you want to keep your credit card balances as low as possible to maximize your credit score. **If you are able to do so, you should pay off or pay down your credit balances to enhance your score. But whatever you do, never close your credit cards, just pay them as close to zero as possible; don't close them.**
- If you are not able to payoff your credit cards there are still steps you can take to improve your credit scores. First and foremost, I suggest restructuring your credit card balances whenever you are carrying revolving credit card debt you can't pay to zero. Given the way that the scoring engine treats the accounts individually, **spreading your debt evenly across all cards will appreciably boost your credit score.**

Example: Assume you are not able to pay a dime on your current credit card balances but want to maximize your credit score by evenly distributing your debt among all

your cards by transferring balances. Assume you had a current debt ratio as described above as being 20%, given the below credit limits you would want to structure your credit card debt as follows:

Creditor	Current Balance	Current Limit	Ideal Balance (increases score 5 to 20 points)
Citibank	\$7,400	\$10,000	\$2,000
First USA	\$ 20	\$ 6,500	\$1,300
Dillards	\$2,244	\$ 9,000	\$1,800
MBNA	\$1,336	\$14,500	\$2,900
Chase	\$4,000	\$35,000	\$7,000
Total	\$15,000	\$75,000	\$15,000

The best way to accomplish the above redistribution example is to start with your lowest balance account and where possible, transfer UP to the ideal balance for that card. For example; on First USA, the above ideal balance should be \$1,300 and the current debt owed is \$20. In this example, you should use First USA to transfer \$1,280 onto Citibank in order to pay DOWN Citibank from \$7400 to \$6,120 in order to bring Citibank closer to the ideal balance of \$2000 but at the same time bring First USA from \$20 to the exact ideal balance of \$1300. Now that we have First USA exactly where it needs to be, we would then transfer \$3000 from Chase to Citibank to bring Chase to it's ideal balanced of \$7,000 and also bring Citibank closer to it's ideal balance of \$2000. Citibank would be at \$3,120 after this transfer is made. Now that First USA and Chase are exactly where they need to be, we would next move to MBNA, which we can transfer a total of \$1564 onto in order to bring MBNA up to it's ideal balance of \$2,900 and the others down to their ideal balances. The only 2 cards remaining we can transfer to is Dillard and Citibank. Dillards needs \$444 paid to it to achieve the ideal balance of \$1800, which leaves \$1120 remaining to transfer from MBNA. Since Citibank is the only card NOT at their ideal balance, we transfer the remaining \$1,120 from MBNA to Citibank to bring that balance from \$3,120 down to it's ideal balance of \$2,000 DONE !

Please note! Some revolving credit cards (mostly department store cards) do not allow you to transfer debt to another card, in which case the only option would be cash payments in order to get to your ideal balance.

Please keep in mind that this advice is meant to maximize your credit score. It does not take into consideration varying rates of interest that you may be paying on different credit card accounts. You may find that steps you take in order to improve your credit score for purposes of qualifying for preferred mortgage financing may need to be reconsidered and possibly reversed once that financing has been completed.

Please also note that it is impossible for both a husband and wife to get to their ideal balance if they carry joint credit cards because only one can get to the ideal balance and follow the advice exactly because the same balance will show on both credit reports; so if you had an ideal balance on a Discover card that suggests a balance of \$3244 and your spouse has an ideal balance for the same card as being \$500, it is impossible for both to achieve their ideal balance since that same card shows on both credit reports for the husband and wife. The best thing you can do is carry a balance somewhere in between the ideal balance of both spouses.

Another step you can take to improve your credit scores is to lower your debt ratio by raising your current credit limits. CAUTION: You need to approach this matter with due care. Call and ask each credit card company if they will increase your card limit based on a review of your payment history with them only. INSIST that you do not want them to pull your credit report and thereby create an inquiry that will damage your score. Some creditors will do this, some will

not. I do not suggest letting them pull your credit if you plan to make a credit purchase in the next six (6) months since the inquiry will decrease your credit score.

Now you know that the most important factor in determining your credit score is based on the handling of your debt obligations

Whether you pay your creditors on-time is 35% of the score

You also know that the second most important factor in determining your credit score is determined by the amount of debt you carry as it pertains to your revolving debt ratio

Revolving account debt ratio is 30% of the score

The remaining three factors that determine your credit score also offer you opportunities to enhance your credit score even further. Those factors are:

- **15% of the score is derived from the average length of time you have had credit.** The longer an account has been open, the better. Never close a credit card account; leave it open with a zero balance. You actually reduce your score by closing older accounts as your average account age will not increase in the future as quickly. The strategy described above on getting added as an authorized user to a seasoned "old" account can also help you "age" your average account in this area on top of what it does for your debt ratio.
- **10% of the score is derived from the mixture of credit you have on your credit report.** To maximize this area you want to have one mortgage, one car loan, and a few credit cards. The magic number of credit cards to have is three but it is never a good idea to close credit cards to get down to that number because closing the card does more damage than the increase received by having fewer cards.
- **10% of the score is derived from the number of times you apply for credit.** There are several types of inquiries but the only kind that hurt your credit score are those linked to an application for credit. In some cases, even asking for a credit limit increase is considered applying for a loan and can trigger the wrong kind of inquiry when the bank runs your credit as a result of the credit limit increase request. Pulling your own credit report online or directly through the credit bureaus is considered a personal inquiry and does not hurt your credit score. I suggest getting your credit report from each of the three credit bureaus at www.annualcreditreport.com. Federal law now allows you to get all three bureaus for free at this site once a year. Anytime you receive a pre-approved credit offer in the mail it is considered what the industry calls a "promotional inquiry" and will not affect your score either. Lastly, a current creditor of yours looking at your credit report without you asking them to is considered an "account review" inquiry and has no effect on your credit score.

Given the importance of credit scores in today's economy, I think it is crucial that you are informed and have the highest score possible. We can help you tremendously in the biggest area affecting your credit score: **Payment History**

Here's how:

If you have less than a 720 credit score, for every 10 points you increase your credit score on a \$250,000 30 year fixed loan, you will save on average of more than \$100,000 in interest over the life of your loan. We increase our client's credit scores an average of 25 points in 30 days and 50 points in 90 days. We charge an average flat fee of only \$1200 and back our work with a 100% warranty that says we will refund all of your money if we fall below 25% success rate in removing the negative items you hire us to remove, even if the sub 25% success rate only happens on one of the three bureaus.

Example: Assume you hire us to remove 10 negative items from your credit report and we are successful in removing all 10 from Experian and Equifax, but only remove 2

from Trans Union. In this example, you would receive a 100% refund because we fell below 25% removal on one bureau, even though we got all 10 removed from the other 2 bureaus.

I also want to ask that you also keep us in mind if you know someone that has less than a 720 credit score and refer them to us. I would be happy to do the same custom analysis for them too. Remember; not having the highest credit score possible can cost you more than \$500 a month extra on your mortgage payment and prevent you from having the best credit card and auto loan rates too. Please feel free to give me a call if you have any questions or need additional information.

Sincerely,

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