BRIEF DESCRIPTION OF THE PROPOSAL

This proposal would eliminate a government-sanctioned quasi-monopoly that, for more than a decade, has choked off innovation to the detriment of the mortgage market. As exists elsewhere in consumer lending, it would introduce an element of competition between the major developers of credit scoring models. This would benefit the economy, credit worthy consumers unfairly shut out of homeownership, lenders and the GSEs.

Since before the housing market collapse of 2008, Fannie Mae and Freddie Mac's seller-servicer guidelines have required mortgage lenders to price and underwrite their loans using credit scoring models that were developed using data from 1995 to 2000. This critical gateway today serves to discourage, disqualify, or "price out" many would-be borrowers, who today pay penalties as high as 3.25% based on their credit scores.

This requirement stands despite the availability of other validated scoring models that are more predictive, more inclusive, and more consumer-friendly. These other models are readily available and have been widely-adopted by lenders in the credit card auto, and personal lending industries, where there are no central utilities to entrench a requirement to use a legacy scoring model.

This proposal would require the GSEs to establish a process under which developers of credit scoring models could submit their models for evaluation, validation and possible approval by the GSEs for lender choice. In its capacity as regulator of the GSEs, the Federal Housing Finance Agency would have the authority to establish standards and criteria for any process used by either Fannie Mae or Freddie Mac to validate and approve credit scoring models. This proposal would not mandate that the GSEs necessarily adopt other scoring models but simply put in place a mechanism for consideration and review of other scoring models. Likewise, this proposal would not in any way undermine the rigorous underwriting standards in place today.

IMPACT ON ECONOMIC GROWTH

Implementation of this proposal would have a significant positive impact on economic growth. By allowing lenders to utilize newer, more predictive and more inclusive credit scoring models, they could identify creditworthy borrowers who are unscoreable under the legacy scoring model currently mandated by the GSEs – and do so without compromising credit quality. Lenders would not be lowering the bar, but simply widening the window. This would:

- Stimulate the purchase of both new and existing homes.
- Have a cascading effect of increased home construction and renovation, benefitting the building trades and suppliers of the building trades.
- Enhance local communities.
- Lead to increased mortgage lending activity, benefitting mortgage lenders both in the local community (community banks and credit unions) as well as those national in scope.
- Result in the increased sale of well-underwritten loans to Fannie Mae and Freddie Mac.

IMPACT ON THE ABILITY OF CONSUMERS TO PARTICIPATE IN THE ECONOMY

Private sector as well as government agency studies conclude that when utilizing the legacy credit scoring model mandated by the GSEs, 30 to 35 million consumers go unscored who are, in fact, scoreable using newer scoring models. Of that group:

- The average age is 46, nearly identical to the nationwide average.
- The average household income of $55,884 is in line with the national average.

While not all would get a "good" score, at a minimum they would get a score that would serve as a foundation on which to build. But significantly, about 7.6 million of those unscoreable under the legacy scoring model mandated by the GSEs would, in fact, obtain at score of 620 or above. How many of them might want and qualify for a mortgage? See the table below:

Begin	**7.6 million Expanded consumers with 620 or higher**
Exclude	Younger than 25 and older than 70
Exclude	Any indication of current homeownership
Exclude	Foreclosure on credit file
Exclude	Any 90-day delinquency in prior two years
Subtotal	**3.4 million potential borrowers**
Terms*	*How many can afford payments on median home in their Zip?*
4.2% rate	**2.8 million**
5.0% rate	**2.7 million**
6.0% rate	**2.6 million**

**Payment calculated assuming DTI less than 43% and 80% LTV*
Source: VantageScore Solutions

IMPACT ON THE ABILITY OF MARKET PARTICIPANTS AND FINANCIAL COMPANIES TO PARTICIPATE IN THE ECONOMY

Three separate surveys indicate a growing desire among lenders for the ability to choose among validated credit scoring models when underwriting mortgage loans.

- 52% of lenders responding to a SourceMedia (publisher of *American Banker*) survey in 2013 said they would consider a model other than FICO for mortgage originations if they could;
- 67% of lenders involved in the selection of which credit score model their institution will use responded to a Spectrum Associates survey in 2014 and said they were at least "reasonably likely" to adopt a new model that is proven to perform better than their current one; and most recently,
- 74% of lenders responding to a FTI Consulting survey in 2014 said they would consider using a different credit scoring model for their mortgage origination business if the GSEs didn't require the use of FICO scores.

There is no law, rule or regulation preventing lenders from utilizing a newer, more predictive and more inclusive scoring model; the only obstacle is an outdated requirement in the GSEs' seller-servicer guidelines. That provision persists even though, like other technologies, credit scoring models evolve over time and become more predictive and inclusive. The fact is that credit scoring models will continue to improve as competition feeds innovation.

LEGISLATIVE LANGUAGE

Legislation to address this issue entitled the "Credit Score Competition Act of 2017" was introduced in the House of Representatives in the 114th Congress as H.R. 4211 and was reintroduced on February 7th of this year as H.R. 898. The text of the "Credit Score Competition Act" is available at https://www.congress.gov/115/bills/hr898/BILLS-115hr898ih.pdf. The bill was introduced by House Financial Services Committee Member Rep. Ed Royce (R-CA) and at the time this was written had 10 cosponsors – 5 Republican and 5 Democrats. They are:

- Rep. Kyrsten Sinema (D-AZ)
- Rep. Terri Sewell (D-AL)*
- Rep. Gregory Meeks (D-NY)
- Rep. Robert Pittinger (R-NC)
- Rep. Pete Sessions (R-TX)*
- Rep. Jim Himes (D-CT)
- Rep. Carolyn Maloney (D-NY)
- Rep. Scott Tipton (R-CO)
- Rep. Mike Coffman (R-CO)*
- Rep. Al Green (D-TX)

** Not on House Financial Services Committee*

We hope to see the "Credit Score Competition Act" enacted into law this year. If it is it will be a win-win: More creditworthy consumers would get access to the mortgage credit for which they qualify and mortgage lenders would gain more customers.

OTHER BACKGROUND MATERIAL

Column by Kenneth H. Harney: *When will Fannie and Freddie switch to a new credit-scoring model?* Published: December 3, 2016 (http://newsok.com/article/5528899) in which he writes:

> *The two behemoths of the mortgage business, Fannie Mae and Freddie Mac, continue to use a credit scoring model that even its developer, FICO, says is not as "predictive" as its much newer models.*
>
> *Worse yet, Fannie and Freddie require that all lenders who want to submit loan applications to them must also use the same, outdated technology.*

Seven consumer organizations, trade associations and advocacy groups' letter to HUD, OCC, Federal Reserve, FDIC, FHFA and SEC dated October 30, 2013, in which they write:

"The problem is clear and the solution is simple:

- *The problem is that a regulatory bias that disenfranchises millions of potential well-qualified borrowers was unintentionally included in the CFPB's Ability-to-Repay / QM rule and that bias was unintentionally included in the Credit Risk Retention / QRM proposal when the regulators choose to make QRM the "mirror image" of QM.*
- *The solution is to require the GSEs to accept mortgages underwritten with other validated credit scoring models in addition to the single brand currently permitted."*

  - *American Financial Services Association*
  - *Asian Real Estate Association of America*
  - *Consumer Federation of America*
  - *National Association of Hispanic Real Estate Professionals*
  - *National Community Reinvestment Coalition*
  - *National Consumer Reporting Association*
  - *Woodstock Institute*

Mortgage Bankers Association letter to FHFA Director Watt dated November 5, 2014 in which they write:

> *"As the nation's housing markets continue their slow recovery, we are concerned that the GSEs' continued use of outdated credit scoring models may be adversely impacting the cost of credit for some American families—especially first-time, minority and moderate-income buyers."*

Eighteen consumer, civil rights and advocacy groups' letter to FHFA Director Watt dated November 14, 2014, in which they write:

> *… over 38 million consumers are potentially being treated unfairly due to the failure of Fannie Mae and Freddie Mac to adopt updated credit score models that better predict credit worthiness … We urge you to insist that Fannie Mae and Freddie Mac revise these policies immediately… The evidence is in: thirty-eight million consumers cannot wait for Fannie Mae and Freddie Mac to conduct further studies or engage in lengthy delays before changing these policies… The evidence is already in … There is no need to delay implementation of more updated models that would substantially benefit consumers. We urge FHFA to direct Fannie Mae and Freddie Mac to implement changes immediately …*

  - *National Consumer Law Center (on behalf of its low-income clients)*
  - *Americans for Financial Reform*
  - *Anderson, Ogilvie & Brewer LLP*
  - *Center for Economic Justice*
  - *Center for Responsible Lending*
  - *Community Service Society of New York*
  - *Consumer Action*
  - *Consumer Federation of America*
  - *Consumers Union*
  - *Empire Justice Center*
  - *HealthLawAdvocates*

- *NAACP*
- *National Association of Consumer Advocates*
- *National Council of La Raza*
- *National Housing Resource Center*
- *Philadelphia Unemployment Project*
- *Reinvestment Partners*
- *U.S. PIRG*

Eight trade associations, advocacy and civil rights groups' letter to FHFA Director Watt dated November 21, 2014, in which they write:

> *… For Hispanic and African American consumers, the country is faced with the lowest level of credit access in 14 years ... As organizations focused on expanding sustainable access to mortgage credit, we urge you to work with the GSEs to revise their seller-servicer guidelines to eliminate the requirement that all loans be underwritten using only FICO scores. Instead, by requiring the GSEs to accept loans underwritten using other empirically derived and statistically sound models it will expand homeownership opportunities and help responsibly expand the lending business… We understand there are alternative scoring models that will score up to 35 million more consumers than the legacy FICO model required by the GSEs. Because the previously unscoreable consumers tend to be immigrants, infrequent credit users and new entrants into the credit market, this important change could expand broad access to these important consumer segments and increase business for the industry.*

- *Asian Real Estate Association of America*
- *Center for Responsible Lending*
- *Greenlining Institute*
- *The Leadership Conference on Civil and Human Rights*
- *National Association of Hispanic Real Estate Professionals*
- *National Community Reinvestment Coalition*
- *National Fair Housing Alliance*
- *The Woodstock Institute*

Excerpt from testimony of Dory Rand on behalf of The Woodstock Institute at FHFA's "Duty to Serve" public listening session held at the Federal Reserve Bank of Chicago on January 25, 2017:

> *"Woodstock Institute has spoken repeatedly with FHFA about the possibility of including other scoring models like VantageScore solutions 3.0, in addition to the current FICO model. Credible research shows that the VantageScore model would make millions more creditworthy low and moderate income people and people of color eligible for homeownership."* [pp. 113-114]

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