# BRODY | GAPP LLP

*Clarity in Compliance.  Confidence in Litigation.*

## AI Governance Survival Guide for Mortgage Lenders

*Prepared by James W. Brody, Esq.  | Founding & Managing Partner*

*James@BrodyGapp.com | 415.246.3995*

## The mandate is enterprise-wide — and already in effect.

Freddie Mac Bulletin 2025-16 amended Guide Sections 1302.2 and 1302.8 effective March 3, 2026. This obligation is not triggered by application received dates or loan-level decisions. It is an enterprise-wide Seller/Servicer Agreement requirement applicable to every IMB, depository, credit union, mortgage broker, and fintech approved to sell or service Freddie Mac loans. The obligation applies to every AI or ML tool used anywhere in connection with Freddie Mac loan origination or servicing — including vendor-embedded tools.

## THE 5 THINGS YOU MUST UNDERSTAND

| | |
|---|---|
| **1.  The regulatory framework already applies.** | ECOA, the Fair Housing Act, UDAAP, SR 11-7, and Freddie Mac Bulletin 2025-16 all create current compliance obligations for AI in mortgage. No AI-specific legislation is needed — examiners are applying existing frameworks right now. The question is not whether you will face scrutiny. It is whether your governance will survive it. |
| **2.  Proxy risk is the silent threat.** | AI models can recreate redlining patterns using ZIP code, transaction patterns, or credit utilization in LMI areas — with zero discriminatory intent. The model does not know it is discriminating. Historical mortgage data reflects decades of inequity, and AI trained on it learns those patterns. You have to test for it before deployment — and continuously after. |
| **3.  Opacity is an adverse action violation.** | If your AI model cannot produce the specific principal reasons for a denial — reasons that reflect actual model logic — you are in violation of ECOA/Reg B, regardless of whether the model itself is fair. CFPB Circular 2022-03 was explicit on this point before its withdrawal in May 2025. The statutory obligation under ECOA § 701 and Reg B § 1002.9 remains fully operative. Black-box models require explainability infrastructure before deployment. |
| **4.  Your vendor's compliance is your liability.** | ECOA and the Fair Housing Act do not recognize 'my vendor said it was compliant' as a defense. SR 11-7 and CFPB examination procedures are both explicit: the institution is responsible for the fair lending performance of every tool it deploys, regardless of who built it. Your vendor's representations are a starting point — not a safe harbor. |

| 5. AI can improve fairness — but only if governed. | Consistent algorithmic application of credit criteria reduces human discretion bias. A well-governed AI model applies the same standards to every file. Well-governed AI can detect pricing disparities faster than any manual review process. The answer to AI fair lending risk is not avoidance — it is governance. |
|---|---|

## WHAT REGULATORS AND INVESTORS WILL ASK

1. How did you test this model for disparate impact BEFORE deployment — and what did the results show?

2. How are adverse action reasons generated, and do they reflect the actual logic of the model that made the decision?

3. What is your post-deployment monitoring process, at what frequency, and what thresholds trigger escalation?

4. How do you oversee your third-party AI vendors' fair lending compliance — and what contractual rights do you hold?

5. Who is accountable for model risk at the senior management level — and what documentation establishes that accountability?

## THE GOVERNANCE FRAMEWORK: FIVE PHASES

| PHASE 1 Pre-Deployment | Fair lending risk assessment for every AI use case · Proxy variable correlation testing · Synthetic protected class estimation (BISG) where HMDA data unavailable · Independent model validation before go-live · Model card documenting purpose, data sources, features, performance metrics, and fair lending test results |
|---|---|

| PHASE 2 Deployment Controls | Senior management approval in writing — required by Guide § 1302.8 · Audit trail for every AI-touched credit decision: model, version, inputs, output · Audit rights and model documentation requirements in every vendor contract · Change approval process for any model update or threshold adjustment |
|---|---|

| PHASE 3 Ongoing Monitoring | Monthly or quarterly disparate impact testing on approvals, pricing, and exceptions — disaggregated by race/ethnicity using HMDA data or BISG estimates · Drift detection on model performance metrics · Complaint trend review for AI-related patterns · Annual full revalidation at minimum — earlier if market conditions shift materially |
|---|---|

| PHASE 4 Human-in-the-Loop | AI flags — does not finalize — borderline credit decisions · Every human override documented: reason, who, outcome · Override patterns monitored for demographic disparities · If underwriters override AI denials at higher rates for one demographic group, which is a fair lending problem in the override — not the model |
|---|---|

| PHASE 5 Vendor Oversight | Model card required from every AI vendor before deployment · Contractual notification before any material model change · Right to re-validate before model changes take effect · Fair lending test results on file · Data sourcing disclosures: vintage, coverage, known exclusions |
|---|---|

## REGULATORY LANDSCAPE NOTE — MARCH 2026

CFPB Circular 2022-03 (adverse action / AI explainability) was formally withdrawn May 12, 2025, as part of a sweeping rescission of agency guidance documents. However, the underlying statutory obligations of ECOA § 701 and Reg B § 1002.9 remain fully operative and unchanged. The guidance withdrawal eliminates CFPB-specific interpretive support — it does not alter the legal requirements.

Fannie Mae has NOT issued an equivalent AI governance mandate. Dual-eligible Seller/Servicers face an asymmetric compliance posture: they must build Freddie Mac-compliant infrastructure without a corresponding Fannie Mae requirement. Brody Gapp recommends adopting Freddie Mac's framework as the enterprise baseline for all GSE loan activity.

State-level AI regulation: Colorado AI Act (effective June 30, 2026) covers consequential decisions in finance and housing. Texas TRAIGA (effective January 1, 2026) prohibits AI for unlawful discrimination. Illinois AI amendments to the Consumer Fraud Act (effective January 1, 2026) apply to employment and HR decisions — not directly to mortgage credit decisions.

### James W. Brody, Esq.

Founding & Managing Partner
BRODY | GAPP LLP

**415.246.3995 · James@BrodyGapp.com · www.BrodyGapp.com**

**Key Sources:** Freddie Mac Guide § 1302.8 · Freddie Mac Bulletin 2025-16 · SR 11-7 — Model Risk Management · HUD Fair Lending Resources · Interagency AVM Final Rule (Oct. 2025)