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March 19, 2019

Alfred M. Pollard, General Counsel
Federal Housing Finance Agency
Eighth Floor
400 Seventh Street, SW
Washington, DC 20219

Re: Proposed Rule: Validation and Approval of Credit Score Models, Docket Number: 2018-27565, 83 Fed. Reg. 65575

Dear Mr. Pollard and the Staff of the Federal Housing Finance Agency,

On behalf of UnidosUS (formerly National Council of La Raza), we appreciate the opportunity to comment on the Federal Housing Finance Agency's (FHFA) Proposed Rule on the Validation and Approval of Credit Score Models by Fannie Mae and Freddie Mac (the Enterprises). Given the importance that credit plays in determining Latinos' access to purchase an affordable home, credit scoring models must be inclusive and fair. UnidosUS urges FHFA to require the Enterprises to evaluate the impact of their current use of credit scores and address homeownership disparities driven by the use of existing credit score models. Ultimately, UnidosUS believes the Enterprises should evolve in the way they use credit scoring information in their decision-making processes because a credit score provides only a limited snapshot into a borrower's full financial picture. FHFA's proposed rule presents an opportunity to achieve two goals: 1) improve the accuracy of evaluating the creditworthiness of borrowers inadequately scored or unscored by traditional credit reporting systems and 2) increase access to affordable homeownership opportunities for creditworthy low-and moderate-income borrowers, including Latinos.

UnidosUS is the largest Hispanic civil rights and advocacy organization. For 50 years, we have worked to advance opportunities for low-and middle-income Latino families, so they can achieve economic stability and build wealth. In this capacity, UnidosUS and its Affiliate network of nearly 300 local, community-based organizations in 35 states, the District of Columbia, and Puerto Rico, provide education, healthcare, housing, workforce development, financial coaching programs, and housing counseling to millions of families in the U.S. Over the last three decades, UnidosUS has conducted research and analysis and has on numerous occasions testified before Congress on issues related to improving the financial standing of Latinos. UnidosUS has also testified on the impact of credit scores on access to opportunity and strengthening the Community Reinvestment Act and the Home Ownership and Equity Protection Act (HOEPA), to support strong fair housing and lending laws, and to expand access to affordable credit.

UnidosUS has a long and successful history of working with the UnidosUS Wealth and Housing Alliance (UWHA), a network of housing counseling providers to further inform our understanding of how Latinos interact with the financial marketplace. The UWHA is the nation's largest network of community-based organizations working to empower Latino wealth-building through homeownership. As a HUD-approved housing counseling intermediary, the UWHA trains hundreds of housing counselors emphasizing individual, culturally competent counseling; building strong program infrastructure; and efficiently connecting other wealth-building programs, such as tax preparation and financial coaching. Established in 1997, the UWHA includes 50 independent organizations that support more than 60,000 families each year.

UnidosUS is further informed of Latinos' credit needs by the experiences of consumers using our lending model, Fuente Crédito. In 2016, UnidosUS developed a loan program to increase access to small-dollar lines of credit for Latino immigrants who needed assistance paying for the costs associated with naturalization. The program helps community-based service providers connect underserved Latinos and immigrants to credit unions, community banks, and Community Development Financial Institutions (CDFIs) which offer safe and affordable loan products to build credit and finance small-dollar expenses. Several lenders participating in Fuente Crédito obtain credit scores from the three largest traditional credit reporting agencies—Equifax, Experian, and TransUnion—in addition to alternative data bureaus, such as Clarity and LexisNexis, to help supplement the credit history for Latinos who have little to no formal history.

Background

Latinos compose nearly 18% of the U.S. population and represent one of the fastest-growing segments of the U.S. population.[1] As a younger population whose median age is 29, combined with substantial projected growth, Latinos' access to economic opportunities will be critical to shaping the nation's future. A positive credit history and score, and access to credit on affordable terms, are important factors to ensure that Latinos can fully achieve those opportunities.

Credit in the U.S. has been traditionally extended based on a credit score. While intended to be an impartial measure of an individual's creditworthiness, credit scores reflect and reinforce the widening racial wealth gap. Individuals with higher assets and higher incomes are more likely to have better credit history and a positive credit score because they have the security net to pay their bills on time, even when weathering a financial setback. This is demonstrated in data gathered from The Financial Clinic in 2017, which revealed that individuals with an excellent score of 750 or above had an average asset balance of $15,559, while individuals with a poor score of lower than 650 had an average asset balance of $1,343.[2] Latinos and other communities of color tend to have lower levels of wealth and are more likely to have lower credit scores. For example, the Urban Institute found that in 2013, only 41% of Latinos and 33% of Black

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[1] U.S. Census. *Quick Facts: United States.* Accessed February 2019. https://www.census.gov/quickfacts/fact/table/US/PST045217.

[2] "Analysis of Differences between Consumer- and Creditor-Purchased Credit Scores." Consumer Financial Protection Bureau. September 2012. Accessed February 2019. https://files.consumerfinance.gov/f/201209_Analysis_Differences_Consumer_Credit.pdf.

consumers had a FICO score of 750 or higher, while more than 64% of Whites had a score of 750 or higher.[3]

According to the CFPB, 26 million American consumers are credit "invisible," including one in ten adults whose credit information has not been reported to the major credit repositories.[4] An additional 19 million Americans have "unscoreable" credit files, including those who have credit files with insufficient information (thin) or have stale credit files and lack any recent credit history.[5] Communities of color and low-income communities are disproportionately credit invisible. For example, Latinos are almost twice as likely to be credit invisible or have unscored credit records than Whites or Asians in the U.S.[6] Similarly, consumers in low-income neighborhoods are also disproportionally credit invisible and are more likely to have unscorable credit files.[7]

Latinos are more likely to be credit invisible because mainstream credit scoring models capture and use a limited set of consumer data to assess credit risk, and this often makes Latinos and immigrants appear riskier than they truly are. For example**,** credit scorings systems fail to capture other relevant and predictive data that demonstrates Latinos' ability to make on-time payments, such as regular remittances to family in their country of origin, making rent payments, or cell phone payments—data that could improve a family's credit profile. In addition, young Latinos, like most young adults, are more likely to have an unscoreable credit file as they have not had many opportunities to establish a credit history. Furthermore, immigrants are often considered a credit risk because of a limited credit file. Immigrants are unable to transfer their credit history from their country of origin, and therefore, must start anew in building a credit score in the U.S.

A. How the Enterprises Currently Use Credit Scores:

The Enterprises currently use credit scores in three ways that inaccurately assess and price-out mortgage applicants with limited credit files, unscoreable files, or lower credit scores. First, some Enterprise loan programs require a minimum credit score, which can be a barrier to qualify for a loan for people of color, who are more likely to be credit invisible or have a lower credit score. Next, the Enterprises use a risk-based framework to price the loans they purchase, which takes into account the borrower's credit score. Under the current Classic FICO model, loans with lower credit scores receive greater price adjustments.[8] Finally, the Enterprises use credit scores within their automated underwriting systems (AUS). Even though the Enterprises allow lenders

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[3] Li, Wei. "Weaker Credit or Racial Discrimination: The Data are Unclear." 2014. Accessed February 20, 2019. https://www.urban.org/urban-wire/weaker-credit-or-racial-discrimination-data-are-unclear.
[4] "Who Are the Credit Invisibles? How to Help People with Limited Credit Histories." Consumer Financial Protection Bureau. December 2016. Accessed February 2019. https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201612_cfpb_credit_invisible_policy_report.pdf.
[5] Ibid.
[6] Ibid.
[7] Ibid.
[8] "Credit Fees in Price." Freddie Mac Single-Family Seller/Servicer Guide. December 5, 2018. Accessed February 2019. http://www.freddiemac.com/singlefamily/pdf/ex19.pdf. f

to issue loans without a credit score, these loans are priced as loans with the lowest credit score. Consequently, these borrowers face a significant interest rate hike and a minimum 10% down payment.[9]

To address these disparities, UnidosUS urges the FHFA to include explicit language in the proposed rule requiring the Enterprises to review their use of credit scores—including in their automated systems. The Enterprises should conduct an impact assessment of the credit scores they use, including how their use impacts the cost of a home loan to future borrowers. FHFA should also require the Enterprises to publicly report the results of their assessment and recommended actions.

B. Features of the Proposed Rule

1. Alignment of Enterprises:

To ensure greater transparency, efficiency, and consistency in lending guidelines, UnidosUS recommends that the Enterprises adopt a uniform approval process of new credit score models. This will enable the Enterprises—as separate entities—to learn how they each review and respond to emerging innovations and new approaches to credit risk assessment. As the Enterprises "test and learn" new approaches to credit risk assessment, they should harmonize their guidelines on which credit scores to approve, to ensure continuity and consistency. Without uniformity, the Enterprises will face divergent outcomes for potential borrowers, especially with regard to applicants with lower credit scores, credit invisible borrowers, or borrowers with thin credit files.

2. Credit Score Model Developer Independence:

UnidosUS supports FHFA's proposed rule to ensure credit score model developer independence. However, we are concerned about the conflicts of interest that exist in the current credit system: The Credit Reporting Agencies' (CRAs) have the ability to control credit data that is reported, have adopted FICO score models, and have maintained a financial interest in Vantage Score.[10] An effective way to address these concerns is to encourage greater competition between the credit reporting companies and data providers. For example, permitting the use of alternative data, such as cell phone, cable bill, or rent payment data from bank statements in scoring models would help alleviate current conflicts of interest in the credit reporting and scoring systems.[11]

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[9] "Underwriting Borrowers without Traditional Credit." Fannie Mae. April 2018. Accessed February 2019. https://www.fanniemae.com/content/fact_sheet/desktop-underwriter-nontraditional-credit-fact-sheet.pdf.

[10] *"Who's Keeping Score? Holding Credit Bureaus Accountable and Repairing a Broken System"*, 116th Cong. (2019) (testimony of Chi Wu), https://financialservices.house.gov/uploadedfiles/hhrg-116-ba00-wstate-wuc-20190226.pdf and U.S. Congress. House. Financial Services. *U.S. House Committee on Financial Services.*116th Cong. H. Doc. February 25, 2019. Accessed March 3, 2019. https://financialservices.house.gov/uploadedfiles/hhrg-116-ba00-20190226-sd002_-_memo.pdf.

[11] Goodman, Laurie, Jun Zhu, Rental pay history should be used to assess the creditworthiness of mortgage borrowers, Urban Institute, April 17, 2018. Available at: https://www.urban.org/urban-wire/rental-pay-history-should-be-used-assesscreditworthiness-mortgage-borrowers

C. Enterprise Solicitation of Applications from Credit Score Model Developers:

UnidosUS believes that the Enterprises must update their scoring systems more frequently than every seven years to keep pace with technology, changes in the financial marketplace and innovations in credit assessment models. A reliance on the same score models for seven years may cause the Enterprises' underwriting guidelines to become outdated and less inclusive for future borrowers who are more likely to be younger, Latino and people of color. These communities have had less access historically to mainstream credit and will have a range of non-traditional credit profiles.

D. Enterprise Initial Review of Submitted Applications

1. *Fair Lending Compliance and Certification:*

UnidosUS agrees with the requirement that credit score applicants obtain a fair lending certification. Applicants must clearly state that no characteristic that is based directly on, or is highly correlated with, a protected classification was used in the development of the credit score model or used by the credit score model to produce credit scores.

2. *Demonstrated Use:*

UnidosUS agrees that credit score model applicants should explain the demonstrated use of the credit score. Their use should not be limited to mortgage lenders and may be expanded to lenders, such as consumer lenders; banks; credit unions; and CDFIs. We also agree that limiting applications to models that have been used to make credit decisions in the past may impede innovation and the market's acceptance of new credit score models. As such, we believe the Enterprises should engage new, untested scores through pilot programs, and they should be tested rigorously before being implemented.

E. Credit Score Assessment

1. *Testing for Accuracy:*

While the current standard is to test credit score models with loans already approved or purchased by the Enterprises, continuing to do so could lead to confirmation bias. For example, the Enterprises could validate only the score models in a manner that reaffirms the accuracy of the scoring used to evaluate these loans and dismiss information that could demonstrate inaccuracy. This dismissed information could have influence over which credit score models are approved. To prevent this bias, the Enterprises should test new score models with a subset of loans that existing score models have difficulty assessing: loan credit files with deficient information, no credit score, and with slightly damaged credit histories. At a minimum, the Enterprises should include these credit profiles to test the accuracy of score models in pilot programs.

Data that has a weaker connection link to creditworthiness should be adopted with caution. For example, some lenders consider a borrower's educational background to predict their ability to repay. Data without an obvious connection to repayment comes with a higher risk of being inaccurate or in violation of fair lending laws.

2. Options for Evaluating Test Results

In the proposed rule, it is suggested that the Classic FICO score model be validated and approved because it is already being used by the Enterprises. UnidosUS believes that the Classic FICO must be validated and approved by the same process as any new credit score model applicant. If it is not, UnidosUS is concerned that as a legacy score model that relies on the limited data utilized by the CRAs, the Classic FICO would be given an unfair advantage.

Additionally, among the four credit score options the FHFA is considering, we believe that option 3—the benchmark-based approach—is the optimal choice. Option 3 would safely expand consumer access to credit by requiring all new score models to meet a statistical threshold, while stimulating competition between score providers, and minimizing the likelihood of consolidation. Unlike the other options, creating benchmarks would provide incentives for score providers to offer the best products and services at the lowest possible cost.

E. Enterprise Business Assessment

1. Fair Lending Assessment

UnidosUS agrees that each Enterprise should evaluate the fair lending risk and the fair lending impact of new credit score models according to standards and requirements of the Equal Credit Opportunity Act,[12] the Fair Housing Act,[13] and the Safety and Soundness Act[14] as part of the Enterprise Business Assessment. Additionally, we believe that this assessments should go do more than test for compliance. The assessment should consider whether the new credit score models could more accurately evaluate credit risk and promote access to credit for eligible borrowers across protected classes. For example, if a new score model was able to more accurately evaluate the risk of a borrower with no score, this would evaluate non-traditional borrowers more fairly, and subsequently price the loan more fairly.

G. Pilot Programs

UnidosUS supports FHFA's proposal to allow pilot programs to develop the performance history of models with limited demonstrated use by the financial services industry. In the past, the Enterprises worked with lenders and non-profit community-based organizations to design and implement pilot programs to test how, through the underwriting process, they can safely and accurately evaluate and qualify hard-to-reach and underserved borrowers for affordable home loans. As such, pilot programs that test new models and approaches can be one way for the Enterprises to respond to emerging best practices in the housing market.

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[12] 15 U.S.C. 1691(a)(1)
[13] 42 U.S.C. 3605(a)
[14] 12 U.S.C. 4545(1)

The Enterprises should conduct pilot programs with new credit score models for consumers who have lower credit scores, higher debt to income ratios, or borrowers who are perceived to be at greater risk of delinquency. For example, a pilot could test a subset of performing loans insured by the Federal Housing Administration—providing an opportunity to redefine Enterprise loan purchase requirements. In addition, a pilot program could require a manual confirmation of loans that have been rejected by the Enterprises' AUS, allowing for the Enterprises to refine the accuracy of the AUS. Without pilots to test several factors that have kept communities of color locked out of homeownership, the status quo will remain.

Piloting a supplemental score for the no score AUS, which includes integrating non-traditional credit information, would create opportunities for a fairer evaluation of credit invisible borrowers. There are several data sources that could supplement a score, including rental payment history, transaction history from bank account statements, shared secured accounts history, homebuyer education, and credit and financial education.

Thank you for your consideration. For any inquiries regarding our comments, please contact Agatha So, Policy Analyst at 202-776-1724 or aso@unidosus.org.

Sincerely,

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