

The financial sector's uphill battle to escape the AI Act

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Banks have been seeking to exclude logistic regression, widely used for credit scoring in the financial sector, from the definition of AI in an attempt to escape the AI Act's strict requirements for high-risk systems. However, the European Commission told representatives for EU countries at a recent meeting that it considers these techniques artificial intelligence.

Banks have been battling to exclude statistical regression techniques widely used in the financial services industry from the AI Act since negotiations over the law began.

However, the European Commission considers them to be included, MLex has learned.

The question comes down to the very definition of artificial intelligence. If these techniques are included, AI systems used for credit scoring would be covered under the regulation's tight regime for high-risk applications.

The definition of an artificial intelligence system was contentious during the legislative process. But now that the AI Act is law, the European Commission's AI Office will issue guidelines on how the definition should be interpreted by February 2025.

The European AI Board, which gathers representatives of EU countries, held an ad-hoc meeting on Dec. 3 to discuss the upcoming guidelines. The question of logistic regression used in the banking sector was raised, and the commission reiterated that it considers these techniques to be AI.

Another point raised concerns the extent to which statistical-based systems should be considered artificial intelligence. That is indeed relevant since logistic regression is a statistical technique.

In this regard, the commission said it will publish information concerning what statistical-based systems should be considered AI, presumably as part of the upcoming guidelines.

— The banking sector's argument —

"We recommend that the guidelines explicitly exclude logistic regression from the act's scope, particularly when used in isolation," reads a technical note from leading banking services associations, seen by MLex, that was widely distributed to EU policymakers.

While banking trade groups have been particularly active in this area, logistic regression for credit scoring seems to be a widespread practice in the financial sector at large.

For the signatories, logistic regression is a "simple mathematical function" that lenders use to estimate the likelihood that someone will repay a loan by building scorecards that are then used to calculate a credit score.

The banking sector notes that while the commission's early draft of the AI Act included statistical approaches, the law's final version does not. In their view, this signals the EU institutions' deliberate decision to exclude them from the scope.

During the legislative process, EU lawmakers completely changed the definition of an AI system to align it with the one of the OECD, and the OECD's explanatory memorandum does not include logistic regression.

Representatives from banking institutions point out that logistic regression lacks a key capability of an AI system, namely the capacity to infer beyond basic data processing since the technique infers probabilities in a relatively simple way, and it cannot learn from new data without manual updates nor produce autonomous outputs.

— An uphill battle —

The EU's executive arm opened a public consultation last month to gather stakeholders' feedback on the AI definition guidelines and how to distinguish AI from simpler traditional software features prominently in the questionnaire (see [here](#)).

Prior to the consultation's publication, two leading EU lawmakers had also raised this point via parliamentary questions, asking the commission how it intended to distinguish AI from traditional software and to define "basic data processing" (see [here](#)).

The commission's latest statement at the AI Board's closed-door meeting shattered the banking sector's hopes that logistic regression might be excluded from the scope via the upcoming guidelines.

The regulator, however, is not the only one that considers logistic regression a necessary part of the AI definition; some independent experts also side with their position.

"Logistic regression is at the heart of supervised machine learning. Removing logistic regression would basically remove most of machine learning," Kris Shrishak, a senior fellow at the Irish Council for Civil Liberties, told MLex.

Shrishak argues that the law's definition of an AI system is fully compatible with logistic regression. For instance, the regulation states that an AI system "may exhibit adaptiveness," which means that AI systems can also not exhibit adaptiveness.

Another example he emphasized is the fact that the definition considers artificial intelligence as those systems that have "varying levels of autonomy," which means limited autonomy is within the scope.

— Implications —

If the commission confirms its position in the upcoming guidelines, banks and the whole financial sector will soon be subject to the AI Act's due diligence requirements.

The guidelines are administrative documents, so the battle over interpreting the law would likely play out in the courts.

While waiting for lengthy legal proceedings, the financial sector would have to comply with the AI Act, which clearly indicates that AI systems "used to evaluate the creditworthiness of natural persons or establish their credit score" are high risk.

In terms of compliance, financial institutions normally already have a quality management system since that is required under sectorial legislation; they would need to adjust it to the AI Act's requirements.

The most burdensome compliance measure they would have to apply would be integrating the risk management system the AI law mandates with their legacy software.

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