

NR 97-46
May 20, 1997

OCC Alerts Banks to Potential Benefits and Risks
Of Credit Scoring Models

WASHINGTON, D.C. -- The Office of the Comptroller of the Currency (OCC) today notified its national banks and examiners to potential concerns with the use of credit scoring models by some national banks. The OCC said that although credit scoring models could help bankers make sound credit decisions, the agency has identified practices that could affect a bank's safety and soundness and its compliance with fair lending laws.

Credit scoring models are computer models used by lenders to evaluate potential borrowers and to underwrite all forms of retail credit, including credit cards, installment loans, residential mortgages, home equity loans and small business credit.

"Like all tools, credit scoring models can be used well or badly," said Comptroller of the Currency Eugene A. Ludwig. "Because they are so powerful, their potential for good -- or ill -- is magnified. That means they must be developed, implemented, tested, and maintained with extreme care."

In a bulletin sent to all OCC examiners and national banks, the OCC said credit scoring models can help bankers control risk, manage credit losses, help evaluate new loan programs, shorten processing time for loan applications, and improve bank profitability. When used appropriately, the OCC also said credit scoring models can ensure that a bank's existing credit criteria are sound and consistently applied and can improve bank compliance with fair lending laws.

To ensure that these models are used properly, the OCC said it was issuing today's bulletin to alert banks to potential concerns, including the application of credit scoring models to products and customers for which they were not designed and inconsistent use of credit scoring models, including excessive overrides, which can undermine the integrity of a credit scoring model.

To assure safety and soundness in the use of credit scoring models, the bulletin advises banks to carefully evaluate new models that they develop as well as those purchased from vendors. Banks must then validate their models periodically, including comparing actual performance with expected performance. The bank must also assure that its information systems are adequate to handle and test the models and produce useful reports for management decisions.

Focusing on fair lending issues, the OCC cited the potential for credit scoring models to include characteristics that may be discriminatory, have a disparate impact on a prohibited basis, or raise other Equal Credit Opportunity Act or Fair Housing Act concerns. The bulletin advises national banks to avoid illegal disparate treatment by ensuring that adequate controls exist

during the pre-scoring, scoring, and post-scoring stages of the credit application process.

Banks, the bulletin says, should establish clear guidelines for:

- Providing similar assistance to all credit applicants.
- Overriding a credit score, including who may do so and under what circumstances.
- Training, monitoring, and supervising bank employees who use credit scoring models.

A copy of the Credit Scoring Models Bulletin (OCC 97-24) May be obtained by writing to Comptroller of the Currency, Public Information Room (Mail Stop 1-5), Washington, DC 20219; faxing a request to (202) 874-4448; retrieving the document from the OCC's web page at <http://www.occ.treas.gov>; ordering by phone (202) 874-5043; or visiting the OCC's Public Information Room at 250 E Street, S.W. in Washington, D.C. (9 a.m. - noon and 1-3 p.m., Monday - Friday).

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Note to Editors:

The OCC is in the process of converting from faxing news releases to sending them via e-mail. To make this process go smoothly we are requesting those who want to continue receiving our news releases to send their e-mail address to Sharon.Stevens@OCC.treas.gov or by faxing it to (202) 874-5678.

The OCC charters, regulates and supervises approximately 2,800 national banks and 66 federal branches and agencies of foreign banks in the U.S., accounting for more than half the nation's banking assets. Its mission is to ensure a safe, sound and competitive national banking system that supports the citizens, communities and economy of the United States.