Mr. Alfred M. Pollard
General Counsel
Attention: Comments/ RIN 2590–AA98
Federal Housing Finance Agency
Eighth Floor
400 Seventh Street SW, Washington, DC

March 21, 2019

Dear Mr. Pollard:

I write today regarding the Federal Housing Finance Agency's ("FHFA's") proposed rule to implement the Credit Score Competition provisions contained in Section 310 of the "Economic Growth, Regulatory Relief, and Consumer Protection Act" (S.2155 / Public Law 115-174) ("the Act") because I believe the proposed rule falls far short of fulfilling both the letter and spirit of the law. Competition among firms that produce consumer credit scores would benefit consumers by expanding the pool of borrowers approved by the Enterprises, reduce credit risk, lower costs, and foster innovation. This rule discourages competition by eliminating all existing potential competitors to the incumbent from consideration and discouraging new entrants from participating.

I applaud the Congress and the Federal Housing Finance Agency (FHFA) for carefully considering how the use of outdated credit scores might affect access to mortgage credit through the activities of the Enterprises, Freddie Mac and Fannie Mae. I base my comments on my more than 25 years in economic and credit-policy experience and having previously served as Senior Director and Deputy Chief Economist at Freddie Mac (2001-2011) and as Senior Vice President and Chief Economist at Equifax (2011-Feb 2019). I am currently an independent consultant and have received no compensation for my views as expressed here.

As relates to competition, FICO is a pure monopoly in the market for credit scores within the mortgage-finance market and is dominant in the nonmortgage finance market. This status was naturally derived as there are significant barriers to entry and FICO produces a quality product that carries substantial goodwill. Indeed, FICO produces many scores, and over the years has developed scores that are far superior to the FICO classic scores used by the Enterprises today. Thus, I believe the proposed rule is important in encouraging adoption of modern consumer credit scores by the Enterprises and I expect that any challenger models to the FICO stable of scores would have to be of the most robust form to be considered a reasonable option. Today there is only one such producer, VantageScore, that meets the robustness criterion, and their models are worthy of serious consideration under the goals set forth by the Congress in the Act

I believe the competitive concerns with the ownership structure of VantageScore to be greatly overblown. For historical context, all three national CRAs produce credit scores for sale that in theory could compete with FICO's sizeable offering of scores. These failed to gain much traction except for use in non-decisioning portfolio reviews by

financial institutions and for sale to consumers with credit monitoring products. These scores were maligned by consumer advocates as being "fake" scores as they are not widely used to make credit decisions and their sale to consumers has diminished as a result. It was not that these CRA-produced scores could not be used to make such decisions, or were not statistically robust, but rather that the CRAs were unable to convince many financial institutions that their scores were as good as the incumbent's score or if as good, worth the additional burden to explain to consumers should they be denied credit on the basis of the scores.

The methodological technology behind credit scoring generally is well-known, but recent advances by data scientists have created many innovative approaches to credit scoring (and, by extension, automated underwriting). Among them is the recently granted patent to Equifax for its neural decisioning model, which improves greatly on the limitations imposed by logistic regression, the underlying credit-score modeling method of choice for over 40 years. By the strict limitations imposed by the rule on providers of credit data, Equifax would be barred from developing a score for use by the Enterprises that could have the net effect of greatly expanding credit to credit-worthy borrowers that today would be denied on the basis of the traditionally-modeled score used by the Enterprises. A neural-decisioning score might also beat new scores developed by the incumbent but would not be eligible for consideration under the proposed rule. I think this is unnecessarily harmful to the goal of safely expanding credit opportunity in housing finance.

The idea that the CRAs pose a risk of ruinous competition because of their access to the data in their repositories is not supported by the historical record as cited above. Such laser focus on anti-competitive risks from vertical integration are giving undue weight to hypothetical problems and potential actions that are already illegal under federal antitrust laws. VantageScore Solutions, LLC was established in 2006 to be a viable competitor to FICO, but in the 13 years since has not been able to match the dominance of the incumbent, despite the ownership structure of the firm. No other firms today come as close as VantageScore to being a viable competitor to FICO, and I believe this proposed rule discourages entry in the future, unnaturally reinforcing the monopoly status of the incumbent.

Moreover, the rule requires demonstration that challenger scores are being used in lender decisions. VantageScore gained significant traction in nonmortgage lending use only over the past few years, likely due to its model accuracy and greater ability to score thin files, but despite its ownership structure it is not the dominant player in this segment. Demonstrated market adoption may be a reasonable criterion but by outright eliminating VantageScore, Equifax, Experian and TransUnion (and possibly others) from consideration serves to discourage new entrants from engaging as the burden is too high and is antithetical to the intent of Congress in its passing of this law.

While it is true that the three CRAs set the final prices for the data they sell and for the scores that are sold based on their data, FICO also sets the price for the use of its score algorithms that it charges the CRAs, and by passthrough, consumers. Thus, the

consumer pays for the data and the licensed model used to produce their score. Older models like FICO classic scores are cheaper than more sophisticated recent-generation scores, but not by much – price is not the primary obstacle to score adoption. As mentioned above, the CRAs were unable to gain adoption for their proprietary scores even at very low prices.

Importantly, I also fail to see how a CRA or other owner-interest arrangement in a data provider that produces a score for use by the Enterprises could use their position to raise prices to consumers beyond what the market currently bears under a pure monopoly provider. Federal antitrust laws already make such anticompetitive practices as imagined in the rule illegal. Further, adding competitors does not lead to less competition, and under the rule the Enterprises would have the option to replace the existing scores or add the use of new scores – the latter would increase competition only if the new added scores were from a different provider than the existing one or if replacement options were considered frequently and in open solicitations not limited to one provider.

Operationally there are material costs to adopting a new score, whether produced by the incumbent or a competitor. The many advances in data systems (computational power, storage, and transmission) over the past two decades, the demands for auditable decisions and data, transparency, etc. have reduced the direct costs of adopting a new element in an AUS system or allowing the flexibility of substitute factors. I believe that the Enterprises can support multiple scores within their systems and that this would be beneficial to consumers. Again, history bears testimony to how this could be done. Prior to 2008, the Enterprises allowed the use of approved third-party AUS systems – Freddie Mac and Fannie Mae both purchased loans approved on their competitor's systems. This did not cause issues that could not be overcome relating to reporting on loans, securities issuance, servicing, loan performance, etc. I do not believe the Enterprises do this today, however. There is a risk of adverse selection with the use of different systems simultaneously but specified acceptable uses such as limiting a particular lender to using one score model for all borrowers, careful monitoring, and pricing can be used to mitigate this risk. Another example of a substitute factor that is employed today is the use of either the purchase price or the appraised value of a property (whichever is lower) for calculating the decision loan-to-value ratio. Using one score versus another should not pose a greater burden from a modeling or investor perspective.

The lack of consumer understanding of credit scores is not inconsequential. A plethora of scores are already used throughout the nonmortgage lending market and opening the mortgage market to their use does not materially add to consumer confusion. However, the status quo does significantly more harm by denying credit-worthy borrowers the credit they deserve at prices that accurately reflect the risk they pose to the lender.

The rule envisions the use of data that is currently not provided by the three national CRAs. Such data does not currently exist with broad coverage not because the CRAs refuse to consider such data, but rather that the entities that would report such data are typically small (for example, much of the rental housing stock is held by investors with

only a few units) and they see little benefit to their organizations for the effort of reporting rental or utility payments. This may change over time or new data may be identified that would be appropriate for use in credit decisioning under existing law. There is nothing that bars the incumbent or VantageScore today from using the data that is available through the National Consumer Telecom & Utilities Exchange (sold through Equifax) or the rental payment data collected by TransUnion in creating new score models, but such efforts are wasted if the Enterprises do not allow for meaningful score competition.

Sincerely,

Amy Crews Cutts, PhD CBE®
Reston, VA