

Whalen Global Advisors LLC

March 18, 2019

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12 CFR Part 1254 "Validation and Approval of Credit Score Models"

To: Beth Spring, Senior Policy Analyst, Housing & Regulatory Policy, Division of Housing Mission and Goals, FHFA <Elizabeth.Spring@fhfa.gov>

To: Kevin Sheehan, Associate General Counsel, FHFA
<Kevin.Sheehan@fhfa.gov>

Dear Sirs:

With respect to the above request for information, please see my comments below.

First, as a general matter, the Congress has tasked The Federal Housing Finance Agency (FHFA) to propose a rule on the process for validation and approval of credit score models by the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) (together, the GSEs). This prospective assessment and validation process is a task that is arguably beyond the competency of either of the GSEs much less the FHFA.

Loan originators need to use credit scores when underwriting a loan, but neither of the GSEs really needs to use credit scores in their operations. Far from reflecting the convenience and needs of the mortgage industry or consumers, this absurd requirement is the result of political pressure by one of the credit reporting agencies (CRAs). The public record shows that this rule does not represent the convenience and needs of the investment community, the mortgage finance community or consumers.

Second, by the terms of the solicitation, it appears that only one provider of credit scores, FICO, is actually in a position to submit a complete application to the FHFA. None of the other providers of alternative scores, for example, seem to have sufficient usage in the mortgage finance sector to actually qualify. The solicitation states that "If an applicant's credit score lacks usage by industry to underwrite consumer credit, it may be approved initially for a pilot program only." Again, this whole process represents a needless expenditure of time and resources on an evaluation that necessarily must result in a single outcome.

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Thirdly, it needs to be stated again that there is no groundswell of demand for a new credit scoring methodology in the mortgage finance sector. As the FHFA has noted, it would take years for investors, rating agencies, lenders, regulators and the GSEs themselves to re-tool their systems and controls to accommodate a second credit score.

In addition, were the FHFA to actually allow the use of alternative credit scores, every major rating agency around the world would be required to revise existing default probability models and related ratings criteria, and submit these models and criteria for approval by global regulators. And this assumes that the FHFA could actually evaluate and approve a second provider of credit scores that is truly in use in the industry. Given the lack of viable alternatives, there does not seem to be any compelling cost benefit analysis to support the considerable time and expense required to even prepare to make such a change.

Finally, given the FHFA's previous public statements regarding the importance of independence of the analytic provider, again there does not seem to be a viable alternative to the current incumbent FICO. The fact is that FICO is the only independent provider of consumer credit score that does not have ownership ties to one or more of the CRAs. The FHFA has correctly identified this ownership link as an insoluble conflict of interest that cannot be mitigated. As the solicitation states:

“Each application must include a certification that no owner of consumer data necessary to construct the credit score model is related to the credit score model developer through any degree of common ownership or control.”

In addition, the FHFA has made clear in the past that no credit score provider may be affiliated with a CRA. “The proposed rule would prohibit an Enterprise from approving any credit score model developed by a company that is related to a consumer data provider through any common ownership or control,” the FHFA said in its rule breakdown at the end of 2018. “The proposed rule also would require an Enterprise to consider potential conflicts of interest and competitive effects in assessing the costs and benefits of approving any credit score model,” the FHFA continued.

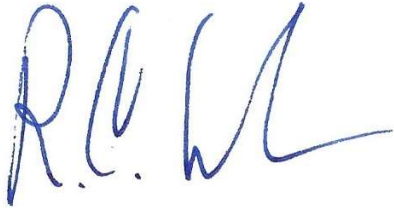
In view of the above, it appears that the subject rule making process is a terrible waste of time and resources. With all due respect, it appears that the FHFA has no alternative but to go back to Congress and tell them that this rule making requirement is without purpose and represents a waste of public resources.

Speaking as someone who has worked in the bond ratings business and as an analyst of commercial banks and mortgage companies for over three decades, the current rule making can only be viewed as a terrible waste of time and money. The FHFA has a duty to the taxpayer to use its limited resources in a

rational and effective fashion. I submit that moving forward with the subject rule as currently constructed is a complete embarrassment that should be halted immediately. The Director of the FHFA should stop the proposed rule making process and seek additional guidance from Congress.

I am happy to discuss any part of the proposed rule at your convenience.

Very truly yours,

A handwritten signature in blue ink, appearing to read "R.C. Whalen". The signature is written in a cursive, slightly stylized font.

Christopher Whalen
Chairman