Consumer Mortgage Coalition

March 15, 2018

Federal Housing Finance Agency
Office of Housing and Regulatory Policy
400 7th Street, N.W., 9th Floor
Washington, D.C. 20219

Re: **Credit Score Request for Input**

The Consumer Mortgage Coalition, a mortgage industry trade association, is very pleased to submit comments in response to the Federal Housing Finance Agency's ("FHFA's") request for information on altering the use of credit scores in connection with the sale of mortgages to Fannie Mae and Freddie Mac (the "Enterprises").

As the Enterprises regulator, FHFA is charged with ensuring that the Enterprises operate in a safe and sound manner and that their operations "foster liquid, efficient, competitive, and resilient national housing finance markets." In essence, the Enterprises' mission is to facilitate the expansion of credit, but only to consumers who are likely to repay their loans. Using an alternative scoring system that would approve otherwise ineligible borrowers will be harmful to borrowers and the communities in which they live, the broader housing market, and taxpayers.

Responsibly incorporating new information or non-traditional credit information, as has been done in the FICO Score 9, is appropriate because that information helps to confirm the borrower's ability and willingness to repay their loan obligation, and is transparent to the lender, credit analyst, guarantor, and investor. At the appropriate time, incorporating FICO Score XD would also be advisable because it also helps to confirm the borrower's propensity to repay their mortgage obligation for those taking the risk on mortgage loans -- guarantors and investors.

It has been suggested that the use of VantageScore will extend credit scores to a segment of the population that is currently unscorable or make otherwise ineligible borrowers sufficiently creditworthy so that they can purchase a home. Since both Enterprises already have programs in place for evaluating unscorable loans and Fannie Mae does not even use credit scores in its underwriting system, Desktop Underwriter (DU), it is unlikely that the use of VantageScore will expand the availability of mortgage credit to the targeted population. Moreover, as discussed further below, Vantage Score does not sufficiently assess the borrower's propensity to repay their mortgage obligation.

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Impact on the To Be Announced ("TBA") Market

Today, credit scores are largely used for the disclosure and summary of the loan's credit quality to guarantors and investors, so it is important to examine this issue from the perspective of the consumers of credit scores -- the lenders, credit analysts, guarantors, and investors. The consumers of credit scores want a single, reliable, stable benchmark for estimating credit risk in residential mortgages. Standardization is a critical component to the efficient operations of the secondary market, including the TBA market. Having alternative methods to measure default probability will be chaotic and impair the functionality of the secondary markets for residential mortgage loans, RMBS and MBS.

"Competing" credit scores might very well result in VantageScore loans being traded at a discount in the secondary market if it is proven that the credit scores for the currently unscorable population are unusually volatile. Borrowers in this class of loans could then face higher mortgage interest rates, as well as higher upfront guarantee fees, thus undoing much of the benefit that might have been expected by the targeted population. Additional research in credit score migration patterns and an examination of the options that FHFA may or may not decide to pursue is needed before a final determination can be made on this point, but the reaction in the TBA market is likely to be extremely negative.

Impact on the Credit Risk Transfer ("CRT") Market

While the reaction in the TBA market may be somewhat less certain without additional research, the risk in the CRT market is more predictable. The CRT market is of significant strategic importance to FHFA and the Enterprises, and credit scores are central to the strategy for building that market because they allow investors to track changes in the credit of a pool of loans over time, on an anonymized basis. Credit scores also allow investors to build and maintain credit risk models that assess and manage transferred credit risk accurately and inexpensively. This system was built on using FICO Scores, which are trusted by investors. So, allowing an alternative scoring system to be used would be highly disruptive with very negative consequences to the CRT program, which is still at a nascent stage.

Impact on Credit Quality

Inevitably, authorization of multiple scoring systems will result in arbitrage between them, and as has been proven historically, lead to a "race to the bottom." The result will not be a responsible expansion of credit, but degradation in credit scoring and underwriting standards.

As further background, the FICO scores and the VantageScore are based on the same underlying data, not the alternative data (e.g., rent, utilities, and telecommunications payments) that many support and that are now included in the FICO Score 9 and FICO Score XD systems. The major difference between the two scores is that the VantageScore drops its minimum scoring requirements regarding the length and recency of the consumer's credit history, thus reducing the VantageScore's predictive power. Less reliable scores will undermine the ability of lenders, investors, guarantors, and insurers to price credit and interest rate risk, and will very likely result in higher mortgage interest rates.

There is a consensus that using additional data, such as rent, utilities, and telecommunications payments[1] would be helpful in measuring a borrower's propensity to default and allow responsible consumers to improve their credit score without jeopardizing the value to guarantors and investors. FICO Score 9 includes all of telecommunications, utility and rental data that resides at the credit ratings agencies ("CRAs"). FICO Score XD incorporates all of the data included in FICO Score 9, but also other alternative data that is also available at the CRAs. Since FICO Score 9 and FICO Score XD already include the alternative data, there is no need to add another credit score, particularly if that alternative score, such as VantageScore, does not adequately assess the borrower's propensity to default.

Alternative scoring systems have been in existence for some years, so it is also important to note that portfolio lenders could use alternative scoring systems, such as VantageScore, but have chosen not to do so because it is inferior to FICO.

In addition, the ownership structure of VantageScore is also problematic. FICO is an independent, standalone firm that generates scores based on data it receives from each of the credit bureaus. The three credit bureaus – Equifax, Experian, and TransUnion – are a government-granted monopoly that control access to the consumers' credit files and control the pricing and distribution of competing credit scores, including the FICO score. As a result, they are in a position to steer the market to VantageScore, the scoring system three credit bureaus own. The decision to use a particular score should rest with the GSEs and their regulator, and investors. To do otherwise would set up a dangerous dynamic similar to the adverse incentives that were in place leading up to the 2008 financial crisis.

Impact on the Enterprises' Market Disclosures and Analysis

Currently, the Enterprises use credit scores and, more specifically, FICO for disclosure purposes. Among other things, the Enterprises' disclosures have enabled analysts to evaluate the availability of credit availability versus the need to manage risk because they are working from the same data set. Injecting alternative data sets would eviscerate the quality of the Enterprises disclosures and analysis. In turn, this would make it very difficult, if not impossible, to assess the Enterprises' performance, and prioritize and determine solutions for the major issues facing the conventional mortgage market.

Eliminate the Tri-Merged File Requirement

Today, Equifax, Experian, and Transunion have a shared monopoly in the consumer finance space because FHFA requires every consumer to purchase all three reports from the CRAs. As a result, the CRAs do not compete in the mortgage market. In the era of Big Data, there is no longer a reason to keep this outdated requirement in place. It simply adds to the consumer's cost and is an unnecessary expense.

Conclusion

The current system has been in place for over 30 years, and has performed well - even during the mortgage crisis. FICO scores are a dependable source of independent and objective data that has worked well for everyone in the mortgage complex – the investors, guarantors, lenders, insurers, and borrowers. As noted earlier, we would recommend that FHFA allow the GSEs to incorporate the FICO Score 9 at this time and, ultimately, move towards adoption of the FICO Score XD.

Furthermore, if FHFA and other federal regulators want to expand the availability of mortgage credit, they should begin by streamlining and updating the CFPB's regulations, including but not limited to the Qualified Mortgage rule, Ability to Repay rule, and the mortgage servicing regulations. They have needlessly and substantially increased borrower's costs and reduced the availability of credit to responsible and credit-worthy borrowers.

Thank you very much for your consideration of our views and recommendations.

Best regards,

Anne C. Canfield
Executive Director

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[i] It might also be helpful to incorporate the borrower's sensitivity to economic conditions, as well.