March 21, 2019

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

Re: Comments/RIN 2590—AA98

Dear Mr. Pollard:

U.S. Mortgage Insurers (USMI)[1] appreciates the opportunity to submit this response to the Federal Housing Finance Agency's (FHFA) notice of proposed rulemaking (NPR) for the Validation and Approval of Credit Score Models by Fannie Mae and Freddie Mac ("the Enterprises").[2] Private mortgage insurance (MI) companies have collectively helped more than 30 million American families attain homeownership over the past 60 years, including more than one million in the past year alone. As sophisticated managers of mortgage credit risk and an industry that is exclusively dedicated to the U.S. single family mortgage market, USMI and its members are devoted to a housing finance system backed by private capital that enables access to prudent and affordable housing finance for all creditworthy borrowers while protecting taxpayers. As the FHFA moves forward with assessing responses to the NPR and issues a final rule, USMI requests that the FHFA provide relevant data from the Enterprises to better inform industry stakeholders about the potential impact of new credit score models. Further, USMI urges the FHFA to adopt an implementation period of *at least* 24 months once any new model is validated and approved.

Credit scores are a prominent element in the U.S. housing finance system and are used by virtually all market participants, including private mortgage insurers (MIs), lenders, servicers, the Enterprises, and investors. The MI industry uses credit scores in a variety of ways, including to determine borrower eligibility, pricing, and to calculate the amount of capital required to comply with the Enterprises' capital and operational standards for MIs, the Private Mortgage Insurer Eligibility Requirements (PMIERs).[3] Credit scores are used to manage risk at the individual loan level and a borrower's credit score is a primary factor for MIs' pricing models. In addition to affecting MI pricing, credit scores play a critical role in determining the precise amount of capital to hold against individual mortgages as required by PMIERs' granular loan-

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[1] USMI is a trade association comprising the following private mortgage insurance companies: Essent Guaranty, Inc., Genworth Mortgage Insurance Corporation, Mortgage Guaranty Insurance Corporation, National Mortgage Insurance Corporation, and Radian Guaranty Inc.
[2] 83 Fed. Reg. 65575 (December 21, 2018).
[3] Fannie Mae PMIERs (updated September 27, 2018) available at https://www.fanniemae.com/content/eligibility_information/private-mortgage-insurer-eligibility-requirements.pdf; Freddie Mac PMIERs (updated September 27, 2018) available at http://www.freddiemac.com/singlefamily/pdf/PMIERs.pdf.

level capital requirements. Last year the FHFA issued a proposed rule on Enterprise Capital Requirements[4] that outlined a post-conservatorship capital regime for the Enterprises in which credit scores play a large role in determining loan-level capital charges. USMI urges the FHFA to carefully consider the interplay between the NPR and the proposed rule on Enterprise Capital Requirements considering the significant impact of credit scores (and any changes in credit score requirements/models) on capital requirements in the housing finance system. A change in the credit score regime utilized by the Enterprises would mean that the risk-based capital component of the proposed rule on Enterprise Capital Requirements would be incorrectly calibrated. The two key issues here are that the proposed rule is calibrated based upon the credit score model currently in use (Classic FICO)[5], and only refers to "Credit Scores" which in effect ignores the very real differences that can exist between versions for a particular model. Switching to a new credit scoring system would mean that a new notice of proposed rulemaking would be necessary to patch the Enterprise Capital Requirements to ensure that the proper amount of capital is being held.

Given the importance of credit scores in assessing, pricing, and managing risk, the FHFA must assure the MI industry and other market participants that any new approved credit score model is equal to or more predictive than the current model authorized for use by the Enterprises. Further, in order to minimize risks associated with adopting new credit score models and potential market confusion in the event that different models are validated and approved at the individual Enterprises, USMI recommends that the final rule require the Enterprises to engage an independent third party for purposes of conducting a joint Solicitation and Credit Score Assessment. While the NPR permits the Enterprises to use an independent third party for the Credit Score Assessment component of the validation and approval process,[6] it does not permit that option for the Solicitation of credit score models.[7] To best mitigate potential marketplace disruption and promote a uniform understanding of borrowers' representative scores across the housing finance ecosystem, the final rule should require the Enterprises to jointly validate and approve credit score models using an independent third party.

Considering that changes in credit scoring will materially affect market participants' business operations, processes, and technologies, it is imperative that the FHFA and Enterprises maximize transparency by engaging with industry on changes related to credit score models and requirements at the Enterprises in order to identify potential issues and challenges. The NPR would require the Enterprises to "consider impacts of a new credit score model or models and the impacts that updating may have on the entire mortgage finance industry."[8] Changes in credit scoring requirements/models at the Enterprises will reverberate throughout the conventional mortgage market and cause MIs to revamp pricing, lenders to modify pricing models and overlays, and MBS and CRT investors to update valuation and performance models. USMI is pleased that the Enterprise Business Assessment will seek to address "business considerations in

[4] 83 Fed. Reg. 33312 (July 17, 2018).
[5] Since 2004, the Enterprises have required the use of FICO 5 from Equifax, FICO 4 from TransUnion, and FICO Score from Experian, which are collectively referred to as "Classic FICO."
[6] 83 Fed. Reg. 65591.
[7] 83 Fed. Reg. 65590.
[8] 83 Fed. Reg. 65587.

terms of the impact, benefits, and costs of adopting or changing a credit score model on market participants, market liquidity, and the cost and availability of credit."[9]

While the NPR requires the FHFA and Enterprises to work with market participants, we ask that industry participants be given access to historical data and the Enterprises' empirical evaluation of credit score models in order to better identify potential issues and challenges associated with changes in credit score requirements. This will allow industry participants an opportunity to provide analysis and feedback on models' accuracy, impact to borrowers, and interactions with various systems throughout the housing finance system.

Finally, Section 310 of the Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018[10] does not specify a timeframe for the adoption of a new credit score model following announcements from the Enterprises and the NPR would only require the Enterprises to "provide notice to the industry about expected timing of changing any credit score model requirements."[11] While the NPR recognizes that industry participants suggested a 18-24 month adoption period in their submission's to the FHFA's 2017 Credit Score Request for Input,[12] USMI is concerned that the NPR lacks a concrete timeline for implementation or meaningful discussion on the need for an appropriate lead time to ensure a smooth transition to a new credit score model. The NPR states that the "FHFA expects that the Enterprises would develop a plan to update their requirements of approved score(s) in a timely manner taking into account the timeframes necessary for any system updates and industry concerns on adequate time for implementation in an orderly matter."[13] USMI strongly urges the FHFA to adopt an adoption period of *at least* 24 months in the final rule for the Validation and Approval of Credit Score Models to reflect the operational complexities associated with migrating to a new credit score model.

USMI appreciates the opportunity to comment on the FHFA's NPR for the Enterprises' Validation and Approval of Credit Score Models and questions or requests for additional information may be directed to Lindsey Johnson, President of U.S. Mortgage Insurers, at ljohnson@usmi.org or 202-280-1820.

Sincerely,

Lindsey D. Johnson
President

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[9] 83 Fed. Reg. 65587.
[10] Pub. L. 115-174 (May 24, 2018), Section 310 codified at 12 U.S.C. 1454(d).
[11] 83 Fed. Reg. 65588.
[12] Federal Housing Finance Agency, "Credit Score Request for Input," December 20, 2017, *available at* https://www.fhfa.gov/Media/PublicAffairs/PublicAffairsDocuments/CreditScore_RFI-2017.pdf.
[13] 83 Fed. Reg. 65588.