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Mr. Joseph Otting
Acting Director
Federal Housing Finance Agency
Constitution Center
400 7th Street SW
Washington, DC 20219

Submitted Via: https://www.fhfa.gov/AboutUs/Contact/Pages/Request-for-Information-Form.aspx

Dear Acting Director Otting:

On behalf of the 1.3 million members of the National Association of REALTORS® (NAR), the following letter is in response to the Federal Housing Finance Agency's (FHFA) notice of proposed rulemaking (NPRM) on *Validation and Approval of Credit Score Models*. NAR has long advocated for a reassessment of the entire credit structure and an exploration of paths to increase the availability of mortgage credit to credit-qualified borrowers. NAR appreciates the FHFA's efforts to develop a framework for reviewing and introducing new credit models to the government sponsored enterprises (GSEs), but remains concerned about the ability to foster innovations in an environment with no competition.

The National Association of REALTORS® is America's largest trade association, including NAR's five commercial real estate institutes and its societies and councils. REALTORS® are involved in all aspects of the residential and commercial real estate industries and belong to one or more of some 1,200 local associations or boards, and 54 state and territory associations of REALTORS®. NAR represents a wide variety of housing industry professionals, including approximately 25,000 licensed and certified appraisers, committed to the development and preservation of the nation's housing stock and making it available to the widest range of potential homebuyers.

REALTORS® believe that homeownership is an integral part of the American Dream that should not be out of reach for individuals and families that lack a deep borrowing history and consequently, access to traditional forms of credit. By assessing the potential benefits and risks of new models and methods that the GSEs eventually adopt, credit and lending institutions could restructure and advance credit opportunity for millions of borrowers, while maintaining or improving market safety and stability.

Importance of Credit Scores

The availability of mortgage credit at a fair and reasonable cost is central to the home purchase transaction that, in turn, is central to the businesses of REALTORS®. Critical to the extension of credit is the credit score. REALTORS® see firsthand the negative impacts on consumers who are buying, selling, leasing, or renting properties when flawed or lacking credit scores make it hard or impossible for their clients to purchase homes.

Credit scoring is built on the credit history patterns of groups of individuals using consumer reporting agency (credit bureau or CRA) records. These comparative patterns translate into statistics used as the basis for estimating the likelihood of an individual to default in the future. Thus, credit scoring innovations are driven by changes in both modeling of credit data and by changes in the credit data itself.

Benefits of Alternative Credit

A borrower's credit score is crucial for entrance to the housing market; with a poor score, or none at all, a borrower stands little to no chance of obtaining a loan. Yet millions of Americans – particularly minorities, immigrants, and people with modest incomes – come from backgrounds that avoid debt, leading many to have little to no credit history. As a result, there must be ways to incorporate alternative credit data and innovations to enable these populations to access the mortgage market.

While expanding the system to incorporate innovations in credit scoring and data will necessitate an expense, such costs will be outweighed by the benefits afforded by extending ownership to millions more credit worthy Americans. The second factor in Section 1254.8 requires Fannie Mae and Freddie Mac (the Enterprises or GSEs) to conduct a fair lending analysis of new models as part of their "enterprise business assessment". The FHFA also requests comment on, "whether the credit score model has the potential to promote access to mortgage credit for creditworthy applicants across all protected classifications". However, the third factor in Section 1254.8, titled the "Impact on Enterprise operations and risk management, and impact on industry", directs the GSEs to, "consider whether the benefits of using credit scores produced by that model can reasonably be expected to exceed the adoption and ongoing costs of using such credit scores, considering projected benefits and costs to the Enterprises and borrowers, including market liquidity and cost and availability of credit." While the need to confirm *compliance* with fair lending laws and expand access is stressed, the NPRM does not explicitly direct the Enterprises to consider their public mission to support a national market for housing finance and support for underserved markets as an offset to costs. Therefore, the third factor of Section 1254.8 should be amended to reflect the enterprises' affirmative responsibility to support the public mission and the positive impact that a new score may have to expand the universe of credit worthy individuals and potential homebuyers as an offset to costs.

The Need for Different Models

The FICO Corporation and VantageScore Solutions, LLC. are private companies that provide credit scores based on their proprietary models to lenders, insurers, investors, and other users. Both companies have developed models that account for newer data as well as innovations in credit scoring. However, the GSEs currently only accept "classic" FICO scores, an older credit model built on data that existed prior to the financial crisis. REALTORS® view competition as critical to the development and adoption of innovations to meet the expanding needs of American homeowners. Furthermore, dependence on a single credit modeling company raises the counterparty risk to the GSEs, the public mission, and the entire industry that depends on the scores.

Introducing competition to a market with one actor, which has had decades to develop institutional knowledge and infrastructure, presents challenges. Late entrants must overcome high entry barriers as an incumbent has gained economies of scale in both cost and infrastructure. The capital and long-view required to take on such a task is often only available to large companies or oligopolies, who have a common interest with the new entrant, or government corporations. Indeed, it is reasonable to assert that VantageScore Solutions, LLC. has made inroads into the credit modeling industry due to its financial backing by the three credit reporting agencies. However, the FHFA asserts that the potential for vertical integration between a CRA and a credit score could undermine competition and harm consumers. To prevent such a problem, the FHFA proposes guidance to establish independence of a credit modeling company from the CRAs, but REALTORS® believe the FHFA should also create a separate set of rules that would level pricing and access to the credit infrastructure that credit modeling companies utilize.

With respect to independence, the FHFA proposes to require independence of credit modeling companies from CRAs, which could otherwise provide a competitive advantage. However, if the FHFA will require a company to divest itself of a CRA in order to prevent vertical integration, the FHFA should give reasonable time to allow aligned companies to mature sufficiently in order to compete with incumbent companies. VantageScore Solutions, LLC, was able to grow outside of the GSE market into a mature company. This experience suggest a model path for future credit scoring companies. However, once the FHFA accepts a score for integration into the GSEs, the FHFA should allow sufficient time for the company to divest itself of a parent company in a sustainable manner.

The FHFA should also analyze and provide guidance on the infrastructure for pricing and delivery of credit scores within the conventional mortgage space. Credit modeling companies should compete on the quality and accuracy of their scores, not through control of pricing, margins, and discounts or through control of the delivery of scores or other infrastructure. Though the Federal Trade Commission (FTC) and Consumer Financial Protection Bureau (CFPB) have jurisdiction over CRA and credit scoring regulation, the FHFA should consider guidance on how to level the playing field around the pricing and delivery of credit scores to lenders and investors, from both the CRAs and proprietary platforms. Competition could be limited and counterparty risk magnified in an environment without equal access to infrastructure or unfair control of pricing.

Tri-merge Score

Competition should extend beyond credit modeling and to the CRAs. The FHFA requested input on the usefulness of the tri-merge credit report in its *Credit Scoring Request for Input* from March of 2018, but did not reintroduce this question for this NPRM. The CRAs have grown in size over time and now each maintains a national footprint. Under the current system, an applicant for a mortgage pulls a tri-merge score, which displays the individual's credit score from all three CRAs and the middle score is used for underwriting. With the tri-merge report, the credit bureaus are not incentivized to improve the data in their repository, as each CRA's score is considered regardless of the overall quality of the data and analysis.

By allowing lenders to choose a score, conditional on a requirement that each lender continue to use a single scoring model for all originations over a fixed period of a year or two, lenders are likely to gravitate towards the score of the bureau with the best data. This in turn would incentivize the credit bureaus to improve their data, fix errors, and extend partnerships with other data vendors in order to integrate other sources of consumers' financial life such as telecom, utilities, and even bank statements. Thus, competition among the CRAs would help to foster better data and benefit consumers, lenders, investors, and the GSEs.

Conclusion

Adoption of innovations in credit scoring will help many more families achieve the American Dream by responsibly boosting consumer access to mortgage credit. NAR appreciates the FHFA's efforts to create a framework that would allow the GSEs to review and adopt new credit models. However, when evaluating the cost of adopting new models, the enterprises should balance the cost against their public missions. The FHFA also could aid the development and adoption of future innovations in credit scoring and reporting through guidance on how to improve access for new entrants and equalize the playing field for competition. Finally, competition should extend beyond the credit modeling companies to the CRAs. NAR appreciates the opportunity to provide input and look forward to continuing to work together on these important issues. If you have any questions, please contact me or NAR Senior Policy Representative, Ken Fears, at 202-383-1066 or KFears@REALTORS.org.

Sincerely,

John Smaby
2019 President, National Association of REALTORS®