Sorry, No Credit

By Noel Capon

BOSTON — Appearing before the Federal Trade Commission in Washington, Bloomingdale's department-store chain agrees to pay $50,000 in civil penalties for alleged sex discrimination against women in its evaluation of credit applications; in San Francisco, a Federal judge denies Standard Oil of California's request for dismissal of a suit brought up a woman who alleges denial of credit on the basis of sex and marital-status discrimination; Montgomery Ward faces credit lawsuits in Delaware and North Carolina. Despite passage of the Equal Credit Opportunity Act in 1974 and its amendments in 1976, the National Consumer Finance Association was told recently that new investigative hearings on consumer credit might be in the offing. What's up?

What's up in consumer credit is point scoring, a computer-based method used by most major retailers, banks, and oil, travel and entertainment credit-card companies to assess consumers' credit-worthiness. Point-scoring systems attempt to discriminate statistically between good and poor credit risks by assigning points to personal situations.

For example, a home phone may be worth 10 points, no phone 2 points; living in one part of town 25 points, in another, 8; owning (or purchasing) a home 20 points, renting 8. Other frequently rated variables are age of automobile, time at employment, time at address, occupation, and maintenance of checking and savings accounts.

An applicant supplies the required personal data on a credit application form. A total point score above the target either earns credit automatically or the applicant's credit history is factored into the decision. A score less than the target results in automatic denial of credit, regardless of credit performance, which is never checked.

Creditors' rush to introduce point scoring resulted from cost-reduction benefits and from passage of the Equal Credit Opportunity Act, which proscribed discrimination on certain illegal bases and prescribed use of supposedly demonstrably and statistically sound, empirically derived point-scoring systems.

The Congress liked these systems because they were objective; they replaced credit managers' judgment with sets of statistical relationships. However, the benefits accorded by objectivity may well be overshadowed by costs not foreseen when the law was enacted.

First, certain uses of point scoring may be illegal. The personal data used, though apparently neutral, may be intimately and highly related to personal characteristics that are illegal to look into under the law. Zip code and owning or renting information may involve racial discrimination; owning and renting information may involve marital-status discrimination; time at employment may discriminate against women. The systems are also biased, since, contrary to the law, creditors use neither random samples of applicants, nor acceptable alternatives, to develop systems.

In addition, the systems do not meet the law's criterion of objectivity.

The occupation groups are crude, judgmentally formed aggregates of individual occupations: For instance "production worker" may include lathe operator, dressmaker and TV repairman. Some creditors "doctor" objectively developed systems to make the point assignments more palatable to credit managers. They also override their systems by awarding credit to rejected applicants who complain, thus discriminating against those who meekly accept credit denial.

For systems that do meet objectivity requirements, problems are equally severe. For instance, the point assignments for time at address and time at employment are often illogical. In a "typical" system, the points awarded for time at address are, less than one year, 5 points; one to two years, 0 points; two to three years, 5 points; three to five years, 0 points; five to nine years, 5 points; 10 years or over, 20 points!

Creditors argue that point scoring can be valid only if all criteria that relate statistically to payment performance are used. One major retailer has already demonstrated that persons whose last names begin with "B" and "K" are good risks. On that basis, hair color and left- and right-handedness could be used.

Most of the personal characteristics used make no sense, but advocates of point scoring are unconcerned about such niceties. Statistical prediction, they believe, is the sole criterion for choice of a system. Although within their own organizations they allocate jobs and budgets on the basis of work performance, they see no contradiction in removing knowledge of an applicant's credit performance from the credit decision. They are thus prepared to reject applicants who may have excellent payment records.

Point-scoring systems may destroy themselves when credit applicants, learning that information on forms is often never checked, decide to supply data that will earn credit, even if untrue. Before that happens, perhaps Congress will hold hearings to learn the real impact of point scoring.

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