Banking and Finance Law Daily Wrap Up, TOP STORY—FHFA releases final rule on credit score models, (Aug. 14, 2019)

Banking and Finance Law Daily Wrap Up

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A Federal Housing Finance Agency final rule sets out a four-phase process for the Enterprises to validate and approve credit score models. A validated and approved credit score model must be used if the Enterprise conditions its purchase of mortgages on the provision of a credit score.

The Federal Housing Finance Agency announced that it is publishing a final rule on the validation and approval of third-party credit score models that can be used by Fannie Mae and Freddie Mac (the Enterprises). The rule implements the requirements in Section 310 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA) enacted on May 24, 2018, and generally adopts the validation and approval process set forth in the proposed rule (see *Banking and Finance Law Daily*, Dec. 14, 2018). It provides a four-phase process for an Enterprise to validate and approve credit score models. An Enterprise is not required to use third-party credit scores for any business purpose, but if an Enterprise conditions its purchase of mortgages on the provision of a credit score, section 310 requires that the score must be derived from a model that has been validated and approved in accordance with section 310 and the final rule. The rule will be effective 60 days after publication in the *Federal Register*.

Section 310 of EGRRCPA amended the Fannie Mae and Freddie Mac charter acts and the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 to establish requirements for the validation and approval of third-party credit score models by the Enterprises. It also set factors that must be considered, including the credit score model's integrity, reliability, and accuracy, its historical record of measuring and predicting borrower credit behaviors, and consistency of the credit score model with the safe and sound operation of the Enterprises. The final rule addresses each of those factors and defines a four-phase process for an Enterprise to validate and approve credit score models:

- solicitation of applications from credit score model developers: each Enterprise must publish a solicitation describing the requirements for credit score model developers to submit applications and the criteria under which it will evaluate the applications;
- submission and initial review of submitted applications;
- credit score assessment: the Enterprise will evaluate the credit score model for accuracy, reliability and integrity on a standalone basis, outside the Enterprise business systems and processes; and
- enterprise business assessment: the Enterprise will evaluate the potential impact of using the credit score model within the Enterprise's proprietary business systems and processes.

The final rule generally adopts the validation and approval process set forth in the proposed rule. However, it does not adopt the proposed conflict-of-interest certification requirement that would have required credit score model developers to demonstrate that there was no common ownership with a consumer data provider that has control over the data used to construct and test the credit score model.

The FHFA also published a fact sheet on the final rule, which focuses on the four phases of credit score model validation and the relevant time frames for each phase. The solicitation phase will take approximately 11 months. The credit score assessment phase must be completed within 180 days, with two possible FHFA-approved 30-day extensions. The enterprise business assessment phase must be completed within 240 days. The final rule does not address the timeframe for industry adoption and implementation of new credit score models. FHFA

anticipates that it will take the industry approximately 18-24 months to adopt a new credit score model after a model has been approved by an Enterprise.

Companies: Fannie Mae; Freddie Mac

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