National Consumer Law Center
(on behalf of its low-income clients)
Atlanta Legal Aid Society, Inc.
Connecticut Fair Housing Center
Consumer Action
Demos
Jacksonville Area Legal Aid, Inc.
National Association of Consumer Advocates
U.S. PIRG
World Privacy Forum

March 21, 2019

Via regulations.gov and RegComments@fhfa.gov
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400 Seventh Street SW, 8th Fl.
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Re: Comments/RIN 2590-AA98, Validation and Approval of Credit Score Models

The undersigned consumer and advocacy groups are pleased to submit the following comments in response to the Federal Housing Finance Agency (FHFA)'s proposed rule[1] on the process for validation and approval of credit score models used by Fannie Mae and Freddie Mac, collectively the Government Sponsored Enterprises (GSEs). The proposed rule fulfills the requirement for FHFA to issue regulations governing this issue, as set forth by Section 310 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA) of 2018, Pub. L. No. 115-174.

A. *We Agree that the Credit Score Model Developer Should be Independent of the Data Sources*

Perhaps the most consequential, as well as most controversial, aspect of the proposed rule is the provision at § 1254.6(A)(4) prohibiting the GSEs from approving any scoring model developed by a company that is related to a consumer data provider through any common ownership or control, of any type or amount. VantageScore, - which is FICO's primary competitor and a joint venture of Equifax, Experian and TransUnion - had charged that this provision eliminates competition in the credit scoring market and will stifle innovation.[2] In fact, the FHFA's approach will promote innovation and limit the harms posed by vertical integration of the consumer data providers with the scoring model developer.

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1 83 Fed. Reg. 65575 (Dec. 21, 2018).
2 Press release, VantageScore Solutions Issues Statement Reacting to FHFA's Proposed Rules for Validating and Approving New Credit Scoring Models, Dec. 17, 2018, https://www.vantagescore.com/news-story/292/vantagescore-solutions-issues-statement-reacting-fhfas-propo ("Should the proposed rule stand, the federal government would be picking winners and losers to the detriment of millions of consumers.").

Certainly consumer groups are in favor of competition and believe that competition is a good thing. While there may be some advantages, in theory, to having more than one scoring model and an alternative developer in the market, the paramount consideration is that the credit reporting system is an entirely anomalous market in which competition does not and cannot play its normal role.

If one simply views credit scores and modeling developers in isolation, it may appear that having one company provide scores – *i.e.*, FICO - indicates there is a lack of competition. However, as FHFA has rightfully recognized, the market must be analyzed in the context of the entire credit reporting system, which includes the nationwide consumer reporting agencies (CRAs), *i.e.*, Equifax, Experian and TransUnion, which own the underlying credit information needed to generate credit scores.

From that perspective, this market is extremely dysfunctional and anti-competitive. As we and many others have repeatedly noted,[3] there is essentially no competition in the credit reporting market. While there are 3 nationwide CRAs, it is not even really an oligopoly, because consumers have no choice to decide between these three companies -- we are their commodity not their customers. If we want credit or in some cases, a job or apartment, we are forced to deal with all three companies. Even for mortgage lenders, there is no competition because they must pay for and use credit reports from all three credit bureaus.

With this highly abnormal market, FHFA is right to be concerned about the possible consequences of vertical integration. While there appears to be nothing inherently defective about the credit score produced by VantageScore, we would be extremely concerned if by virtue of vertical integration, it became the dominant score and drove FICO out of the market. If the Big Three nationwide CRAs owned both the underlying credit data and the only scoring developer, competition and innovation would decrease due to the expanded concentration of market power.

Finally, we note that, while not ideal, having FICO as the dominant credit score on the market and the only scoring model provider for the GSEs has not stifled innovation. In fact, it is FICO that has released two of the three new products using alternative data – FICO XD and UltraFICO, discussed below. We note that VantageScore has not released any scoring models that do not use nationwide CRA data, perhaps due to the fact that it is owned by all three of those companies.

B. *We Applaud FHFA for Permitting the GSEs to Engage in Pilot Testing Initiatives of New Scoring Methods*

As discussed above, one of the inherent problems in the credit reporting and scoring market is the lack of choice and competition in dealing with the nationwide CRAs. Thus, creating real competition in the credit reporting and scoring market will not just be about the scoring models – it will require competition in the underlying data sources. Both FICO (Classic and FICO 9) and

[3] *See, e.g.*, Who's Keeping Score? Holding Credit Bureaus Accountable and Repairing a Broken System," Hearing before the H. Comm. on Fin. Serv., 116th Cong., (2019)(testimony of Chi Chi Wu, National Consumer Law Center).

VantageScore use the same data: the files of the nationwide CRAs, which have been problematic in terms of accuracy and poor treatment of consumers.[4]

Thus, real competition can only come about when credit scoring models start using new sources of data. This of course dovetails with the issue of "credit invisibility," *i.e.*, the fact that 26 million Americans (or about 1 in 10) do not have a credit history and 18 million are unscorable because their histories are too scant ("thin") or old. As we said in our March 2018 comments, we have urged a cautious, devil-is-in-the-details approach to the use of alternative data. However, that does not mean we think there should be no attempts to experiment with alternative data.

Thus, we strongly support proposed § 1254.11 allowing for pilot programs to test new scoring models. This is perhaps the most important part of the proposed rule. And it will be the provision with the most long-lasting impact in terms of encouraging innovation and progress. We applaud FHFA for permitting the GSEs to engage in pilot initiatives.

We think there are several new models that are worth testing in pilot programs. For example, UltraFICO is a voluntary opt-in product that will rely on bank account transaction information from Finicity, a data aggregator working in partnership with Experian.[5] Bank account transaction/cashflow data appears to be a promising form of alternative data. This data can potentially incorporate an analysis of ability to repay, since it includes both income and expense information. It does carry some risks, as it could be misused to undertake debt collection efforts and could include sensitive information such as debit card purchases showing where the consumer shops. But as it is currently structured, UltraFICO does not implicate those concerns. Transaction data, depending on how it is used, could implicate privacy and disparate impact issues, but our understanding is that UltraFICO simply analyzes cashflows, not where people shop.

ExperianBoost is another new scoring model worth consideration. While we have consistently opposed efforts to include monthly gas and electric utility payment history for all consumers in the files of the nationwide CRAs without choice, we do not have a similar opposition to opt-in use of such data. Thus, ExperianBoost considers utility payments, but does so by reviewing bank account transactions that do not get included in traditional credit reports and is voluntary opt-in by the consumer.[6]

Another alternative data score that may merit consideration is FICO's XD score, which uses data from specialty consumer reporting agencies such as the National Consumer Telecom and Utilities Exchange, which we understand overwhelmingly (over 90%) consists of payment information from telecommunication companies. Using data not in the nationwide CRA files to create special scores for otherwise unscoreable consumers is preferable to the wholesale addition

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[4] *See* Chi Chi Wu, et al., National Consumer Law Center, *Automated Injustice Redux: Ten Years after a Key Report, Consumers Are Still Frustrated Trying to Fix Credit Reporting Errors* (February 2019), https://www.nclc.org/images/pdf/credit_reports/automated-injustice-redux.pdf.

[5] https://www.fico.com/ultrafico/.

[6] https://www.experian.com/blogs/ask-experian/introducing-experian-boost/ (Dec. 18, 2018).

of the same data to traditional credit reports, where it might damage consumers who already have a credit score.

We urge FHFA and the GSEs to engage in pilot studies on the use of UltraFICO, Experian Boost and FICO XD scoring models in their underwriting. There is a significant possibility these scores may be able to help thin or no file consumers, and expand access to mortgage credit without creating greater risk.

C. *The Timelines Set Forth in the Proposed Rule are Much Too Long and May Violate Statutory Requirements*

The timelines set forth in the proposed rule are extremely lengthy, adding up to an over two-year period (as shown below) from the time a GSE begins publication of a solicitation to the beginning of implementation. This is an inordinately long period of time, given that FHFA has already been working on this issue and assessing FICO 9 and VantageScore 3.0 since 2015, or nearly 4 years. It is a bit perplexing that FHFA and the GSEs require another 2 years to make a decision.

Phase	**Time period**
Credit Score Solicitation Publication	90 days
Solicitation Phase	120 days
Credit Score Assessment Phase	180 days
Possible Extensions	2 x 30 days = 60 days
Enterprise Business Assessment Phase	240 days
Approval Determination with Notification	45 days
TOTAL	734 days or *over 2 years*

This overly extended time period also violates the intent, and perhaps the letter, of Section 310 of the EGRRCPA. Section 310 specifically requires the GSEs to:

> make a determination with respect to any application submitted [for validation and approval of a scoring model], and provide notice of that determination to the applicant, before a date established by the corporation that is not later than 180 days after that date on which an application is submitted to the corporation.[7]

Section 310 does allow for two thirty-day extensions past the 180 days. However, it certainly did not contemplate an additional 240 days for a separate "Enterprise Business Assessment" plus another 45 days for notification. And Congress certainly did not anticipate that the entire process would take over two years.

The proposal to have a separate "Credit Score Assessment" and "Enterprise Business Assessment" with a total of 420 days (plus 60 days in extensions) is playing fast and loose with

[7] 12 U.S.C. § 1717(b)(7)(G)(i); 12 U.S.C. § 1454(d)(7)(A), added by Pub. L. No. 115-174, § 310.

requirements of Section 310. It certainly violates the intent of the statutory timeline that any assessment of the credit scoring model be concluded within 6 months plus extensions – not 14 months plus extension. We urge FHFA to require that both the "Credit Scoring Assessment" and the "Enterprise Business Assessment", as well as any other Assessment plus any notification period, take place within 180 days. Any other timeline could be challengeable as a violation of Section 310's plain language.

Finally, for the first round of applications, we believe that the GSEs should be permitted to use any testing results from previous rounds of review that occurred during the 2015 to 2018 time period prior to the passage of EGRRCPA. As FHFA notes, in 2015, the Agency and the GSEs "conducted an in-depth review of three models: Classic FICO, FICO 9, and VantageScore 3.0".[8] There is no reason to waste the significant resources devoted to conducting this in-depth review. Any information or results from that review should be considered when applications for any of these models are submitted. This should greatly shorten the time needed for assessments of these scoring models.

D. *The FHFA's Proposed Rule Should Include Greater Consideration of the Interests of Borrowers/Consumers*

The proposed rule primarily focuses on the needs of, and impact on, GSEs, lenders, investors and other members of the mortgage industry vis a vis updating scoring models. As with the previous December 2017 Request for Input of Credit Scoring Models, we urge FHFA to equally consider the needs of and impact on consumers and to do so throughout the entire process of approving or rejecting a scoring model. FHFA's website highlights stability and access in the housing finance market as two agency missions; incorporating the needs of consumers into the development of the proposed rule will help meet those goals.

First, one of the explicit criteria for the initial credit score assessment should be whether a scoring model will expand access to mortgage credit for borrowers. Nowhere in either the Credit Score Assessment or Enterprise Business Assessment is there any consideration of this critical factor. FHFA does request comment on whether it should include this factor in the fair lending assessment with respect to expanding access to credit for protected classes.[9] However, we think this consideration should be in the initial credit score assessment as a factor in any of the approaches for evaluating test results. Thus, for example, the Comparison-Based Approach should evaluate whether a new credit model produced scores that are more accurate or just as accurate but approve more borrowers than the old model. If FICO 9 has the same accuracy rate as Classic FICO but approves more borrowers without losing any predictiveness, then the GSEs should approve FICO 9.

Second, impact on consumers should be explicitly included in the Enterprise Business Assessment. Proposed § 1254.8(b) lists five criteria for this assessment, including (1) accuracy & reliability; (2) fair lending assessment; (3) impact on GSE operations and risk management, and impact on industry; (4) competitive effects; and (5) third-party vendor review. We believe that criteria (3) should also include impact on consumers. Thus, the cost-benefit analysis

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[8] 83 Fed. Reg. at 65,576.
[9] 83 Fed. Reg. at 65587.

discussed on criteria (3), proposed § 1254.8(b)(3), should not be limited to the benefits to the GSEs, industry operations and mortgage market liquidity, but should also include benefits to consumers in terms of greater access to mortgage credit and lower costs for borrowers.

Third, benefit to consumers should explicitly include reducing the unfair impact of medical debt. Medical debt has tremendous impact on credit reports and scores, affecting one in five consumers with a credit report.[10] As the Consumer Financial Protection Bureau has found, medical debt unfairly penalizes a consumer's credit score by 10 points, and for a medical debt collection item that is subsequently paid, by up to 22 points (*i.e.* the consumer's credit score should actually be 10 points or 22 points higher).[11] In addition, as discussed in our comments on the December 2017 RFI on Credit Scoring Models, medical debt also has a racially disparate impact.[12] Reducing its harm by updating to FICO 9 may also help with the yawning racial divides in mortgage lending.[13]

Conclusion

If nothing else, Section 310 stands as a rejection of the status quo with respect to scoring models. In adopting Section 310, Congress recognized that the need for improvement and progress outweighed the potential cost for the GSEs and industry to adopt a new scoring model.
We urge that this process of updating credit scoring models, already over four years in the making, proceed in as expeditious a manner as possible, and that the final regulations encourage a speedy process that benefits consumers.

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[10] Consumer Fin. Prot. Bureau, Consumer Credit Reports: A Study of Medical and Non-Medical Collections 5 (Dec. 11, 2014), www.consumerfinance.gov (finding that 52.1% of debt collection tradelines on credit reports were for medical debt).

[11] Consumer Fin. Prot. Bureau, Data Point: Medical Debt and Credit Scores (May 2014), www.consumerfinance.gov. *See also* Consumer Fin. Prot. Bureau, Consumer Credit Reports: A Study of Medical and Non-Medical Collections 7, 28 (Dec. 11, 2014), www.consumerfinance.gov (consumers whose credit reports show only collection items consisting of medical bills are more reliable payers, owe less, and have more available credit).

[12] National Consumer Law Center, et al., Consumer Group Comments in Response to FHFA Request for Input Regarding Credit Scores, March 30, 2018, https://nclc.org/images/pdf/credit_reports/comment-fhfa-rfi-credit-scores.pdf.

[13] Aaron Glantz and Emmanuel Martinez, Center for Investigative Reporting, Kept Out: For people of color, banks are shutting the door to homeownership, Reveal, Feb. 15, 2018, https://www.revealnews.org/article/for-people-of-color-banks-are-shutting-the-door-to-homeownership/.

If you have any questions about these comments, please contact Chi Chi Wu at cwu@nclc.org or 617-542-8010.

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