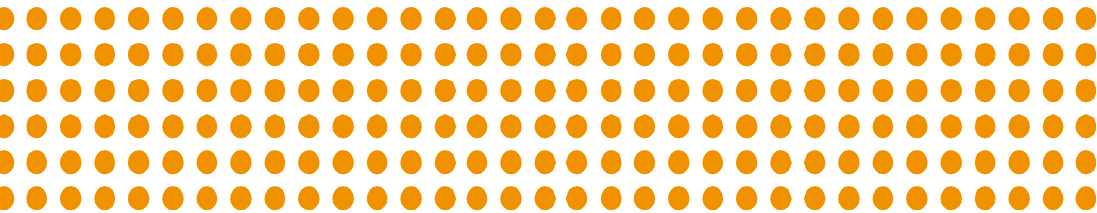# PRINCIPLES OF CREDIT SCORING

-A REGULATORY PERSPECTIVE

Nthupang Magolego, Executive Senior Legal Advisor, NCR

National Credit Regulator

OVERVIEW

- **INTRODUCTION**

- **CONCLUSION**

- **REGULTORY PERSPECTIVE:**
  - **CONSUMERS' LENS**
  - **REGULATION LENS**

- **CHALLENGES**

- **SUPPORT TECHNOLOGY OVERSIGHT AND THE EXPLAINABILITY OF CREDIT UNDERWRITING MODELS.**

- **CONCLUSION**

NCR
National Credit Regulator

Introduction

- ❑ Adequate disclosure of information is one of the fundamental principles underpinning consumer protection.

- ❑ One of the purposes of the NCA is to promote and advance the social and economic welfare of South Africans, promote a fair, **transparent**, competitive, credit market and industry,

- ❑ The NCA further states that consumers should be provided with adequate disclosure of information to enable them to make informed decisions and to protect their rights.

National Credit Regulator

NCR's view on credit scoring

❑ The NCR views issues of credit scoring from two perspectives:

❑ **Consumers' lens**

❑ **The regulation lens.**

National Credit Regulator

Consumers' lens

❑ The consumer's lens on credit scoring is informed by the types of complaints or enquiries that the NCR receives from consumers:

NCR
National Credit Regulator

Consumers' lens

❑ **1. How to improve their credit score?**

NCR
National Credit Regulator

2.   How are credit scores determined or calculated?

Consumers' lens

3. Why do they have poor credit scores when they have never taken credit before?

NCR
National Credit Regulator

Consumers' lens

☐ **4. Why did their credit scores reduce as a result of them applying for a loan, even though they did not end taking the loan applied for ? (enquiries)**

NCR
National Credit Regulator

Consumers' lens

❑ **5 Consumers believe their credit score is low/bad because of discrimination-racial discrimination being the main alleged discrimination.**

NCR
National Credit Regulator

Regulation lens

Credit scoring under the NCA:

❑ A **credit provider** may determine for itself any scoring or other evaluative mechanism or model to be used in managing, underwriting and pricing credit risk, provided that any such mechanism or model is not founded on any of the grounds of unfair discrimination prohibited in section 9(3) of the Constitution.

National Credit Regulator

Regulation lens

❑ **Information that may not be contained on the records of the credit bureau**:

➢ race

➢ political affiliation;

➢ medical status or history;

➢ religion or thought, belief or opinion;

➢ sexual orientation, except to the extent that such information is self-evident from the record of the consumer's marital status and list of family members; and

➢ membership of a trade union, except to the extent that such information is self-evident from the record of the consumer's employment information

Regulation lens

❑ **Information that may not be contained on the records of the credit bureau :**

❑ The consumer credit information may be used for purposes of credit scoring or credit assessment for a maximum period permitted.

❑ No source of information may submit information that has prescribed in terms of the Prescription Act.

NCR
National Credit Regulator

Challenges

❑ **Indirect discrimination-** models that appear to be non-discriminatory, but in practice have an unfair discriminatory outcome.

❑ **Intellectual property rights of credit bureaus and credit providers-** how to render credit scores transparent without infringing on the IP rights of credit bureaus or credit providers.

❑ **Algorithms/ AI's role in credit scoring-** The methods of credit scoring have become increasingly sophisticated over the years, with the incorporation of Artificial Intelligence, which can exacerbate the lack of transparency

❑ **Alternative data-** Alternative data, especially in comparison to traditional data, lacks transparency and will exacerbate the lack of transparency.

NCR
National Credit Regulator

Support Technology oversight and the explainability of credit underwriting models.

- ❑ While artificial intelligence/Machine Learning models & alternative data have potential to bridge data gaps & promote access to credit, they come with risks regarding transparency & fairness . Policymakers in SA need to understand the functioning of credit scoring models, especially the complex models that are based non-traditional data sources.

National Credit Regulator

Support Technology oversight and the explainability of credit underwriting models.

❑ The activities will include:

- assessing performance credit scoring models including credit data and file profiling, and score predictive accuracy, bias and interpretation

- assessing the use of machine learning and alternative data for credit underwriting including a review of existing consumer protection laws and regulations with respect to the use of data and complex analytics.

National Credit Regulator

Conclusion

❑ The explainability of credit scores is a consumer protection measure, and therefore it is important that in our work of ensuring data integrity, enhancing data governance, consideration on the use of alternative data etc, that we take consumers along in the journey, and render the work that we do transparent and explainable, so that as the main stakeholder, the consumer can have confidence and trust in the outcomes of the work.

NCR
National Credit Regulator

THANK YOU