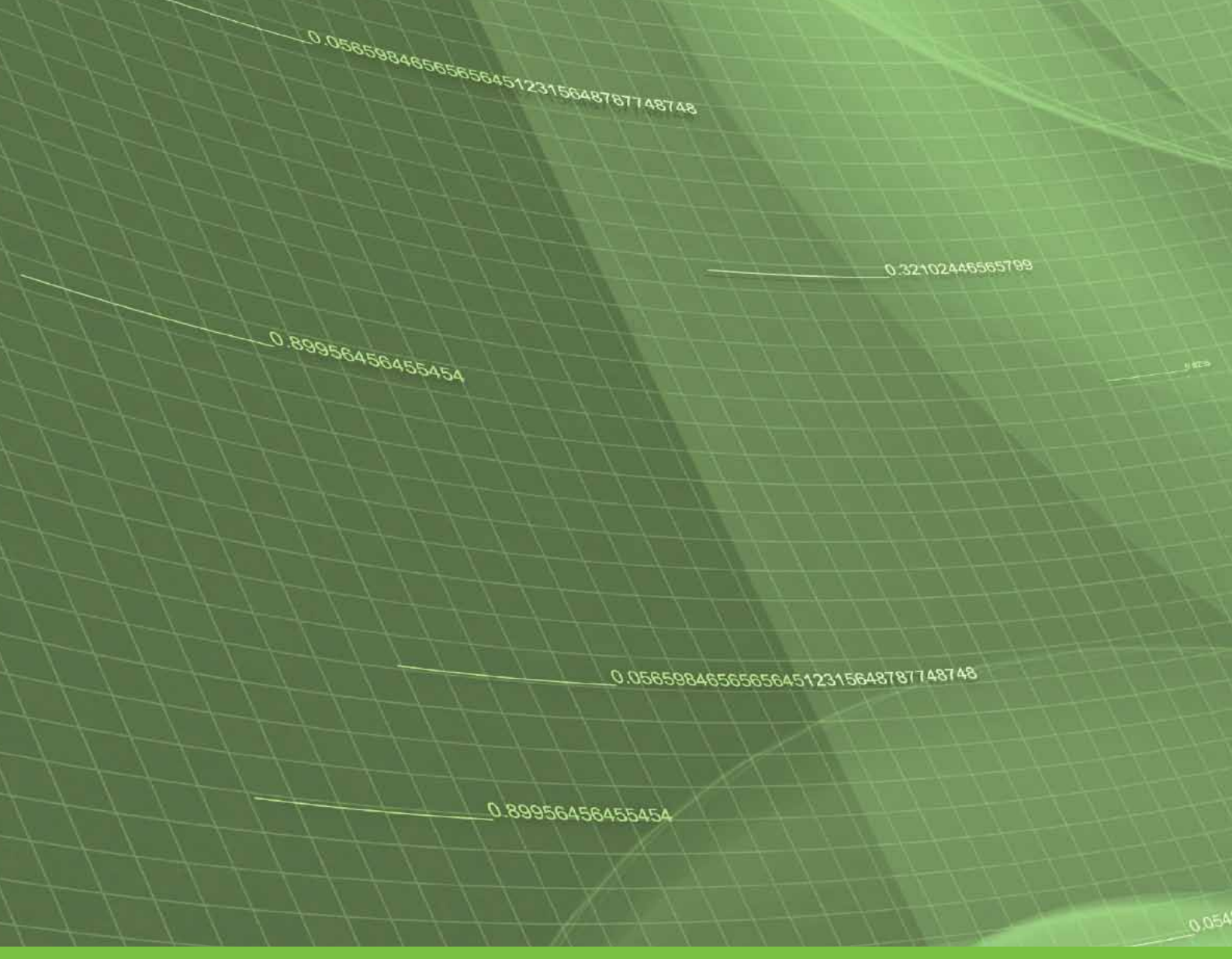


Public credit registries, credit bureaus, and the microfinance sector in Latin America

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Prologue

Credit bureaus and public credit registries in Latin America and the Caribbean

More than three decades have passed since the initial experiences of microfinance in countries such as Bolivia and Bangladesh demonstrated that offering financial services to low-income populations would be viable. Over time and throughout a rich experimentation period, it is evident that microfinance institutions are sustainable, and today have reached economies of scale, profitability, and a level of sophistication which would have been unimaginable in the beginning.

As time has passed, microfinance has integrated itself into the financial systems of our countries in a notable way. This has allowed millions of families to access quality financial services for the first time. And while microfinance institutions still see themselves as fundamentally micro-credit providers, many institutions have broadened their product line to include savings, remittances, and insurance, among others. Microfinance is, without a doubt, a powerful tool for financial inclusion.

The introduction of millions of new clients into the financial system has its own challenges. One important challenge is the need for large data bases, which include the availability of credit information on each and every client in the financial system. This would help promote healthy growth in the sector. This type of information, which is generally provided by credit bureaus and public credit registries, is vital in preventing over indebtedness of clients, as it allows for a complete profile of the client.

Conscious of the risks and adhering to their original mandate to support clients in the long and arduous journey to greater success, the microfinance industry has reacted positively. Today more than ever there is a genuine interest in the industry to ensure that the products and services offered, as well as the conditions to obtain the services, are actually contributing to the wellbeing of its clients.

Many programs to measure the effectiveness of microfinance, including socio-economic impact indicators, have been introduced. Great efforts are being made to improve and implement the use of these indicators in order to make better decisions. Credit bureaus and public credit registries are vital in measuring effectively the true level of indebtedness of clients, which helps reduce the possibility of over indebtedness, which ultimately affects not only clients, but also microfinance institutions and their fund providers. This makes credit bureaus and public credit registries critical in the reduction of the risk of over indebtedness.

The objective of this study, written by MicroRate, is to identify the best practices of credit bureaus and public credit registries in Latin America in order to pinpoint opportunities for improvement, with the goal to create a suitable environment for their operations with a special emphasis on the characteristics of microfinance.

To this end, and especially in the effort to reduce the risk of over indebtedness as a possible consequence of the growth of microfinance, we offer this study, which we trust will contribute to the strengthening of credit bureaus and public credit registries, with the ultimate goal of ensuring greater transparency in the microfinance sector and financial system as a whole.

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Objectives, scope, and limitations



The objective of this study is to identify the main problems faced by the Latin American microfinance sector in reporting and using credit bureaus as a tool to reduce the risk of over indebtedness. Furthermore, the study seeks to identify best practices that have been implemented in various countries to mitigate or avoid these difficulties.

This study is funded by the Multilateral Investment Fund (MIF), the Development Bank of Latin America (CAF), and Calmeadow, and is executed by MicroRate Inc. (www.Microrate.com).

A sample of ten countries was selected for the study: Bolivia, Brazil, Colombia, Ecuador, El Salvador, Guatemala, Mexico, Nicaragua, Peru, and the Dominican Republic. The criteria for the selection of these countries was the representativeness of countries from North, Central, and South America, as well as the maturity of the microfinance sectors (both mature and immature markets).

From May 14 to July 27, 2012, key microfinance players who accepted the invitation to participate in the study were required to fill out a questionnaire framed by the General Principles for Credit Reporting¹, published by the World Bank in September 2011. This document is considered a global guide on the minimal requirements that a credit reporting system must meet. After the survey, some of the participants were interviewed to expand on key points.

Of the five general principles, only four were used in this study: 1) Data; 2) Data Processing: Security and Efficiency; 3) Governance and Risk Management; and 4) Legal and Regulatory Framework. The last principle, Cross-Border Data Flows, was not considered given that the microfinance sector does not typically share clients between different countries.

An analysis of each country regarding their alignment to the General Credit Reporting Principles helped to identify the difficulties faced by each country. This analysis is presented as an appendix of this report.

Ecuador is not included in the appendix because, during the release of this report, significant changes were expected in the regulatory framework of credit bureaus. These changes would fundamentally change the environment evaluated by MicroRate in May 2012.

Based on the challenges found in each county, MicroRate identified the principal and most common problems affecting the analyzed countries. Further, the best practices that have been applied in other countries to reduce or avoid these problems are also included.

¹ General Principles for Credit Reporting" (http://siteresources.worldbank.org/FINANCIALSECTOR/Resources/Credit_Reporting_text.pdf)

This report is not intended to be an in depth statistical or legal study. Rather, the report seeks to draw conclusions about the perception of the challenges expressed by the participants in each country. The study is framed by MicroRate's experience rating microfinance institutions and broad knowledge of the microfinance context of the countries included in this report.

It must be noted that in the analyzed countries there are no official figures on credit providers to the low-income sector of the population (including MFIs, cooperatives, pawnshops, etc.), which made it difficult to estimate how many do not report to the credit bureaus.

It was also difficult to get figures from credit registries and credit bureaus regarding the number and type of reporting institutions from the microfinance sector. For some this was due to internal confidentiality policies, while others did not have detailed records of the types of institutions that report.

In the analyzed countries there are different names for the credit report service providers. For this report, MicroRate focused on those most commonly used in order to facilitate understanding. Thus, "Public Credit Registry," refers to the service provider of credit reports that collects information from the regulated financial system. Normally, public credit registries are managed by a supervisory body that provides credit information to regulated reporting financial institutions and uses this information for supervisory purposes. "Credit Bureaus" refer to credit report service providers, usually private, that, in addition to the credit information for the regulated financial system, collect credit information from the non-regulated financial sector, non-financial sector, judicial system, tax system, etc. (*See the exact definition in the Glossary*).

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Executive summary



The microfinance sector in Latin America has advanced by using public credit registries and credit bureaus (*See definition in the previous section*) as important tools in reducing credit risk. However, significant challenges remain, mainly in markets where the sector had not yet matured.

Approximately 30 years ago, the financial sector was composed of mainly regulated banks with lending that was usually delayed several months. When public credit registries were first created, they concentrated on banking information, with information primarily on payment appropriations, generally monthly, or revolving lines of credit.

After the emergence of microfinance institutions, the characteristics of the financial sector changed (daily, weekly, bi-weekly payments, as well as credit approvals as quick as in 24 hours). Consequently, the informational needs of public credit registries also changed.

Microfinance institutions (MFIs) did not have access to public credit registries because they were not within the scope of the supervisory body. Some regulatory bodies covered this need by regulating MFIs, as occurred in Peru.

In other countries, when faced with increasing competition, generally after a crisis, the non-regulated microfinance sector began to pressure the authorities to share information with the regulated sector.

Since approximately the year 2000, private credit bureaus began to be approved in various countries in order to serve both the regulated and non-regulated sectors. The MFI networks have played an important role in this process, with some even creating their own credit bureaus. This was done with the goal of filling the void left by some public credit registries and/or credit bureaus that served only the banking sector. The credit bureaus specialized in the microfinance sector have championed the inclusion of industry-specific data, such as quota amount, payment frequency, exact days in arrears, maximum days in arrears, individual and group debt, etc.

With the exception of Brazil (which started credit bureaus in the 1950s) and a few credit bureaus that have international partners, experience with credit bureaus in the analyzed countries is limited. In recent years, credit bureaus have been adapting their databases to the microfinance sector and continue learning about its needs.

In this context, efforts have been made to include non-regulated MFIs (generally affiliated with MFI networks) in the credit bureaus. With the exception of Mexico and Guatemala, where many microfinance credit providers are not included, the largest MFIs have been reporting information to credit bureaus.

In some countries, numerous credit providers for the low-income sectors of the population are not yet included, but for the most part they are very small. It is unknown which ones or how many they are due to the lack of official records. Their different legal statuses (cooperatives, pawnshops, commercial associations, NGOs) make the task of identifying them more difficult.

Currently, the challenges surrounding credit bureaus are great. Besides the struggle to include a larger number of credit providers as reporting institutions, the biggest problem is access to data. Given the different characteristics involved in microcredit, such as weekly and bi-weekly payments (uncommon for banks) and excess supply that allows for quick access to loans, it is necessary to update data more frequently.

To achieve this, more technology is needed, as demonstrated by Brazil, where processing large amounts of information daily has only been possible because of better technology. In most of the countries studied, weak information systems are prevalent. Even the bigger banks use different databases and are delayed in their consolidation. Public credit registries are also outdated, both in technology and in the adequacy of the data adapted to MFIs. Credit bureaus, largely technologically strong, still lack the capacity to process information online as Brazil does. They usually process information monthly, leaving an informational void between 40 and 60 days, generating high risk for the microfinance sector. Providing technological resources to the financial system that would help process information adequately on a daily basis would be a modest investment compared with the positive impact that it would have on the healthy development of microfinance.

Another major challenge is the dissemination of information between the different credit bureaus. Only in the Dominican Republic do reporting institutions voluntarily share information with the two existing bureaus. Although some of the microfinance reporting institutions in this country do not yet follow this practice, credit bureaus generally have similar information and compete on services and prices, benefitting all users.

In contrast, in the other countries studied, the credit bureaus compete for reporting institutions, which leads to the dispersion of information and pushes institutions to consult at least two bureaus in order to analyze the debtor's situation in the financial and non-financial sectors. In addition to increasing operating costs, this affects the scores' data integrity and that of other specialized products offered by the credit bureaus.

Although there is an obligation to report to public credit registries, there is no obligation to report to credit bureaus. It is part of the government's task to create the necessary mechanisms so that reporting institutions provide information to all credit bureaus. This would incentivize healthy competition, which would benefit the sector with higher information quality.

There is also a significant gap with regards to the number and type of reporting institutions from the non-financial and public sector with relevant information. With the exceptions of Brazil and the Dominican Republic, there is only moderate participation from these sectors, which does not allow for a comprehensive analysis of the borrower's credit standing.

Another issue of concern is data accuracy, which is linked to the MFIs' low technological and organizational capacity. In countries where the microfinance sector is immature, most unregulated MFIs have trouble reporting reliable information. This results in errors that lead to loss of trust in the country's credit reporting system, but of primary concern is the loss of control of the debtors' credit history. Furthermore, there is the added deficiency of some governments to reliably manage a national citizen identity system.

Additionally, MFI share ownership in credit bureaus has caused fear of unfair competition in the sector. Despite the lack of concrete evidence to justify this fear, its presence suggests the need to mitigate the risk.

There is a need for more training in the importance and use of credit bureaus in countries with an immature microfinance sector, such as Mexico and Guatemala. Because competition and crises have not yet pressured the sector, some MFIs feel comfortable with the high profitability generated and even continue to doubt the importance of the credit bureaus as a tool to reduce credit risk.

Institutional strengthening in corporate governance and risk management would help fill the organizational vacuum that exists in some unregulated MFIs. This would allow for greater data accuracy and trust in the credit reporting system.

In some countries, the participation of the authorities is necessary to remove legal barriers, such as advanced notification to the debtor (Colombia and Brazil), the unregulated sector's lack of access to the regulated sector's data (El Salvador), and the bureaus' lack of access to all credit products of the regulated financial system (Bolivia).

Finally, there is a need for the effective enforcement of consumer protection regulation in various countries. For this, the necessary resources must be provided to allow for the effective functioning of bodies dedicated to monitoring compliance of consumer protection norms.

3

Main challenges facing the microfinance sector regarding public credit registries and credit bureaus (in order of importance), and best practices to mitigate these challenges



By analyzing the alignment of each country with the General Principles of Credit Reporting published by the World Bank in September 2011, the specific problems of the countries analyzed were identified.

Appendix No.1 includes each country report, which assesses to what point the country's credit reporting system is approaching minimum standards for maintaining a strong system. Each principle and guideline is analyzed (*See Annex 3*), ending with Conclusions and Recommendations for each country.

The comparison of each country's alignment with the World Bank's General Principles (*See Annex 2*) helped to identify the main problems facing the Latin American microfinance sector. Following is a list, in order of importance, based on the impact that each issue has on the credit analysis system and on the risk control of the debtor's over-indebtedness.

After each challenge there are best practices that have been applied in the surveyed countries to help mitigate or avoid the challenge.

3.1 Lack of Available Data

Lack of available data is the biggest problem identified in the analyzed countries. This is due to the speed with which loans are granted in the microfinance sector, which does not correspond to the frequency of data updating in the credit registries and credit bureaus.

Brazil (Appendix 1-ii) is the only country that stands out for updating its data daily. Other countries, such as Mexico and Colombia, partially update weekly or bi-weekly, depending on loan payment frequency.

In the remaining countries, data in the credit bureaus is outdated as it is usually updated monthly. This leads to a lack of information for periods between 40 and 60 days, which is risky for the microfinance sector.

The following practices help improve the timeliness of data:

Strong computer systems and internet service: Generally, MFIs with robust computer systems and unique client databases report data more quickly. In contrast, MFIs with numerous databases delay in consolidating and validating information and sending it to the credit bureaus.

Also, in countries with good internet, MFIs have online systems. This allows for faster consolidation of data than for other MFIs that have agencies in rural areas where there is no internet. In cases where agencies lack internet access, they send a hardcopy of the database to headquarters to be consolidated.

The technological strength of credit bureaus in Brazil is a good example of what reporting institutions have achieved with daily online data updates.

Direct transfer of data to credit bureaus: The regulation of some countries, such as Colombia, the Dominican Republic and El Salvador, allows regulated entities to send data directly to credit bureaus. This enables greater frequency of data updates.

This benefit has been seen in Brazil, where data is updated online daily, making Brazil the leader in data availability and allowing for a more precise credit analysis.

In other countries, such as Peru and Bolivia, the bureaus are bound to be less timely because they depend on the public credit registries' database, which is shared monthly.

Data reports based on payment frequency: Mexico is making efforts to improve the timeliness of data.

One of these efforts is the updating of credit data based on the frequency of payment. For example, weekly loan payments are reported weekly and bi-weekly payments are reported bi-weekly. This initiative of the Mexican credit bureaus is commendable given that is not a legally required.

The Mexican credit bureaus' initiative reduces the information gap created by monthly data reporting and also benefits the Mexican microfinance sector given that many MFIs have weekly and bi-weekly loan payments.

Another noteworthy case is Banco Ademi in the Dominican Republic, where despite monthly loan payments, it voluntarily reports to credit bureaus on a bi-weekly basis.

Publication of negative information without previously notifying the debtor: Most of the analyzed countries (except Brazil and Colombia) do not notify debtors before reporting arrears to the credit bureaus, expediting the reporting process.

Although such notices promote information accuracy, (See section 3.3), Colombia could improve the timeliness of data if reporting institutions were not obligated to notify the debtor of the release of their arrears to the credit bureaus. Colombia requires a notice of 20 calendar days prior to the release of information. Besides delaying the process, the notices incur additional shipping costs for the MFI.

In Brazil, the debtor must be notified ten days prior to the release of information. However, because data is updated daily, the misinformation window is shorter than if updated monthly.

Discontinuation of service due to late delivery of data. After Brazil, Mexico is the country which most frequently updates data in the credit bureaus.

In Mexico, credit bureaus have the legal authority to discontinue service to institutions that do not provide accurate information in a timely manner. The inability to consult the credit bureau and attend clients obligates the MFIs to comply with the time limits agreed upon with the credit bureaus.

“Request Footprint” Registry: Given that various countries have technical, legal, and regulatory limitations to acquire timely data, they have been able to mitigate this deficiency by registering the number of attempts made by the debtor to seek loans from other institutions (also known as a “request footprint”).

Sometimes credit bureaus send this data daily to MFIs as an alert service. The MFIs immediately send the information to their respective credit officers as an alert of further indebtedness. In other cases, credit officers only discover the “request footprint” upon obtaining the credit report when evaluating the request for an additional loan.

Despite being a mitigating factor for the lack of timeliness of data, request footprints only provide partial information. With the exception of the Dominican Republic, in all of the analyzed countries data is scattered amongst various credit bureaus. As a result, some bureaus have data corresponding to some institutions, while other bureaus contain information pertaining to others. Consequently, if the MFI consults the “request footprint” in only one credit bureau, they will not see the debtor’s entire credit history.

3.2 Lack of reporting institutions and the dissemination of data in credit bureaus

While the inclusion of non-regulated MFIs in mature microfinance markets is important, the inclusion of small MFIs and other credit providers such as pawnshops, cooperatives, appliance stores, etc., remains a challenge.

Though some loan providers do not provide microcredit (i.e. - they do not specialize in production loans), their loans target the same niche as the microfinance institutions, thereby affecting the customer’s ability to pay.

In markets where the microfinance sector is still immature, like Guatemala and Mexico, most non-regulated MFIs do not report to credit bureaus. The reasons are numerous, for example, organizational weaknesses, inadequate technology, unawareness of the importance of credit bureaus, fear of losing customers, and high operational costs, among others.

In other countries there is moderate participation from the non-financial and public sectors. Brazil and the Dominican Republic are the two countries (out of 10 analyzed countries) where we observed that most credit providers report to credit bureaus. This is achieved through years of experience and the transparent work of private initiatives.

In most countries, credit bureaus are competing based on number of reporting institutions rather than by service quality and prices. This occurs because reporting institutions only send information to credit bureaus where they have contracted services to consult the bureaus’ information. This results in high data dissemination among multiple credit bureaus, causing institutions to have to consult at least two bureaus in order to obtain the debtors’ credit history.

Moreover, data dissemination affects the quality of special services such as scores and data analysis because the credit bureaus may not have all of the debtors’ credit information. Market risk analysis is also affected, as the information of all loan providers is not available. Further, the institutions lose motivation to report data because it is considered insufficient, untimely, and costly.

The factors that have resulted in higher institutional participation in credit bureaus and less dissemination of information are:

Public credit registries sharing information with credit bureaus: In various countries there are public credit registries. However, Peru is the only country where the public credit registry shares its database with credit bureaus, allowing for standardized information of the entire regulated financial sector.

In Colombia and Mexico, there are no public credit registries, which limits the possibility of a single database for the regulated financial system. The information from regulated institutions is disseminated amongst the various credit bureaus, preventing the authorities' regulation and supervision of the financial sector.

Since Peru provides the database to all regulated financial institutions, it is the only country where regulated institutions can themselves perform an assessment of the debtor's rating² (i.e. the debtor's rating based on the entire financial system).

This practice reduces systematic risk and institutional costs. Regulated institutions in the other countries in this study can only make individual consultations of debtors via the supervisory body's webpage, therefore they cannot perform this assessment at the database level.

Requirement to consult at least one credit bureau: Regulated MFIs in Bolivia are required to consult a microcredit and consumer loan credit bureau in addition to one public credit registry. This requirement forces increased reporting of financial institutions to the credit bureaus which they will consult.

Active MFI network participation with credit bureaus: The leadership of MFI networks in encouraging their members to participate in credit bureaus has been fundamental in several countries, such as Peru and Bolivia.

In addition to providing training and support, for a few months networks offered free service and awarded technical help such as simple electronic archives to facilitate the reporting of data. This resulted in high participation of non-regulated MFIs.

Another mechanism, used in Colombia, has been the signing of a code of ethics, which promotes reporting to at least one credit bureau. For the ProDesarrollo network in Mexico, the use of credit bureaus is "mandatory" for its affiliates.

Some credit bureaus in Bolivia, Peru, and the Dominican Republic have performed fieldwork throughout various cities, identifying MFIs, often times those not affiliated with a network, and convincing them of the importance of reporting. Such efforts have proven successful.

It was observed that MFI networks have achieved higher participation after a crisis. This was the case in both Bolivia and Nicaragua, where groups of debtors agreed not to pay their debts. Since that time, in both countries there is no doubt of the great benefit of reporting and using credit bureau data.

Requirement to report to credit bureaus as a condition for funding: In Mexico, development banks and some international funders have required that, in order to receive funding, MFIs must report to at least one credit bureau. This practice has encouraged greater participation from non-regulated MFIs.

Information technology systems owned by MFIs: MFIs with their own information systems can respond more easily to public credit registries' and credit bureaus' requirements.

Small MFIs sometimes have external information systems suppliers, which implies higher costs to modify the database. Moreover, these institutions do not have their own trained staff capable of making the changes required by credit bureaus, inhibiting their participation in the credit system.

² In the Dominican Republic, the supervisory body performs these debtor assessments internally, but they do not share their database with regulated institutions.

Respect of bank privacy and consumer protection: Brazil is one of the countries that has achieved widespread participation from the regulated and non-regulated financial systems, as well as the non-financial sector, due to the trust that exists in the credit reporting system.

Regulation has helped avoid mechanisms that promote unfair competition. Thus, it was possible to adopt and strictly enforce a lending and borrowing regulatory framework, as well as consumer protection standards.

In contrast, in Guatemala there is no regulatory framework for credit bureaus and consumer protection. Instead, there is fear of unfair competition and credit bureau misuse of data. This has led to limited reporting by financial institutions and, as a result, to insufficient information in credit bureaus.

Voluntary data reporting to all credit bureaus: In the Dominican Republic, many reporting institutions submit data voluntarily to the two existing credit bureaus.

This allows credit bureaus to compete based on price and quality of service. Furthermore, the adequacy of data and the large number of reporting institutions favors data integrity and therefore better score results and other specialized data studies.

For reporting institutions, credit bureaus become an effective collections tool; customers will be rejected at any institution since their arrears information will appear in all credit bureaus.

It should be noted that some MFIs in the Dominican Republic do not report to both credit bureaus for fear of losing customers.

3.3 Lack of data accuracy

In the analyzed countries there is data accuracy in mature markets, but not in immature markets, due to the lack of MFI regulation, which leads to inadequate data security measures.

In contrast, there were acceptable data security measures in regulated MFIs and credit bureaus.

The factors that help improve data accuracy are:

Simple formats: Credit bureaus and MFI networks supported the provision of simple formats for MFIs to fill out, facilitating the accuracy and timeliness of data. There were cases where, at first, incomplete data was accepted; however, these MFIs were supported in their gradual progress until they reached the desired data level.

The partnership between credit bureaus and microfinance networks has been vital in this process. For example, in Peru there was an agreement between Copeme³ and Equifax⁴, where the MFI was motivated, trained, and aided in reporting and using credit bureaus.

Price discounts for providing high-quality and timely data: A good incentive for MFIs is to receive discounts on credit bureau services for reporting quality data in a timely manner.

Mexico is a good example where MFIs can receive up to 30% off the regular price of services for meeting these requirements. Further, credit bureaus in Mexico have the legal power to discontinue service or to not accept reporting institutions with low-quality data, thereby protecting the accuracy of their information. This practice also favors the efficiency of service (See section 3.8 Good service, though with relatively high costs).

³ The Consortium of Private Organizations to Promote the Development of Small and Microenterprises.

⁴ Credit Bureau headquartered in the United States and with offices in Peru, Ecuador, Brazil, the Dominican Republic, El Salvador, Honduras, and Costa Rica.

Tight data security measure: Generally, regulated MFIs have information technology systems with tight security and supervisory measures that enable data accuracy.

In addition to on-site visits by the supervisor, there are system, internal, and external audits. In Peru, there is an additional requirement whereby an Official is required to oversee data security.

Generally, the supervisory entity establishes strict standards of risk management. Specialized risk units, depending on the Board, are mandatory and are responsible for coordinating the business' risk management.

Bolivia is a good example of how non-regulated MFIs decided to self-regulate. These institutions followed the risk management rules of the regulated system. Currently, some count on strong Risk Units that play an important role in reducing business risk.

In some of the surveyed countries, the regulation of credit bureaus is done by the supervisory entities, thereby establishing data security standards.

Of the analyzed countries, the supervisory bodies of Bolivia and Peru have regulated that data must first be sent to public credit registries in order to validate data and for quality control purposes. Then the data is sent by the supervisory body to credit bureaus. On the other hand, there are various countries where MFIs report directly to credit bureaus and accuracy has not been harmed.

This is explained by the fact that credit bureaus are aware that data is their most valuable asset and generally are very careful in maintaining a strong data validation system. Effectively, though in some of the analyzed countries credit bureaus are not supervised, they usually have strict data protection measures.

In contrast, in the case of Guatemala, credit bureaus are not supervised and there is strong user distrust of the data protection measures that some credit bureaus apply.

Contracts requiring minimum data quality measures: Credit bureaus reduce the risk of MFI data inaccuracy by requiring minimum data quality standards in their contracts. These contracts establish consequences such as discontinuing service to repeat offenders.

Unique national identification records: In most countries there is a unique national ID for each citizen. This allows for a unique credit history for each debtor, improving the accuracy of data in the country.

As of May 2012 in Bolivia, there were estimates by the credit bureau Infocred that as many as approximately 15% of IDs were duplicate, making it difficult to maintain accurate data. The absence⁵ of a unique national ID registry in Mexico is one of the main causes of inaccuracy.

Clear identification of home addresses: In many countries there are public registries of addresses and properties that clearly detail the client's home address, a key detail in identifying the consumer.

In Mexico, however, the lack of precise addresses in some rural and urban areas leads to data inaccuracy. For example, sometimes an address may be listed as a "known address", which could be identified as an "inconsistency" by the credit bureaus and lead to questioning of the MFI's data quality.

Penalties for errors: In several countries, such as Brazil and Peru, the regulatory framework is strict, imposing heavy fines on MFIs or credit bureaus for credit report errors.

⁵ Although there is a "population code registry," it is not reliable as a national ID.

In general, institutions in those countries put more care in data accuracy for fear of the heavy payments they would have to make in case of an error.

3.4 Regulatory frameworks that discriminate against MFIs

In general, among the analyzed countries there is no legal discrimination in order to access data. However, in Bolivia and El Salvador, non-regulated MFIs are legally discriminated against in accessing data from the regulated financial system (See below).

Best practices observed:

Non-discriminatory standards: In 8 of the 10 analyzed countries, all users legally have the same rights and requirements in the credit bureaus.

However, in El Salvador there is legal discrimination as non-regulated MFIs do not have access to information from the regulated financial system, according to the Banking Law. This occurs despite the fact that credit bureaus attain information from the regulated reporting institutions.

Another case of legal discrimination occurs in Bolivia. According to the Banking Law, public credit registries can only provide credit bureaus information on microcredit, small business, and consumer loans from the regulated financial systems. Therefore, non-regulated MFIs cannot access other types of loans, such as mortgages and corporate loans.

Both situations fail to maintain a balance of rights, as regulated institutions have access to information from both the regulated and non-regulated financial system though non-regulated institutions do not. This also violates the reciprocity principle (See below), increasing distrust in the credit reporting system.

Respect for the Reciprocity Principle: Most of the countries in this study respect the reciprocity principle, which stipulates that only those institutions that report data to credit bureaus can consult them.

In some countries, where it is not mandatory to report positive data, namely all of the debtor's credit information whether it includes on-time payments or not (*See Glossary*), some institutions report negative information (only arrears) and therefore only have access to the credit bureaus' negative data.

However, in Guatemala, some bureaus accept inquiries from large financial institutions even if they do not report data in order to maintain business sustainability. This practice is unfair for all other reporting institutions that are required to report in order to have access to the information.

In other cases, in order to facilitate the adaption of MFIs to credit bureaus, MFIs are occasionally allowed to consult the database for a limited period of time to encourage them to report.

3.5 Excessive legal protection of the debtor

For the most part debtor and MFI rights are proportional in the countries studied.

However, there are countries where the debtor is excessively protected, creating informational gaps for the MFIs.

In contrast, in other countries there are imbalances in favor of financial institutions.

The best practices observed are the following:

Standards that can be met by all participants: In most countries it was observed that the participants of the credit reporting system could meet the standards without much difficulty.

In Peru, where the regulatory framework is strict and some standards may be initially challenging (such as the implementation of offices specializing in customer service), MFIs are learning the rules leading up to their continued compliance.

Balance between the rights of the debtor and those of the MFI: In some of the analyzed countries there was a clear balance between the protection of the customer's information and adequacy of data for MFIs to perform credit analysis.

On the other hand, in Peru and El Salvador, the limitation of 2 to 3 years of data retention of canceled loans in credit reports over-protects the customer and fails to protect the MFIs. This period is too short to analyze the debtor's payment behavior, disfavoring the MFIs credit analysis.

Reasonable and staggered penalties based on the amount of errors: Brazil is an example where the penalty is calculated based on the credit report's number and size of errors. For example, the fine corresponds to 10 times the amount of the error, thus creating an incentive to prevent errors.

3.6 Insufficient Data

Generally, in the surveyed countries positive information is reported. In other cases, the reporting institutions are free to choose the type of information they want to report (positive or negative).

In some countries there are legal limitations to reporting positive information (e.g. Brazil), or in showing the name of the loan provider (e.g. Mexico), which hinders data accuracy for credit analysis.

Most countries meet the minimum data requirements of the World Bank's General Credit Reporting Principles. Therefore, they have been able to incorporate specific microfinance data in credit bureaus.

The factors that have successfully led to sufficient data are the following:

Regulation allowing positive information: In most countries it is possible to publish all of the debtor's credit information, be it timely or not.

In contrast, Brazil did not allow this for many years, limiting the financial institutions' credit analysis. The regulatory framework that allows the reporting of positive information was recently approved.

It should be noted that in some countries it is voluntary to report positive information, which leads to insufficient data. For example, in Nicaragua and Guatemala some institutions report positive information and others only report negative information. In some cases there are accords with credit bureaus to only report some credit products and in others they also agree on the age of arrears. This limits the credit analysis of MFIs and the services offered by credit bureaus.

Contracts requiring positive information: Since in some countries it is voluntary to report positive or negative information, some bureaus fill this gap by requiring positive data reporting.

For example, in the Dominican Republic, the obligation to report positive information in credit bureaus' contracts has led to data sufficiency and to the offering of sophisticated products, benefitting the financial system.

Credit bureaus share arrears information to mitigate risk: Generally MFIs only report to and consult one or two credit bureaus. Despite the costs involved, they cannot see all of the debtor's financial behavior given that the information is dispersed amongst various credit bureaus.

To fill this gap, credit bureaus in Mexico share arrears information that is 30, 60, and 90 days past due (depending on the type of loan), as well as fraudulent loans. Though it is not ideal to share all information between credit bureaus, this practice mitigates risk. In addition to supporting the repayment of loans, it also helps to achieve data sufficiency.

Consultations priced based on the amount of information reported: Transunion of Nicaragua and Guatemala has a policy of establishing a price per consultation based on the number of inquiries and the amount of information reported to the credit bureau.

Given the significant difference in price of reporting positive vs. negative data (the savings can reach up to 20%), it is a motivating factor to report positive data. This also significantly favors service efficiency (*See section 3.8 Good Service, though with relatively high costs*).

In both countries, it is not a requirement to report positive data, so it is necessary for credit bureaus to administer this policy in order to obtain positive data.

Partnerships between credit bureaus, MFIs and MFI networks to incorporate necessary data into the financial system: In various countries, credit bureaus and MFI networks have made efforts to understand what data is needed by the microfinance sector.

Credit bureaus, specialized in microfinance, have done commendable work. These specialized bureaus, often with share ownership by MFIs, were created to fill the gaps left by the traditional credit bureaus. Since then, the non-specialized bureaus have made efforts to offer similar sector specific MFI data.

The achievements of specialized credit bureaus in Bolivia, Mexico, and Nicaragua are seen through their offering of additional, non-traditional credit data, rarely seen in other countries, such as:

- a. Quota amount.
- b. Payment Frequency.
- c. Exact number of days in arrears.
- d. Number of payments past due.
- e. Maximum number of days in arrears.
- f. Methodology type.
- g. Direct and indirect customer debt in group loans, etc.

Amounts reported (from one unit) in local currency: In all of the surveyed countries there is no minimum amount to report. Institutions are allowed to report debts in local currency from one unit of the currency, which favors microfinance, given the small loan amounts.

3.7 Short data retention

In general, the data retention period in the surveyed countries is good given that it allows for the evaluation of the debtor's behavior in a reasonable amount of time. However, in both Peru and El Salvador, legal limitations impose tight timelines on bureaus, hindering credit analysis.

The best observed practices are:

An average of six years for unpaid debts: Mexico provides the best example from the surveyed countries in terms of data retention for unpaid debts. In Mexico, an unpaid debt remains listed in credit bureaus for six years, which appears to be an acceptable period of time for MFIs.

In contrast, in Colombia unpaid debts remain for 10 years (plus another 4 as a penalty) in the credit bureaus, which seems too long and prevents the customers from reinstating themselves in the financial system.

Five year average for canceled debt: In the surveyed countries, canceled debts remain approximately five years in the debtor's history, a reasonable amount of time in order to analyze the customer's credit history.

In Peru and El Salvador, on the other hand, regulations only allow canceled debts to remain in the client's credit history for 2 and 3 years, respectively, which is an insufficient amount of time to study the customer's credit behavior.

This does not maintain the proportionality of rights since it favors the debtors and disfavors financial institutions by providing less information.

Staggered data retention periods for unpunctual debt: In Colombia, debts that were not paid punctually remain for twice the amount of time in which the debts were paid, up to a maximum of four years in the debtor's credit history.

Staggered retention periods reward customers who pay with less time in arrears. Consequently, this can be a motivating factor for customers to pay their arrears more quickly.

3.8 Relatively high prices

In most of the analyzed countries, credit bureaus are trusted. Their service is good and is generally done over the internet and via dedicated communication (*server to server*). In the latter instance, MFIs design their own reporting format, facilitating the work of loan officers.

In many countries, credit bureaus have a department or a person dedicated exclusively to the microfinance sector, enabling a better identification of the sector's needs.

Besides regularly consulting with debtors, credit bureaus offer MFIs other specialized services, such as monitoring, alerts, standard scoring, personalized scoring, credit evaluation, etc.

However, in some countries, credit bureau services are expensive and can be a limiting factor in institutional participation. The average cost per consultation in the surveyed countries is US\$1.00. However, in some countries the price is higher, reaching up to US\$3.00 and US\$5.00 per consultation.

Factors that help attain good service and to reduce the prices of these services are:

Good Internet Providers: In general, there is good internet service in urban areas.

In Bolivia there are some rural areas where the service is not good and the credit bureau, Infocred, has provided fiber optics to MFIs with high transaction volume. This measure has improved service reliability.

Advanced notice prior to maintenance: Generally, credit bureaus notify customers in advance of any upcoming service interruption. These usually occur during the weekends.

Backup equipment in case of a disaster or service interruption: Credit bureaus usually have service continuity programs in the event of an interruption. In some cases, these include service providers in other cities, which involves large investments.

Competition among various credit bureaus: In countries where there are several credit bureaus, service prices tend to be lower. For example, in Peru where there are five credit bureaus, prices range between US\$0.10 and US\$0.70 per consultation, depending on the number of inquiries. The average price in the surveyed countries is US\$1.

Furthermore, in Peru, there have been increased efforts by the various credit bureaus to offer specialized services at affordable prices. This benefits MFIs by reducing credit risk.

Public credit registries provide data to credit bureaus: In Peru, the public credit registry shares its entire database with credit bureaus at no cost. This reduces operational costs, since credit bureaus do not have to independently collect data, but it also harms the timeliness of data.

Though there are public credit registries in other countries such as Brazil, Nicaragua, El Salvador, and the Dominican Republic, credit bureaus do not receive their information. Rather, credit bureaus collect data independently, increasing their costs.

Agreements between MFI networks and credit bureaus: Mexico has achieved good agreements between MFI networks and credit bureaus. It is positive that both of Mexico's credit bureaus had the opportunity to negotiate with the networks, while at the same time signing individual contracts with each institution. This has led to healthy competition and balanced data between the credit bureaus in the microfinance sector.

A positive experience in Peru has been the partnership between an MFI network and the credit bureau Sentinel. In achieving an increased number of credit bureau consultations, they were able to reduce the price to US\$0.06 per client per month (unlimited consultations per month). This is the lowest price seen throughout the surveyed countries.

Trade association partnerships to collect data: In Brazil, trade associations have experimented for many years with data collection and these in turn coordinate with credit bureaus. This has allowed for lower prices for consultations, since credit bureaus' operating costs are reduced.

Zero charge when the customer has no credit history: In Mexico, in order to provide incentives to MFIs that provide loans to the lower niche of the population, there are agreements to not charge for the credit checks when the customer has no credit history.

This is more beneficial for MFIs that provide loans from village banks, where there are many customers and they often have no credit history.

Credit reports with different levels of information: In El Salvador, credit bureaus offer three types of credit reports depending on the level of data (basic, intermediate, and complete).

These reports are priced differently and it is up to the MFI to decide which type of report they need and are willing to pay for.

In some countries, credit bureaus only offer one type of credit report, some of which may be lengthy and include data that is not necessarily useful for the MFI's analysis. This increases the MFI's costs, both for the consultation and for the price of printing such lengthy reports.

3.9 Fears of conflict of interest because of MFI share ownership in credit bureaus

Generally, MFIs and credit bureaus publish information about their businesses, services, and customer complaints. However, information is not published regarding shareholder composition (ownership), which leads to fears of conflicts of interest within the microfinance sector.

Usually the users in the surveyed countries have the same rights to report and access information.

The best observed practices in the analyzed countries are:

Banning financial institutions from being shareholders in credit bureaus: Some countries prohibit financial institutions from ownership of credit bureaus in order to avoid conflicts of interest. Reliability and trust in the credit bureaus help increase institutional reporting to credit bureaus, benefitting data integrity.

In contrast, in Mexico and Guatemala, where microfinance institutions can be shareholders in credit bureaus, there are fears of unfair competition. These fears exist despite the lack of evidence to justify the fears and affect the participation of institutions in credit bureaus.

Limits on shareholder participation by financial institutions in credit bureaus: In order to avoid conflicts of interest by financial institutions in credit bureaus, Mexican regulations limit MFI shareholder participation to 18%.

This legal standard helped to reduce the risks of conflict of interest. However, fears of unfair competition remain in the microfinance sector.

Publication of share ownership percentages in newspapers: Bolivia is the only country that publishes credit bureaus' share ownership. This data is published bi-annually in newspapers by the supervisory body. Both credit bureaus also publish a list of their shareholders on their websites.

This law is important in Bolivia given that laws do not prohibit financial institutions from owning shares of credit bureaus.

Equitable access to information for all users: Although some MFIs are shareholders in credit bureaus, there are no differences between them and non-shareholders in the requirements or type of information available.

In some cases where financial institutions are shareholders in the credit bureaus, there is a minimal reduction in the consultation cost, but this does not restrict the use of the data by other institutions.

Banning of exclusive reporting contracts: In Nicaragua, contracts that force institutions to report exclusively to one bureau are prohibited. As a result, MFIs that are shareholders in one credit bureau can freely report to other credit bureaus and generally do so.

By contrast, in Peru, the contract between Copeme and Equifax (*See section 3.3 Lack of data accuracy*) initially required exclusive reporting to Equifax. This resulted in Equifax's predominance of information in the microfinance sector, which has led to higher prices (compared to other bureaus) of both consultations and specialized services.

3.10 Inadequate disclosure or failure to comply with existing rules on data and consumer rights protection

In most of the surveyed countries there are sufficient rules to protect data and consumer rights. Regulations are clear and the penalties for failure to comply are predictable.

The rules include the minimum rights of the debtor, such as: to be informed of the purpose of the collection, processing, and distribution of their information, periodic access to their information, and claims.

Claims are usually resolved by government consumer protection agencies. However, the failure to disseminate regulatory information in effective ways limits the consumers' awareness of their rights to make these claims.

Some countries are in the early stages of adopting these standards, while in others the rules exist but are not enforced, harming consumers.

The best practices related to data protection and consumer rights are:

Bank privacy over lending and borrowing: In most of the analyzed countries there is banking privacy over lending and borrowing operations. Meaning, customers are consulted for their permission prior reporting their information to credit bureaus.

Peru, on the other hand, does not have bank lending privacy, which could eventually expose the consumer to misuse of their information.

Credit bureaus audits of bank privacy compliance: In Mexico, credit bureaus conduct audits, soliciting proof from MFIs of customer authorization to obtain credit reports. If breaches are detected, they are reported to the government's consumer protection agency and service is discontinued to the financial institution.

This helps build trust in the credit reporting system. Brazil is an example where compliance with credit bureau and consumer protection standards is strict and can incur severe penalties, thereby generating trust and maintaining a strong credit reporting system.

Clear and short processes: Peru is an example where there is a clear customer complaints process. Besides establishing petitions in the regulated and non-regulated system, there are reasonable deadlines to tend to the claims.

On the other hand, in Guatemala there are no established processes for making claims. This causes the customer to sometimes approach the institution that made the errors and other times to approach the credit bureau. Credit bureaus in Guatemala have established internal policies to resolve claims due to the absence of consumer protection regulations.

Effective dissemination of regulations: In Peru there is strong dissemination of the regulations and, consequently, customers guard their rights.

Visible means are used to disseminate the regulations, for example, posters and videos in offices and the use of radio and television mass media.

However, in other countries there is insufficient dissemination of the regulations, leading to few customer claims.

Effective agencies to monitor compliance: A key factor in compliance with the participants' rights in the credit reporting system is the effectiveness of monitoring agencies.

In some of the surveyed countries there are government agencies and a supervisory body that efficiently enforce consumer protection regulations. Penalties are applied based on the regulations.

In Nicaragua, on the other hand, some institutions were unaware of the consequences of non-compliance or, if they were aware, they acknowledged that regulations are not enforced.

Accessible places to file claims: Establishing customer complaint locations near the customers facilitates their ability to file claims.

Brazil is a good example, where in every mall there are claims kiosks. There are also small claims courts that resolve small, short term claims.

Peru is another example where each regulated financial institutions is supposed to have a specialized unit that receives consumer claims, facilitating access.

In Nicaragua and other countries, however, there is only one office of the supervisory body and of the credit bureaus in the country's capital, making it impossible to make claims in the interior cities of the country.

4

Conclusions



1. The main challenges faced by the Latin American microfinance sector regarding credit bureaus, in order of importance, are:
 - ▶ Lack of available data
 - ▶ Lack of reporting institutions and dissemination of data in the credit bureaus
 - ▶ Lack of data accuracy
 - ▶ Regulatory framework that discriminates against MFIs
 - ▶ Excessive legal protection of the debtor
 - ▶ Insufficient data
 - ▶ Short data retention
 - ▶ Relatively high prices
 - ▶ Fears of conflict of interest caused by MFI share ownership in credit bureaus
 - ▶ Insufficient dissemination or failure to comply with the existing data and consumer protection regulations.
2. Each country has different challenges, which are listed in Appendix 1 of this report. The appendices also list the legal, regulatory, government policy, technical, and training recommendations that could mitigate these problems.
3. There are “best practices” that have been used in the analyzed countries, which have helped mitigate the aforementioned problems. These best practices are listed after each challenge presented in the body of this report (*See Conclusion 1*).

5

Recommendations



1. We recommend that the appropriate authorities and the various participants in the credit reporting system take actions to reverse the problems mentioned in Conclusions 1 and 2.
2. For the solution of the aforementioned challenges, it would be useful to compare the priorities of the problems listed in Conclusion 1, with the respective challenges for each country (Conclusion 2). This would be done in order to achieve a greater positive impact in reducing the risk of customer over indebtedness.
3. When possible, it would be useful to include within the individual country solutions the best practices that have been successful in other countries to mitigate or avoid the challenges discussed above.

Annex1

ANALYZED COUNTRIES' ALIGNMENT
WITH THE GENERAL CREDIT REPORTING
PRINCIPLES



↳ EXECUTIVE SUMMARY

The level of microfinance institution (MFI) inclusion in the Bolivian credit bureaus and the strong culture of reporting and using credit bureau information is commendable. However, the microfinance sector still has a relatively long road to travel towards achieving an excellent credit reporting system. Improvements could be made in the accuracy, adequacy, and timeliness of the data, as well as in the regulatory framework.

The timeframe for missing information is approximately 50 days, quite far from the record achieved by Brazil, which updates data daily. Despite the high participation of MFIs in credit bureaus, there is still low participation of public sector institutions and non-financial sector credit providers compared with the other countries studied.

The public credit registry⁶ provides information to regulated financial institutions (including eight MFIs). However, since the credit bureaus were legally formed to serve the microfinance sector, the supervisory entity⁷ only provides information on microcredit, consumer and SME loans. This affects the sufficiency and integrity of the non-regulated MFIs' credit analysis.

Given its specialization in the microfinance sector, Infocred is the credit bureau with the greatest number of reporting MFIs. It is hoped that with the regulation currently in process for non-regulated MFIs, they will be able to report and access comprehensive information on the regulated financial system via the public credit registry.

While rules exist regarding consumer protection for the regulated sector, they are still in the implementation process for the non-regulated sector.

⁶ Central de Información de Riesgos (CIRC).

⁷ Autoridad de Supervisión del Sistema Financiero (ASFI).



UNDERSTANDING THE BOLIVIAN MICROFINANCE SECTOR IN RELATION TO THE PUBLIC CREDIT REGISTRY AND CREDIT BUREAUS

Bolivia has a mature microfinance sector. It is characterized by a high level of competition, moderate portfolio growth (in comparison to other countries), and lending rates among the lowest in the microfinance sector worldwide.

There are eight regulated microfinance institutions grouped within ASOFIN and 13 non-regulated grouped within FINRURAL⁸. Through a 2008 resolution by the supervisory agency, the latter are in the process of becoming regulated with the possibility of accepting deposits.

Though the government has not set interest rate limits, it has sent a clear message encouraging their reduction and emphasizing a focus on productive sector loans. The government contributes to its effort to keeping rates low by offering favorable funding conditions through a second-tier bank.

Bolivia's public credit registry has been run by a supervisory agency for more than 20 years and has been one of the pioneers in getting non-regulated MFIs involved in reporting to and consulting with credit bureaus. The strong competition in this small market has quickly turned it into a mature market. This, coupled with the strong consumer loan offerings in the 2000s, resulted in a decline in portfolio quality and an increase in groups of non-paying debtors. This unrest resulted in acts of violence against the supervisory agency and MFIs.

This situation, along with the strong leadership of microfinance networks, contributed to Bolivian MFIs recognizing earlier than other markets the benefits of reporting to credit bureaus.

The search for institutional strengthening, transparency, better interest rates for funding, and the need to collect deposits to finance growth have led to self-regulation efforts.

During this process, non-regulated MFIs began to voluntarily comply with the rules of the regulated system, such as adopting a chart of accounts, debtor's credit ratings, and provisions, among others. This resulted in a high participation among MFIs in the credit bureaus.

In effect, the level of culture of use of Bolivia's credit bureaus is surprising. Currently, all the non-regulated MFIs that belong to FINRURAL report their information, with even most of the unaffiliated ones reporting as well. It is estimated that there are very few unaffiliated MFIs who do not report.

There is one public credit registry and two credit bureaus (Infocred and Enserbic). These are regulated and were formed to serve the microfinance sector. Infocred has regulated and non-regulated MFIs as shareholders, and Enserbic's shareholders are the country's Chambers of Commerce.

The public credit registry, run by the supervisory agency, collects information from regulated institutions, but only sends information on microcredit, consumer, and SME loans to the credit bureaus.

The credit bureaus collect additional information on the unregulated microfinance sector and public and private institutions. Their services are offered through agreements with the financial and non-financial sectors users. Regulated institutions can access all the supervisory agency information online for free.

⁸ The Association of Financial Entities Specialized in Microfinance (ASOFIN) and the Association of Financial Institutions for Rural Development (FINRURAL) are networks of regulated and non-regulated MFIs, respectively.

Lessons learned after several crises have led to strong, prudent measures by the supervisory agency. In addition, with the active participation of the microfinance networks and to fulfill a constitutional mandate to support the microfinance sector, the supervisory agency issued specific village banking and agricultural loan regulations not seen in other Latin American countries.

ALIGNMENT OF THE BOLIVIAN MICROFINANCE SECTOR TO THE WORLD BANK'S GENERAL PRINCIPLES FOR CREDIT REPORTING

Utilizing the General Principles for Credit Reporting published by the World Bank in September 2011 as a reference, the following is presented as a diagnostic of the Bolivian microfinance sector.

General Principle 1: **Data** *(See definition in Annex 3)*

↘ **Guidelines on accuracy of data**

The accuracy of the data issued by the credit bureaus is moderate⁹. MFIs are reporting with minimal errors; however, there are cases of inconsistencies stemming from the duplication of personal identity documents by the public entity that administers them¹⁰.

The supervisory agency oversees the public credit registry where all the regulated financial institutions report. The forms for collecting information can be easily filled out by MFIs and the data is strictly validated by the supervisory agency.

Likewise, the credit bureaus have reliable authentication systems. Currently, there are efforts taking place with the public entity that handles identity documents to reduce duplication inconsistencies. According to estimates from Infocred in May 2012, duplication inconsistencies accounted for 15% of reported debtors.

In addition, the supervisory agency has given specific instructions to regulated institutions in order to minimize this problem.

Further, some MFIs are incorporating debtor biometric information in order to avoid the duplication of personal identification.

⁹ See "Scale" in the Glossary.

¹⁰ General Personal Identification Service (SEGIP).

↘ Guidelines on timeliness of data

Credit bureau data is not timely for its users.

After receiving the information from the public credit registry, the credit bureaus make it available to users approximately 20 calendar days after the close of the month. This represents, on average, a 50 day time frame where the information is not available. For example, information from March 31, 2012 cannot be accessed until May 20, 2012

The lack of data timeliness is risky considering that the debtors in the microfinance sector have quick access through various MFIs to small loans without guarantees. One of the reasons for this is the technical limitations in the Bolivian financial system in collecting and distributing information with greater frequency.

For the regulated institutions, this risk is mitigated because they have access to public credit registry information approximately 10 days after a month's close.

This information gap is also covered by the credit bureaus, which provide MFIs with the debtor's "request footprint," that is, the attempts made by debtors in other institutions to obtain loans during the information gap phase.

Of the countries studied, a good example of timeliness is Brazil, where negative information is reported daily online daily through the use of sophisticated technology.

↘ Guidelines on sufficient data – including positive

Data adequacy in Bolivia's credit bureaus is moderate. There is an absence of some basic data because the credit bureaus do not have information on corporate and mortgage loans.

The public credit registry provides all of the information on the regulated financial system to the regulated institutions (including eight MFIs). However, because of the Bank and Financial Institutions Act, the credit bureaus only have access to information on microcredit, consumer, and SME loans. The other types of credit (corporate and mortgage) are available only to regulated institutions via the public credit registry.

Although the microfinance sector does not predominantly provide corporate and mortgage loans, this still constitutes a gap in the loan analysis of non-regulated MFIs (greatest in number). Of the countries studied, Peru's public credit registry provides the credit bureaus with all of their databases, reducing the credit risk in both the regulated and non-regulated sector.

The information listed by the credit bureaus is positive (*See Glossary*), that is, it reflects all of the activity of the debtor, whether they are timely or not in fulfilling their obligations. However, the authorization of the debtor is required to be listed and consulted.

A positive aspect of Bolivia's reporting system is that institutions report loan amounts starting from even one Boliviano (approx. US\$0.15). This is commendable given that MFIs have access to information on even the smallest debtors.

Bolivia registers village banking loans as a type of credit authorized by the supervisory agency, which has not been the case in other countries where either there are no village banking loans within regulated institutions or they are lumped under microcredit. The supervisory agency in Bolivia even displays both individual and group balances.

Annex 1 **Bolivia**

In general, it would be useful to have the following additional information in order to improve credit risk analysis:

1. Corporate and mortgage loan information (legally restricted).
2. Refinanced loans (change of original loan conditions because of payment difficulties).
3. Criminal proceedings.
4. Information on public service companies such as water and electricity.
5. Tax debt (legally restricted).
6. Greater number of loan providers from the non-financial sector.
7. Chamber of Commerce information.

↘ **Guidelines on collection of data on a systematic basis from all relevant and available sources**

Collection of microfinance data within the country is very good. The majority of non-regulated microfinance institutions submit reports. However, they only report to one credit bureau that specializes in microfinance. Furthermore, there is a shortage of data collection and relevant information from loan providers in the non-financial sector and public entities.

According to legal regulations, regulated financial institutions report directly to the public credit registry, which then forwards the database to the credit bureaus.

Unlike other countries, the microfinance institutions in Bolivia have a strong culture of reporting to and consulting with credit bureaus. Despite the fact that there is no legal obligation for MFIs and non-regulated cooperatives to report, there is no doubt of the importance of credit bureaus in controlling credit risk. It is estimated that there are very few even small credit providers (including cooperatives) that do not report.

The efforts made by the Finrural network (a network of non-regulated MFIs) over the past several years in promoting a culture of working with credit bureaus are admirable. These initial efforts to include affiliates as credit bureau reporters went hand in hand with the “self regulation” process (*See Context*).

Initially, it helped MFIs to have an electric filing model to report to Finrural (despite the fact that, at that time, it was not legally recognized as a credit bureau).

Subsequently, the supervisory agency issued a ruling that would officially permit the development of credit bureaus to serve the microfinance sector. From there, Infocred was born (owned by Fundapro and MFIs affiliated with Asofin and Finrural)¹¹ and Enserbic (owned by the country’s Chambers of Commerce).

Infocred stands out for adapting its services to the microfinance sector and has the majority of regulated and non-regulated MFIs reporting to it. Enserbic has specialized more in commercial and judicial information.

In both credit bureaus, credit reports still lack important data from public institutions. Of the non-financial sector, the credit bureaus say that there are still credit providers who do not report out of fear of losing their customers.

¹¹ Fundapro is a second-tier non-regulated financial entity. Asofin, Finrural and Fundapro have a 35%, 35% y 30% stake as shareholders Infocred, respectively.

↘ **Guidelines on retention of data**

The information retention among the country's public credit registries is good.

Unpaid debt appears on the credit reports for five years and lapses after ten years. Internally, credit bureaus should keep all information for ten years.

The canceled debt history also appears for five years.

General Principle 2: **Data Processing: Security and Efficiency** *(See definition in Annex 3)*

↘ **Guideline on security measures**

The information security measures in the credit reporting system of the Bolivian microfinance sector are moderate.

For regulated MFIs, there are strict measures regarding information security which were set by the supervisory agency.

The supervision over the credit bureaus also requires information security measures. In general, these entities are governed by strict internal security standards.

By nature, MFIs do not have information security standards required by outside parties. This is a big void, considering that they are larger in number than regulated institutions.

This risk is mitigated through a credit bureau service contract, which stipulates minimum requirements regarding quality and continuity of information. Despite this, some institutions still exhibit technological limitations and a lack of specialized personnel.

↘ **Guideline on reliability**

The public credit registry and the credit bureaus in Bolivia offer very reliable service.

In general, the service is continuous. There are minimal interruptions in internet service or previously scheduled disruptions by the credit bureaus.

↘ **Guideline on efficiency**

Generally, credit bureau service is very good and has low prices.

Infocred has most of the information on the microfinance sector and is able to offer alert services, which reduce credit risk.

The most common method available to access credit reports is through online access. However, there are internet limitations in remote rural areas which do not allow for efficient service. Infocred has offered fiber optic services to its users with a high enough level of operations to justify the investment.

Annex 1 **Bolivia**

The price per request (on average US\$0.35) is low in comparison to the average of the countries included in this study (US\$1.00).

The supervisory agency annually requests a justification of the prices charged by credit bureaus. The public credit registry service is free for the regulated institutions.

General Principle 3: **Governance and Risk Management** *(See definition in Appendix 3)*

↘ **Guideline on accountability of governance arrangements**

The credit bureaus in the country respond to third parties in an acceptable manner. They report to the supervisory agency, promoting a high level of accountability in the business' management and data and consumer protection.

↘ **Guideline on transparency of governance arrangements**

The credit bureaus' transparency regarding their business is excellent. Bolivia is the only country that publishes credit bureaus' shareholder percentage composition.

Typically, the credit bureaus have a webpage describing their business, products, consumer complaint system, and the names of their shareholders.

The shareholder percentage distribution is published biannually in the newspapers at the supervisory agency's request. This information is particularly necessary in Bolivia, since the law does not prohibit financial institutions' ownership in credit bureaus. Within this context, Infocred has both regulated and non-regulated MFI shareholders.

↘ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

Although the credit bureaus are regulated, business risk management supervision by the supervisory agency is less stringent than with the regulated MFIs.

The supervisory agency has a specialized unit responsible for monitoring the credit bureaus, which allows for continuous monitoring.

It should be noted that in general the credit bureaus are careful in their business administration because of the high level of sensitive information that they handle.

↘ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

Though the credit bureaus would like to have the right to access all information, there is a legal restriction within the regulatory framework that only allows the credit bureaus to receive micro-credit, consumer, and SME loan information from the public registry database *(See Guidelines on non-discrimination)*.

Supposedly, there are no conflicts of interest of ownership despite the fact that Infocred is the property of the regulated and non-regulated MFIs.

General Principle 4: Legal and Regulatory Environment *(See definition in Annex 3)*

↘ Guidelines on clarity and predictability

The standards regarding credit bureaus are framed in the Business Auxiliary Services standards of the supervisory agency. The consequences for failure to comply with these standards are predictable.

However, in comparison with the other countries studied, there is little effort on the part of the authorities to disseminate consumer rights information. In microfinance, such dissemination takes place through credit officers, who inform debtors about their rights and obligations.

Of the countries studied, Peru is a good example of effective information diffusion, where various outlets accessible to the debtor are used, such as videos, posters in offices, as well as information in the mass media: radio, TV, etc.

↘ Guidelines on non-discrimination

According to the Bank and Financial Entities Law, credit bureaus only have access to information on microcredit, consumer, and SME loans in the regulated¹² financial system, which affects the adequacy of data for non-regulated MFIs.

In this situation, equal rights are not maintained, as regulated institutions have access to information on all of the loan products in the regulated financial system (via the public credit registry) and the non-regulated financial system (via the credit bureaus). This breaches the reciprocity principle, undermining confidence in the credit reporting system.

The lack of information for the non-regulated financial sector and the non-financial sector prohibits a comprehensive analysis of the debtor.

It also impacts the integrity of the database for the specialized products offered by the credit bureaus. For example, the regulated institutions are not favored in the specialized products offered by Infocred because the credit bureaus do not have complete databases of information on regulated institutions.

↘ Guidelines on proportionality

The current regulations in the country are balanced and proportional.

It is possible for all members of the credit reporting system to comply with regulations. In the case of non-compliance, the penalties given by the authorities are reasonable.

¹² Only loans overdue by more than 90 days are received.

Annex 1 **Bolivia**

However, over the last few months, because of the legal regulations regarding credit bureaus, Infocred has not been assigning a score, as it had been doing previously. The supervisory agency's fear is that the score will be used as the sole factor to approve or deny credit. This represents less information to the sector, weakening the balance that had been maintained up to this point.

↘ **Guidelines on consumer rights and data protection**

There have been recent efforts by the authorities in the country regarding comprehensive rules on data protection and debtor rights.

Although there are some rules on minimum rights of the debtor, they are general and do not refer exclusively to data protection and consumer rights.

Banking privacy exists for savings and loans. As a result, the authorization of the debtor is required in order to report and access their information. Both credit bureaus verify that the institutions reporting to them comply with this legal standard.

↘ **Guidelines on dispute resolution**

There are only clear legal mechanisms to address debtor complaints in the regulated system.

This system requires that each institution have an area dedicated to notifying the debtor and receiving their complaints. The system has been successful in processing complaints within the established timelines.

There is a Deputy Minister of the Defense of User and Consumer Rights that regulates the general protection of the consumer (including financial) for the non-regulated sector. However, the participants in this study feel that the average citizen does not know of them or how to use this as a way to resolve their complaints.

When they have a complaint, some debtors turn to the institution where the error originated while others contact the credit bureau directly, where they are treated according to the bureau's internal rules.

The recent implementation of complaint resolution areas in non-regulated MFIs that are in the regulatory process also helps mitigate this risk (*See Context*).

CONCLUSIONS

This section classifies conclusions according to the principles set forth in the body of the report:

General Principle 1: Data

- ▶ In general, the accuracy of the data issued by the credit bureau is moderate. The MFIs report with minimal errors. However, there are cases of inconsistencies from the duplication of personal identification documents, coming from the public entities that produce them.
- ▶ The data of the country's credit bureaus is not appropriate for the users. There is an information gap of an average of 50 days.
- ▶ The timeliness of the data in the credit bureaus in the country is moderate. In addition to missing some basic information, the credit bureaus only have information on microcredit, consumer, and SME loans, but not on corporate or mortgage loans.
- ▶ The collection of microfinance data in the country is very good. The majority of non-regulated microfinance institutions report. However, they only report to a specialized credit bureau. There is also limited participation of credit providers in the non-financial sector and public entities with relevant information.
- ▶ The retention of information by the public credit registry and the credit bureaus is good.

General Principle 2: Data Processing: Security and Efficiency

- ▶ Information security measures in the credit reporting system of the Bolivian microfinance sector are moderate because the sector is largely unregulated.
- ▶ In the country, the services of the public credit registry and the credit bureaus are trusted.
- ▶ In general, credit bureau service is good and has low prices.

General Principle 3: Governance and Risk Management

- ▶ The credit bureaus in the country respond favorably to third parties. They report to the supervisory agency, promoting a high level of accountability in business management and data and consumer protection.
- ▶ The credit bureaus' level of transparency is excellent. Bolivia is the only country that publishes the credit bureaus' shareholder percentages.
- ▶ Although the credit bureaus are regulated, the supervision of risk management by the supervisory agency is less stringent than with the regulated MFIs.
- ▶ Though the credit bureaus would like to have the right to access all information, there is a legal restriction within the regulatory framework that only allows the credit bureaus to receive microcredit, consumer, and SME loan information from the public registry database (*See Guidelines on non-discrimination*).

General Principle 4: Legal and Regulatory Environment

- ▶ The credit bureau standards are framed by the supervisory agency's rules on auxiliary services companies. The consequences for non-compliance are predictable.
- ▶ According to the Bank and Financial Entities Law, the credit bureaus only have access to information about microcredit, consumer, and SME loans in the regulated financial system, affecting the timeliness of the information for the non-regulated MFIs. This violates the principle of reciprocity.
- ▶ Within the country's current regulations, there is proportionality and balance. However, in the last few months because of the legal regulations regarding credit bureaus, Infocred has not been assigning a score, as it had previously done. This represents less information for the sector, weakening the balance that had previously been maintained.
- ▶ There have been recent efforts by the authorities regarding comprehensive rules on data protection and consumer rights.
- ▶ There are only clear legal mechanisms in the regulated financial system to address debtor claims.

RECOMMENDATIONS

This section classifies recommendations according to their type.

Legal

- ▶ Give credit bureaus access to all public credit registry information.
- ▶ Adopt specific rules on consumer protection, which apply to debtors in the non-regulated financial system, as well as the necessary mechanisms to ensure their compliance.

Regulatory

- ▶ Study the supervisory body's to determine the feasibility of increasing the frequency of updating information, with the goal of improving the timeliness of information.
- ▶ Establish mechanisms to mitigate conflicts of interest that could arise from the financial institutions' ownerships of the bureaus.
- ▶ Develop regulations regarding the obligatory use of the reciprocity principle in using and reporting information to the credit bureaus.

Government Policies

- ▶ Although efforts have been made, the public agency that manages citizen identification needs to be make additional efforts to correct the duplication of personal identity documents.
- ▶ Encourage public entities with relevant information, to share information with the credit bureaus at a reasonable cost in order to benefit the country's credit system.
- ▶ Motivate the credit providers in the non-financial sector to participate in credit bureaus, which will contribute to the improvement of the debtor credit evaluation.
- ▶ Publicize the rights and obligations of the consumer related to the credit bureaus through effective public channels.

Techniques and training

- ▶ Provide technological resources to the financial system that would allow adequate daily information processing. This would be a modest investment compared to the positive impact that it would have on the healthy development of microfinance.
- ▶ While regulation is in process, encourage the non-regulated MFIs to follow similar rules to the regulated sector regarding information security and, in general, microfinance business risk management.
- ▶ Incorporate the following additional information in the credit bureaus' credit reports as much as possible:
 1. Corporate and mortgage loan information (legally restricted).
 2. Refinanced loans (the change of original loan conditions because of payment difficulties).
 3. Criminal proceedings.
 4. Information on basic public service companies such as water and electricity.
 5. Tax debt (legally restricted).
 6. More information on non-financial sector credit suppliers.
 7. Information on Chambers of Commerce.

↘ EXECUTIVE SUMMARY

Brazil's microfinance sector has only a short way to go before achieving an excellent credit reporting system. For many years, the country has been building the most timely credit reporting system of all the countries included in this study. The significant participation of the regulated and non-regulated financial system, as well as the non-financial sector, is impressive. A challenge remains for Brazil's credit bureaus of achieving greater sufficiency of information because currently only negative information is reported.

In fact, although only overdue debts are reported to credit bureaus, daily online updates are made, a process that is not seen in other countries with microfinance.

Technology has been instrumental in the timeliness and accuracy of information. The credit bureaus have made significant investments to reach this level. Based on recent legislation, a database of positive information is being developed to identify the total level of indebtedness of the country's debtors.

The commercial associations in each city have been instrumental in instilling confidence in the reporting institutions. The regulatory framework regarding consumer protection is strong. There is no doubt that reporting to and consulting the credit bureaus is important. The number of financial and commercial institutions that don't participate in the system is minimal. Respect towards banking privacy in lending and borrowing transactions, in addition to reciprocity agreements, have neutralized the fear of unfair competition (a fear prevalent in other Latin American countries).



UNDERSTANDING THE BRAZILIAN MICROFINANCE SECTOR IN RELATION TO THE PUBLIC CREDIT REGISTRY AND CREDIT BUREAUS

The Brazilian microfinance sector is in a stage of development. Due to a large population with income inequality, a poverty index of 25% and an informal sector that represents 18% of the gross domestic product, there is a potential market for microfinance.

Although, there are some rules for the microfinance sector, they are very recent and insufficient to promote its development. The microcredit programs run by the central government have had limited success. Significant subsidies to the public banks do not allow for healthy competition with MFIs that do not receive subsidies.

There are approximately 42 MFIs regulated by the Brazil's Central Bank (known as Microcredit Enterprise Societies, SCM for their initials in Spanish), that are not authorized to receive deposits from the public. The microfinance NGOs (148, known as Public Interest Civil Society Organizations-OSCIP) are only authorized to offer productive microcredit. Additionally, some banks have departments or subsidiaries that specialize in microfinance.

The central and regional governments, through the development banks, offer loans to microfinance organizations under the condition that they only finance productive microcredit. Funding conditions are favorable with low interest rates over and long terms, though with low lending rates (4% monthly) and limits to loan amounts.

Despite reduced competition in microfinance, the large supply of consumer loans increases over indebtedness risk among low-income segments of the population.

Nationally, there is one public credit registry and two credit bureaus. The first, run by Brazil's Central Bank (BCB), collects information from the regulated financial system for monitoring purposes and makes it available to its participants. The BCB also manages the public registry of bounced checks. Additionally, each municipality keeps a record of unpaid municipal taxes.

Serasa Experian and Boavista Services are the two national credit bureaus. Apparently, there are other local credit bureaus, but they are not well known. Serasa Experian still has limited participation from some banks (*not confirmed*). Boavista Services emerged in 2010 from a private equity merger with the Associação Comercial de Sao Paulo. This Association has been in operation for more than 100 years, 60 of which have been as a credit bureau. Equifax has a low level of participation in this credit bureau.

The credit bureaus do not receive information from the public credit registry. They receive negative information directly from the regulated and non-regulated financial sector, as well as from the non-financial sector. Some commercial associations have agreements with the credit bureaus to be intermediaries in collecting and accessing information.

There is a strong culture of producing and accessing information in the Brazilian credit bureaus. All of the financial institutions and almost all of the trade institutions (many members of the trade associations) report negative information (arrears) on a daily basis. In this regard, MFIs have timely information, although it is insufficient because it is only negative.

Since 2001, legislation has allowed for the reporting of positive information. However, a database is being built to support this information, which requires the authorization of all consumers.

ALIGNMENT OF THE BRAZILIAN MICROFINANCE SECTOR TO THE WORLD BANK'S GENERAL PRINCIPLES FOR CREDIT REPORTING

Using the General Credit Reporting Principles published by the World Bank in September 2011 as a reference, the following is a diagnostic of the Brazilian microfinance sector:

General Principle 1: Data *(See definition in Annex 3)*

▾ **Guidelines on accuracy of data**

The accuracy of data issued by the public credit registry is very good.¹³ The supervisory agency oversees the public credit registry, where all the regulated financial system institutions report, which are the only institutions can access the information in the public credit registry.

Simultaneously and voluntarily, these institutions report negative information to the credit bureaus daily, as do the non-regulated financial system and the non-financial sector. The forms designed to collect information are easy to fill out. For this reason, mistakes are minimal, which shows that the direct reporting of information to the credit bureaus does not compromise its accuracy, as is thought to be the case in other countries such as Bolivia and Peru.

Harsh penalties for mistakes *(See Guidelines on proportionality)* are a deterrent to avoid making them. In addition, the debtor has 10 days to review their negative information before being reported to the credit bureaus *(See Guidelines on timeliness of data)*, allowing the possibility of correcting information before it is published.

▾ **Guidelines on timeliness of data**

The credit bureaus' timeliness of information is excellent. Surprisingly, the collection of information from all the participations is completed online. However, there is no standardization regarding the age of the debt (number of days in arrears) that each institution reports.

The credit bureaus collect negative information daily. Brazil is the only country (in this study) whose online collection of data highlights the capacity of the credit bureaus to process a high volume of information. The institutions may report arrears beginning from one day late, however, each one can select how many days of arrears to report.

Immediately after receiving negative information, the credit bureaus should send a notification to the debtor, indicating that they will be reported within 10 calendar days. The notification allows the debtor time to either correct a mistake if one has been made or to pay the debt.

¹³ See "Scale" in Glossary.

Given the cost for the reporting institutions to notify the debtors, some of them report 90 days of default while others may report 15 days, for example. In this context, the information about overdue debts is not standardized and there are periods of misinformation despite the fact that the debtor is already overdue.

The information in the public credit registry is updated monthly. Given that it displays positive information only from the regulated financial system, it is used as a complement to the daily negative information gathered by the credit bureaus.

↘ **Guidelines on sufficient data – including positive**

The adequacy of the information is weak because the credit bureaus do not collect positive information. Only information about overdue debt is published, leaving a gap in data that is important for the credit risk evaluation of the debtor. In the public credit registry, positive information is available, but only regulated entities have access to it.

It is positive that loan amounts are reported to the credit bureaus from one real (approx. US\$0.50), which is commendable given that it makes MFIs with information, even from smaller debtors. For the public credit registry, they recently reported amounts greater than 1,000 reales (approximately US\$500).

In this study, Brazil and the Dominican Republic are the only countries that list in their credit reports information about basic electricity and water services payments, useful information in microloan analysis that is not seen in other Latin American countries.

In general, it would be useful if the credit bureaus had the following information in order to analyze credit risk:

1. Positive information on the debtors.
2. Original loan amount.
3. Balance in default.
4. Individual and group balances for group loans.
5. Quota amounts.
6. Frequency of payments.
7. Loan term.
8. Loan type.
9. Refinanced loans (change in original loan conditions due to payment difficulties).
10. Guarantees.
11. Name of the guarantee.
12. Criminal proceedings.

↘ **Guidelines on collection of data on a systematic basis from all relevant and available sources**

Information collection in the country is excellent. The majority of regulated and non-regulated microfinance institutions report to and consult the credit bureaus. Furthermore, there is strong contribution by the non-financial sector entities with relevant information.

Reporting to the credit bureaus is not mandatory for any regulated or non-regulated entity. Unlike other countries, the culture of microfinance institutions in Brazil reporting to and consulting credit bureaus is very good. Estimates show that very few small MFIs fail to report.

This has been achieved through confidence among the commercial associations, which have been exchanging information for many years. Furthermore, bank privacy for lending and borrowing transactions neutralizes the fear that competitors are competing unfairly.

Some local commercial associations have made agreements with credit bureaus to collect information. To do this, they have software that is very easy to use on a daily basis through the internet. These commercial associations report on a daily basis to the credit bureau, thus keeping all participants informed with timely information.

Independently, the local and federal governments, manage tax records and bounced checks, respectively. The latter are included in the credit bureaus on a daily basis.

↘ **Guidelines on retention of data**

Data retention in Brazil's credit bureaus is weak, considering that the information reported is negative and is only shown in the credit reports until debts are cancelled. However, the credit bureaus retain information internally for ten years, so that a debtor score can be constructed.

The positive information in the public credit registry is maintained through the life of the consumer.

General Principle 2: **Data Processing: Security and Efficiency** *(See definition in Annex 3)*

↘ **Guideline on security measures**

Information security measures in the country's microfinance sector credit reporting system are good.

There are strict information security measures for regulated MFIs. Despite the fact that there is not a supervisory agency for the credit bureaus that regulate and control the information security measures in these companies, they are governed by strict internal information security standards. In addition, there are minimum requirements through the service contracts for the reporting institutions to ensure quality and continuity of information.

Given their nature, a supervisory agency that controls information security for non-regulated MFIs does not exist. However, the daily online approval of information by the credit bureaus significantly reduces the possible inconsistencies.

↘ **Guideline on reliability**

In Brazil, there is a lot of trust in the credit bureaus' services. In general, the services are continuous. It should be emphasized that technological advances within the credit bureaus have allowed for daily processing of abundant amounts of information. Furthermore, the internet service does not cause service problems.

↘ **Guideline on efficiency**

The credit bureau service is good and the price per query is average compared to the other countries studied. The credit bureaus offer diverse standard and personalized services for the institutions according to their agreements, such as debtor risk profile, alerts, score, etc.

The most common mechanism offered to access credit reports is online access to the credit bureaus' web pages.

The price per query is similar to the average of the other countries included in this study (US\$1.00). However, the price is reduced substantially if more queries are made. In this regard, some commercial associations manage to reduce the costs of collecting information from their partners through a web platform, thus increasing the number of queries to the credit bureaus.

The public credit registry service (positive information) to the regulated institutions comes with a minimum charge to cover its operating expenses. However, the supervisory agency does not give public credit registry information to the credit bureaus, as is the case in Peru. Therefore, the credit bureaus have to make an effort to collect information on an individual and a national level, thus increasing operating costs.

Additionally, the act of gathering negative information daily from all the participants presumably raises the operating costs for the credit bureaus.

General Principle 3: Governance and Risk Management *(See definition in Annex 3)*

↘ **Guideline on accountability of governance arrangements**

Brazil is one of the few countries in this study where the credit bureaus are not supervised. The consumer protection agency's vigilant monitoring of standards compliance mitigates third party risk.

↘ **Guideline on transparency of governance arrangements**

The credit bureaus' transparency regarding their business is good, although they do not publish information about their ownership.

Generally, the credit bureaus have a webpage describing their business, products, and consumer complaint system. However, they do not publish information about their shareholder percentage composition, thus limiting transparency to their users.

This indicates that the law does not prohibit the ownership by financial institutions in the credit bureaus. In this context, Serasa Experian is owned by various local banks (not confirmed).

Annex 1 **Brazil**

↘ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

Since the credit bureaus are not monitored, they do not have risk management standards that must be met for the supervisory agency. Nevertheless, it should be noted that they are organizationally strong and have strict measures in place to protect information.

↘ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

It appears that there are no conflicts of interest stemming from the credit bureaus' ownership. All clients have equal access to information.

In the credit bureau Serasa Experian, some banks have minority ownership (*not confirmed*). Despite this, there is free competition among the credit bureaus to offer their services to all the country's users.

General Principle 4: **Legal and Regulatory Environment** (*See definition in Annex 3*)

↘ **Guidelines on clarity and predictability**

The legal regulations for credit bureaus in Brazil, which are well known, are clear and have predictable consequences for the participants in the credit reporting system.

Although there is no specific law, there are various rules regulated by the supervisory agency and government entities pertaining to consumer protection which regulate various aspects within the credit bureaus.

↘ **Guidelines on non- discrimination**

It appears that there is not discrimination within the credit bureaus. All participants have the same right to report and use information. Additionally, the reciprocity principle is strictly respected whereby only participants who report information are able to access it.

↘ **Guidelines on proportionality**

Current legal regulations include provisions for proportionality and balance.

It is possible for all the members of the credit reporting system to meet the regulations. In the event of non-compliance, the penalties by the authorities are reasonable.

The fine is increased in proportion to the error, which serves as a considerable deterrent to making significant errors. Normally, the penalty is 10 times the amount of the error.

↳ Guidelines on consumer rights and data protection

In the country there are sufficient rules on data protection and consumer rights.

The rules include the minimum rights of the debtor, such as to be informed of the purpose of information collection, processing, and distribution, as well periodically accessing their information and the ability to make complaints.

These rules have been implemented since the 1950s and are predominately driven by commercial associations. There is extensive knowledge of debtor rights, which makes Brazil very advanced in comparison with other countries, which have only recently made advances in this area.

There is bank privacy regarding lending and borrowing transactions. Consequently, authorization by the debtor is required to report and access information.

↳ Guidelines on dispute resolution

In Brazil there is a strong culture of resolving debtor complaints. The complaints are resolved within established timeframes. There are consumer protection associations, as well as regional government agencies or federal agencies responsible for protecting consumers of any sector. Additionally, there are small claims courts that resolve small claims in a very short period of time.

In each financial institution or commercial entity, there is a person who receives and manages debtor complaints.

CONCLUSIONS

This section organizes conclusions according to the principles outlined in the body of the report:

General Principle 1: Data

- ▶ The accuracy of the information issued by the public credit registry and the credit bureaus is good. There are minimal mistakes, which shows that providing information directly to the credit bureaus does not compromise information accuracy, as participants in this study in other countries have thought to be the case.
- ▶ The timeliness of the credit bureau information is excellent. The information collection can be done online by all credit bureau users. However, there is not standardization regarding the age of the debt (number of days in arrears) that each institution reports.
- ▶ The adequacy of information is weak, as there is not positive information in the credit bureaus. They only publish information on arrears, leaving a gap in important information for evaluating the debtor's credit risk.
- ▶ The data collection in the country is excellent. The majority of the regulated and non-regulated microfinance institutions report to and consult the credit bureaus. Furthermore, there is a high participation among the non-financial sector entities in providing relevant information.
- ▶ The retention of data in the country is weak, considering that the information reported is negative and only remains until it is cancelled.

General Principle 2: Data Processing: Security and Efficiency

- ▶ Brazil is one of few countries in this study where the credit bureaus are not supervised.
- ▶ The credit bureaus' transparency regarding their business is good, although they do not publish information about their ownership.
- ▶ As the credit bureaus are not supervised, they do not have rules related to risk management that they must fulfill for the supervisory agency.
- ▶ It appears that there are no conflicts of interest in the ownership of the credit bureaus. All the reporting institutions have equal access to the information.

General Principle 3: Governance and Risk Management

- ▶ The legal regulations for credit bureaus in Brazil, which are well known, are clear and have predictable consequences for the participants in the credit reporting system.
- ▶ It appears that there is not discrimination within the credit bureaus. All participants have the same right to report and use information.
- ▶ Current legal regulations include provisions for proportionality and balance. The penalties from the authorities in the event of non-compliance are reasonable.
- ▶ There are sufficient rules regarding the protection of information and consumer rights.
- ▶ In Brazil there is a strong culture of solving debtor claims. The claims are resolved in established timeframes.

General Principle 4: Legal and Regulatory Environment

- ▶ The legal regulations for credit bureaus in Brazil, which are well known, are clear and have predictable consequences for the participants in the credit reporting system.
- ▶ It appears that there is not discrimination within the credit bureaus. All participants have the same right to report and use information.
- ▶ Current legal regulations include provisions for proportionality and balance. The penalties from the authorities in the event of non-compliance are reasonable.
- ▶ There are sufficient rules regarding the protection of information and consumer rights.
- ▶ In Brazil there is a strong culture of solving debtor claims. The claims are resolved in established timeframes.

RECOMMENDATIONS

This section classifies recommendations according to their type:

Regulatory

- ▶ Standardize criteria regarding the age of the debt (days in arrears) that all participants should report to the credit bureaus.
- ▶ Establish mechanisms to mitigate conflicts of interest that could arise from the financial institutions' ownership of credit bureaus.
- ▶ Establish oversight over the credit bureaus, including information security measures.

Techniques and training

- ▶ It would be useful to have the following additional information in order to improve credit risk analysis:
 1. Positive information on the debtors.
 2. Original loan amounts.
 3. Default balances.
 4. Individual and group balances for group loans.
 5. Quota amounts.
 6. Frequency of payments.
 7. Loan term.
 8. Loan type.
 9. Refinanced loans (change in original loan conditions due to payment difficulties).
 10. Guarantees.
 11. Name of the guarantee.
 12. Criminal proceedings.

▾ EXECUTIVE SUMMARY

In terms of accuracy and data adequacy, the Colombian microfinance sector is strong. However, much remains to be done in order to have an excellent credit reporting system. The system is still weak in numbers and types of institutions reporting to credit bureaus. Furthermore, the absence of a public credit registry means that there is substantial dissemination of data among the credit bureaus.

The absence of a public credit registry limits the depth of credit risk analysis in Colombia. This problem is exacerbated because regulated institutions are not required to report to all credit bureaus (only to one). Therefore, data from regulated and non-regulated institutions is scattered among different bureaus. Additionally, there is little reporting done by public institutions and private loan providers.

One of the biggest challenges is to improve the timeliness of data. Despite the efforts made by some institutions to report data more frequently, there is still a large data gap caused by those that report monthly.

Regulations are clear and balanced for the consumer and reporting institutions alike. The service provided is good and the prices are similar to the average of the other countries studied.



UNDERSTANDING THE COLOMBIAN MICROFINANCE SECTOR IN RELATION TO THE PUBLIC CREDIT REGISTRY AND CREDIT BUREAUS

Colombia has a moderately developed microfinance system. Despite the existence of specialized banks, there is no specialized legal framework to regulate microfinance institutions, though efforts are being made to develop specialized regulations. In the meantime, large NGOs are becoming banks and following regulation that is not aligned to its microcredit activity.

There is a ceiling on lending interest rates (usury rate), which is set monthly by the government. This effective rate (along with the allowed commissions), reached 50.2% in Dec.-11 (39.9% in Dec.-10).

Asomicrofinanzas is a network of 30 regulated and non-regulated MFIs (banks, financial corporations, NGOs, and cooperatives). According to statistics from the network, 26% of Colombia's microcredit portfolio corresponds to the State Bank Banagrario. Next in size are the NGO FMM Popayán (14.1%), and the banks Bancamia (18.6%) and WWB (8.9%). The latter three are pioneers of microcredit in Colombia.

There is no public credit registry in Colombia and there are three credit bureaus: Datacrédito, of Experian Computec, headquartered in London; CIFIN of the Colombian Association of Banks (Asobancaria); and Procrédito of the National Merchant Federation (Fenalco).

Microfinance institutions report financial data directly to credit bureaus, however they are not required to report to all bureaus. Therefore, all bureaus do not contain all of the data from the regulated system, like in Peru, where the public credit registry provides all of the regulated financial system's data to the credit bureaus.

Credit bureaus consolidate data from the regulated and non-regulated financial systems, as well as the non-financial sector, though only of the clients who choose to report to them.

There is strict legislation on data and consumer protection. Institutions must request the debtor's authorization in order to report their negative information (*See the Glossary*) to credit bureaus.

The 30 MFIs of Asomicrofinanzas report to at least one of the credit bureaus. However, there are many credit providers from the low-income segment of the population that are not included (both MFIs and Cooperatives). They are estimated at approximately 300, but there are no official records to confirm this.

ALIGNMENT OF THE COLOMBIAN MICROFINANCE SECTOR TO THE WORLD BANK'S GENERAL PRINCIPLES FOR CREDIT REPORTING

Drawing from the General Principles for Credit Reporting published by the World Bank in September 2011, the diagnosis of the Colombian Microfinance sector is as follows:

General Principle 1: Data *(See definition in Annex 3)*

↘ **Guidelines on accuracy of data**

In general, the accuracy of the data submitted by the credit bureaus is good¹⁴. Although there is no public credit registry, resulting in institutions having to report individually to credit bureaus, the risk of errors is mitigated by providing 20 days' notice to debtors in arrears that they will be reported. This allows the debtor to request the correction of any errors before their information is made public.

Another mechanism that reduces the number of errors is data protection regulation. These regulations include penalties for non-compliance.

The formats designed to collect information are easy for MFIs to fill out. Credit bureaus have reliable validation systems. The few cases of error stem primarily from the inconsistencies in the national identification system.

It should be noted that the data from the government agency that manages personal identification is difficult for the credit bureaus to access, limiting data accuracy.

↘ **Guidelines on timeliness of data**

Despite efforts to improve data timeliness, the level needed by the microfinance sector has not yet been reached.

MFIs must notify debtors 20 days prior to their arrears being published *(See Guidelines on accuracy of data)*. This is a good measure in pressuring debtors to pay, but it reduces the data's timeliness.

Credit bureaus mostly receive data on a monthly basis. Some institutions report loan disbursements and payments more frequently (generally twice a month).

The institutions that send information to credit bureaus monthly do so on average 20 days after the close of the month, creating an information gap of about 50 days. For example, up until the 20th of May, the available data was dated March 21, 2012. The lack of data timeliness is a large risk considering that borrowers have fast access to small loans from various MFIs without providing collateral.

This information gap is partly covered by the "loan request footprint," a record of debtors' applications for loans at other institutions. These are important alerts sent to MFIs.

¹⁴ See "Scale" in the Glossary.

Of the analyzed countries, Brazil is a good example of data timeliness. In Brazil, negative data is reported online daily, making strong use of the country's technology. Brazil also sends debtor notifications, but they are only 10 days prior to releasing data, which favors greater timeliness.

↘ **Guidelines on sufficient data – including positive**

Data sufficiency in credit bureaus is good. However, there is still information that should be included to improve credit analysis.

Positive information is reported, meaning that all of the debtor's information is published, whether they make timely or late payments. Loan amounts are reported from one Colombian Peso (approximately US\$0.50), which puts the data of even small debtors at the disposition of MFIs.

Following legal standards, Colombia is one of the few countries in this study that shows full minimum¹⁵ data compared to other countries. For example, they report data such as original loan amount, monthly quotas to be paid per loan, amount in arrears, loan term, collateral, and guarantors.

However it would be useful to have the following additional information to improve credit analysis:

1. Methodology type (group or individual).
2. Group balance based on group loans (only the individual balance is reported).
3. Criminal proceedings.
4. Basic utility company information, such as water and electricity.
5. Tax debt.
6. In general, more information from the non-financial sector.

↘ **Guidelines on collection of data on a systematic basis from all relevant and available sources**

Data collection in Colombia is moderate. This is because there is neither a public credit registry nor a requirement for the regulated system to report to all bureaus. Also, there is low participation from private and public institutions with relevant data.

Since there is no public credit registry, regulated financial institutions are legally obligated to report directly to at least one credit bureau. Consequently, no credit bureau has data from the entire regulated financial system.

The effort made by the network Asomicrofinanzas to encourage its members (30 regulated and non-regulated MFIs) to sign a code of ethics is noteworthy. This code includes the commitment to report data to at least one of the country's credit bureaus.

It is estimated that a large number of loan providers from the low-income sector of the population do not report. Datacrédito is the bureau that has made the most efforts to incorporate a larger number of MFIs as reporting institutions.

Despite these efforts, credit reports still lack important data from public institutions, like basic water and electric services, criminal processes, tax information, etc., because there is no public institution that manages this data. Some of these institutions charge high rates in order to access their data, which makes it difficult to get information about their services.

Other limitations are related to the low capability of the public institutions' computer systems.

¹⁵ Using the World Bank's General Principles for Credit Reporting, published in September 2011.

Annex 1 **Colombia**

There are also credit providers from the non-financial sector that do not report to credit bureaus for fear of losing their debtors.

↘ **Guidelines on retention of data**

Data retention in credit bureaus is good, although relatively excessive for unpaid debts. This debt is retained in the credit system for 14 years, 10 years plus a 4 year penalty, which is a relatively long time to be able to reinsert the debtor into the financial system.

The data regarding debts paid on time is kept indefinitely. Data on debt that is paid late is kept for twice the amount of time that it was late, up to four years. This term is less than the average of other countries (5 years). However, the staggering of penalties is good because it punishes the debtor that is further behind in payments..

General Principle 2: **Data Processing: Security and Efficiency** *(See definition in Annex 3)*

↘ **Guideline on security measures**

Credit report data security measures within the Colombian microfinance sector are moderate because the sector is largely unregulated.

For regulated MFIs there are strict data security measures mandated by the supervisory body. Credit bureaus are supervised by the Industry and Commerce Superintendence, which regulates and protects consumer data. In general bureaus are careful to follow safety regulations since data is the most important asset of its business.

Given their nature, MFIs do not have data security monitoring. This is a large void considering that there are more MFIs than regulated institutions.

This risk is mitigated by credit bureau service contracts, which set minimum data quality and continuity requirements. Strict compliance of these contracts is enforced to protect data accuracy. However, some of these institutions still have technological limitations and lack trained personnel.

↘ **Guideline on reliability**

Credit bureau service in Colombia is reliable. In general, the service is continuous. Good internet connections, mainly in urban areas, and security and quality measures, allow for this level of service.

↘ **Guideline on efficiency**

Credit bureau service is good and prices in Colombia are similar to the average of the other countries studied.

The most common channel offered to access credit reports is online through the credit bureau's website. The price per consultation is estimated at US\$1. Credit bureaus incur high costs from collecting information from various sources nationwide because there is no public credit registry that provides data from the regulated system for free, as is the case in most of the analyzed countries.

Datacrédito has been providing important information to the microfinance sector, including alerts regarding the evolution of the debtor's risk, which have been of great use. Colombia does not yet produce a score similar to other countries.

General Principle 3: **Governance and Risk Management** *(See definition in Annex 3)*

↘ **Guideline on accountability of governance arrangements**

The country's credit bureaus respond acceptably to third parties. The Industry and Commerce Superintendence supervises credit bureaus and Datacrédito also reports to its headquarters abroad.

All of this promotes responsibility in business management, as well as data and consumer protection.

↘ **Guideline on transparency of governance arrangements**

Colombian credit bureaus' business transparency is good. However, data regarding their shareholder composition is not published.

Generally, credit bureaus describe their business, products, and consumer claims system on their webpage. However, they do not publish data regarding their shareholder composition, limiting transparency.

The law does not prohibit financial institutions from owning shares in credit bureaus. Because of this, the Associations of Banks owns the bureau CIFIN.

↘ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

Credit bureaus follow risk management standards set by the Industry and Commerce Superintendence. Datacrédito also follows the risk management standards of its headquarters in London, which mitigates business risk.

↘ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

All users have the same right to access credit bureau data.

Although the credit bureau CIFIN is owned by the Association of Banks, there appear to be no conflicts of interest..

General Principle 4: **Legal and Regulatory Environment** *(See definition in Annex 3)*

↘ **Guidelines on clarity and predictability**

In Colombia there are many laws related to credit bureaus. The regulations and the consequences for noncompliance are clear, although through the interviews it was concluded that there have been few efforts made by the authorities to disseminate the regulations to consumers.

Although initial outreach efforts were made, they have not been continuous through means effective in reaching consumers. The dissemination is done through a website, which is not frequently utilized by consumers. In microfinance, the dissemination is performed by credit officers who inform the debtor of their rights and obligations.

Of the analyzed countries, Peru is a good example of dissemination; various measures visible to customers are used, such as videos and posters in the offices, as well as through mass media: radio, TV, etc.

↘ **Guidelines on non- discrimination**

In general, Colombia's credit bureau and consumer protection standards establish that there should be no discrimination. All reporting institutions and credit bureau users have the same rights to report and access data.

The reciprocity principle, where only those institutions that report have access to consultations, is used in Colombia.

↘ **Guidelines on proportionality**

The current regulations include proportionality and balance. All members of the credit reporting system can comply with the standards and the penalties imposed by the authorities for noncompliance are reasonable.

↘ **Guidelines on consumer rights and data protection**

In Colombia there is sufficient data and consumer rights protection legislation. The standards include debtor's minimum rights, such as: to be informed of the purpose as to why their data is being collected, processed, and distributed, as well as to have periodic access to their data, and to be able to make claims.

Habeas Data Law requires the debtor's authorization to report their negative data to credit bureaus.

↘ **Guidelines on dispute resolution**

Both the regulated and non-regulated systems have the necessary mechanisms to resolve debtor's claims.

Because supervisory bodies are strict with regulation compliance, MFIs are diligent in processing claims within the allotted time limits.

CONCLUSIONS

This section organizes the conclusions based on the principles outlined in the body of this report:

General Principle 1: Data

- ▶ The accuracy of the data provided by credit bureaus is good; consequently the number of claims submitted for data inaccuracy is low.
- ▶ Despite efforts to achieve greater data timeliness, Colombia has not achieved the timeliness required by the microfinance sector.
- ▶ Credit bureaus attain the minimum requirements for information, though there is still data that should be included to improve credit analysis.
- ▶ Data collection is moderate because there is no public credit registry and it is not mandatory for the regulated system to report to all bureaus (it is only required that they report to one). Also, there is low participation from private and public entities with relevant data.
- ▶ Data retention in credit bureaus is good, albeit a bit excessive for unpaid debts and relatively short for the history of canceled debts.

General Principle 2: Data Processing: Security and Efficiency

- ▶ Data security measures of the Colombian microfinance credit reporting system are moderate because the sector is largely unregulated.
- ▶ The Colombian credit bureau system is trusted.
- ▶ Credit bureau service is good and prices are similar to the average of the other countries in this study.

General Principle 3: Governance and Risk Management

- ▶ The country's credit bureaus respond acceptably to third parties.
- ▶ Credit bureaus' transparency is good, however they do not publish information regarding their shareholder composition.
- ▶ Credit bureaus abide by the risk management standards set by the Industry and Commerce Superintendence.
- ▶ All users have the same right to access credit bureau data. Although the Association of Banks owns credit bureau CIFIN, there appear to be no conflicts of interest.

Principio general 4: Legal and Regulatory Environment

- ▶ Colombia has various legal regulations regarding credit bureaus. These regulations and the penalties for non-compliance are clear, although the authorities' efforts to disseminate this information have been minimal.
- ▶ All reporting institutions and users of credit bureaus have the same rights to report and use the data.
- ▶ The current regulations are balanced and proportional.
- ▶ There are adequate data protection and consumer rights regulations.
- ▶ Regulated and non-regulated systems have legal mechanisms to meet the debtor's claims and have complied well in resolving them.

RECOMMENDATIONS

This section classifies recommendations according to their type:

Legal

- ▶ To improve data timeliness, it is recommended that debtor's arrears notice be eliminated or reduced. Within the study, Colombia and Brazil are the only countries that have these notifications, 20 and 10 days respectively.
- ▶ Extend the retention of cancelled late loans from four years to five.

Regulatory

- ▶ To improve transparency, credit bureaus should publish their shareholder composition.
- ▶ Establish mechanisms to mitigate the conflicts of interest that can arise from financial institutions being shareholders or owners of credit bureaus.

Techniques and Training

- ▶ Providing technological resources to the financial system that would allow for the daily updating of information would be a modest investment compared to the positive impact that it would have on the healthy development of microfinance.
- ▶ Motivate small MFIs to increase reporting to credit bureaus. Support could be in the form of training, support during a period of free consultation services, special portfolio reports that demonstrate the benefits obtained from the trial period, technical support with the formats required by credit bureaus, etc.
- ▶ Motivate public institutions to share data with credit bureaus at a reasonable cost, thus benefiting the country's credit system.
- ▶ Motivate the country's MFI's to sign Asomicrofinanzas' code of ethics, consequently committing them to report to credit bureaus.

- ▶ Motivate non-regulated MFIs to follow regulations similar to those of the microfinance sector regarding data security and microfinance business risk management.
- ▶ Motivate the implementation of contracts between MFIs and credit bureaus to elevate the number of consultations and reduce the cost.
- ▶ More widespread dissemination of regulations to consumers in order to improve the knowledge and understanding of credit reporting standards.
- ▶ In order to improve credit analysis, it would be
 1. Methodology type (group or individual).
 2. Balance of the group debt for group loans (only individual balances appear).
 3. Criminal proceedings.
 4. Data from public service companies, such as water and electricity.
 5. Tax debt.
 6. In general, more information from the public and non-financial sectors.

▾ EXECUTIVE SUMMARY

Credit Bureaus in El Salvador have managed to include the largest non-regulated MFIs, but there are still many small ones that do not report. Overall, the Salvadoran microfinance sector has a long way to go to have an excellent credit reporting system, given the data insufficiency caused by the regulatory framework's limitations.

Due to legal restrictions, the non-regulated financial system cannot access information from the regulated system, but the regulated system can access information from the non-regulated system. This implies a discriminatory treatment that harms the microfinance sector's credit analysis, increasing the sector's over-indebtedness risk.

There is a public credit registry that does not provide the regulated system's information to credit bureaus. Furthermore, it is not obligatory for the financial system to report to credit bureaus and share positive information. This exacerbates the credit bureaus' data insufficiency.

Loan providers from the non-financial sector report, though only moderately. The public sector with relevant information also reports only minimally, due to legal constraints.

Moreover, data is upgraded monthly, far behind the record set by Brazil for daily updating negative information.

The recent regulatory framework covers data and consumer protection. However, there is imbalance between the debtor and MFIs, establishing a short data retention period of three years for canceled debts.



UNDERSTANDING THE SALVADORAN MICROFINANCE SECTOR IN RELATION TO THE PUBLIC CREDIT REGISTRY AND CREDIT BUREAUS

The Salvadoran Microfinance sector is competitive, but largely cooperative and unregulated. It is estimated that there are more than 350 loan providers to the low-income segment of the population. Most are cooperatives that offer consumer credit.

There are few universal banks engaged in the microfinance sector, only Procredit and Banco Azteca. Furthermore, there are seven cooperative banks (with variable capital) and three savings and loan societies (with fixed private capital), all regulated.

Non-regulated loan providers are grouped into federations and unions such as, Fedecredito¹⁶, Fedecaces¹⁷, Fedecrece¹⁸, and Asomi¹⁹. These unions somewhat make up for the lack of regulation by providing consulting and auditing services to their affiliates.

The microfinance sector was hit hard by the economic crisis in 2008 because the country's economy is heavily dependent on the United States. Therefore, the banking sector limited its services to the microfinance sector, providing an opportunity for MFIs.

El Salvador is a small country (with an approximate population of seven million people) and there is a belief that the high numbers of credit providers are over-lending. There is also a concern over the high rate of gang violence, as the gangs' extortions affect businesses.

A positive factor is the enforcement since October 2011 of the law: "Regulation of the Services and Information Regarding Peoples' Credit History." This law seeks to protect consumer rights, defining credit report data and the customer claims processes. It also regulates the registration and regulation of credit bureaus by the supervisory body (Financial System Superintendence).

The law's regulations were approved in July 2012 and they are currently in the process of being implemented. Previously there were no regulations for credit bureaus and they applied their own policies to manage various aspects of the business.

A Consumer Protection Law, established in 2005, requires the debtor's approval in order to report or consult their information. There is also a governing body (Consumer Protection Ombudsman) that addresses users' claims from any sector.

There are four credit bureaus: Infored, Equifax, Transunion, and Procrédito. Infored specializes in microfinance and has shareholders within the microfinance sector, including Fedecaces, among others. It was formed to fill the gap left by Equifax, which focused only on the banking sector. Within the last few years, Equifax has been collecting information from debtors in the microfinance sector, obtaining good results.

¹⁶ Credit houses and worker's bank federation. As a federation and second tier funder, it is regulated, but its affiliates are not (approximately 40).

¹⁷ Federation of savings and loans cooperative associations of El Salvador.

¹⁸ Federation of cooperative savings and loans and related services associations.

¹⁹ Microfinance organizations' association.

Transunion was created over the last three years and is in the process of consolidating the number of reporting institutions. Procrédito is an important association of private loan providers that was formed in the 60s. It is trusted by its affiliates and shares positive information, which is not seen in other countries, where private companies only share negative information.

The public credit registry has been making good progress, but does not share data with credit bureaus.

ALIGNMENT OF THE SALVADORAN MICROFINANCE SECTOR TO THE WORLD BANK'S GENERAL PRINCIPLES FOR CREDIT REPORTING

Drawing from the General Principles for Credit Reporting published by the World Bank in September 2011, the diagnosis of the Salvadoran Microfinance sector is as follows:

General Principle 1: **Data** (*See definition in Annex 3*)

▾ **Guidelines on accuracy of data**

The accuracy of the data submitted by the public credit registry and the credit bureaus is good²⁰. MFIs report data with minimal errors.

The supervisory body manages the public credit registry where all regulated institutions from the microfinance sector report. The forms designed to collect information are extensive, but can be easily filled out by MFIs.

Regulated institutions voluntarily send their data to the credit bureau of their choice. Credit bureaus consolidate data from the regulated, non-regulated, and non-financial sectors. They have reliable validation systems and if there are inconsistencies, institutions are asked to correct them.

Errors are minimal, showing that reporting directly to credit bureaus does not threaten data accuracy, as is believed in other countries such as Bolivia and Peru.

On the other hand, the penalties in case of errors (*See Guidelines on clarity and predictability*) covered in the consumer protection law serve as a deterrent to prevent errors.

However, there are complaints relating to identity documents. Within the past few years, El Salvador has implemented a unique citizen identification system, which is apparently working well. However, they are still clarifying the relationship of the previous identification numbers with the new ones.

²⁰ See "Scale" in the Glossary.

↘ Guidelines on timeliness of data

Data from the public credit registry and credit bureaus are not timely enough for users.

Data is updated monthly. The public credit registry and credit bureaus complete the financial sector's data on average 20 days after the close of the month. This generates an information gap of about 50 days. For example up until May 20th, the available information was dated March 2012.

The lack of data timeliness is a large risk considering that borrowers have fast access to small loans without collateral from various MFIs. One reason is the technological system's limitations in collecting and transmitting data more frequently.

This information gap is covered by credit bureaus by providing MFIs with the debtor's "loan request footprint," the number of times that the debtor has attempted to get loans from other institutions.

Of the studied countries, Brazil is a good example of data timeliness, where negative information is reported online daily through updated technology.

↘ Guidelines on sufficient data – including positive

Data sufficiency for the regulated financial sector is good, but for the non-regulated financial sector and the non-financial sector, it is not good because of legal restrictions.

The Banking Law requires that regulated financial institutions have access to both the public credit registry and to all credit bureaus' data. Non-regulated financial institutions and the non-financial sector do not have access to credit bureaus' regulated financial system data. They can only see written-off loans or very poor ratings.

Of the studied countries, El Salvador is the only country with this situation, increasing the microfinance sector's credit risk.

Although regulated financial institutions must report positive information to the public credit registry they are free to send only negative information to credit bureaus. The non-regulated financial system and the non-financial system have the same freedom. Only 8% of reporting institutions share positive information, affecting credit bureaus' data sufficiency.

An exception is the credit bureau Procrédito. This bureau is comprised mainly of companies from the non-financial sector and shares positive information, which has not been seen in other countries.

A positive factor of the Salvadoran credit reporting system is that loans are reported in from 1 U.S. dollar (local currency), making data of even the smallest debtors available to MFIs.

Salvadoran credit bureaus complete the minimum data required by the World Bank's General Principles for Credit Reporting. The data regarding exact days in arrears goes beyond the minimum standards, as arrears are usually presented as range of days past due. However, the latest law regarding credit bureaus restricted access to addresses and telephone numbers. This represents less data for institutions considering the debtor's frequent address and telephone number changes in the microfinance sector.

In general, it would be useful to have the following additional data in credit bureaus to improve credit risk analysis:

1. Address
2. Telephone number
3. Criminal proceedings (legally restricted)

4. Basic utility company data, such as water and electricity.
5. Tax debt (legally restricted)
6. More information from the non-financial and public sectors
7. Chambers of Commerce data

↘ **Guidelines on collection of data on a systematic basis from all relevant and available sources**

The collection of data from loan providers to the population's low-income segment is moderate. Approximately 50% of them report to credit bureaus. Further, there is moderate data collection from private entities and minimal participation from public entities with relevant information.

Despite the absence of a legal obligation for non-regulated MFIs and cooperatives to report, there is significant participation from the largest of these institutions, in large part due to their unionization. The affiliate members of Fedecaces, Fedecredito and Asomi generally report and consult credit bureaus. It is estimated that there are many credit providers to the low-income segment of the population that do not report, however they are so small that in some cases they do not have an information system.

The efforts made by credit bureaus over the last few years to promote the participation of non-regulated loan providers (more numerous in El Salvador than regulated providers) are noteworthy. The Supervisory body's recent authorization for the 55 affiliates of Fedecredito to access data from the public credit registry is also positive.

Infored was created to serve the microfinance sector, initially not served by Equifax. Therefore, its users are mainly MFIs and very few banks. In contrast, many banks report to Equifax and not to Infored. Complementarily, Procredito provides debtor data regarding loans for goods and services (non-financial sector), which is especially important for MFIs that finance debtor's productive activities.

The dissemination of data among the three credit bureaus causes regulated MFIs to have to consult at least two of the credit bureaus to gather a more complete credit history, increase operating costs.

All credit bureaus lack important data from public institutions, such as criminal proceedings and tax debts, which are legally restricted

↘ **Guidelines on retention of data**

Data retention in the public credit registry is good, though not in credit bureaus. The public credit registry retains credit history indefinitely. However, canceled debt is only retained for three years in the credit bureaus' reports. This period is too short to analyze the debtor's payment behavior.

It should be noted that prior to the enactment of the credit bureau law (April 2012), credit bureaus only retained canceled debt information of the regulated financial system for six months, an extremely short period of time. Among the analyzed countries, the accepted data retention period for canceled debt is five years.

General Principle 2: Data Processing: Security and Efficiency

(See definition in Annex 3)

↘ Guideline on security measures

Data security measures of the Salvadoran microfinance sector's reporting system are moderate; this is mostly because it is mostly unregulated.

Regulated MFIs have strict data security measures established by the supervisory body. Additionally, the recent law established credit bureau regulations. Therefore, it is expected that that data security measures will be required in the future.

Given their nature, unregulated MFIs do not have data security measures required by an external body. This forms a large gap considering that they are far greater in number than the regulated institutions. Some of the unregulated MFIs still have computer system limitations and limited numbers of specialized personnel.

↘ Guideline on reliability

In El Salvador, both the public credit registry and credit bureaus are trusted and reliable. Service is generally continuous, as there are only minimal interruptions caused by Internet or power outages.

↘ Guideline on efficiency

Overall, efficiency is moderate. The service provided by the credit bureaus is good but prices are the highest seen of the studied countries.

The channel most often offered for accessing credit reports is online through the bureaus' websites.

The products offered are similar to other countries, including alerts, scores and loan prequalification. However, the range of services the non-regulated sector can offer is limited since it cannot access information from the regulated system.

The price per consultation is high in comparison to the average price of the studied countries (US\$1). The price difference between the three bureaus is also important. For Equifax, the range is approximately US\$2.50-US\$5 per consultation; Infored is US\$0.70-US\$2.30; and Procrédito is less than US\$0.70. This is presumably caused by Equifax's higher number of reporting institutions, which implies higher operating costs for data collection.

Equifax and Infored's offer of credit reports with different levels of information (basic, intermediate, and complete) and prices is positive, as it allows MFIs to choose the information that they need and a price based on their ability to pay.

Equifax has been creating agreements with unions of credit providers in order to offer better prices and to increase the number of consultations.

On the other hand, the public credit registry's services are free for regulated institutions.

General Principle 3: Governance and Risk Management (See definition in Annex 3)

▾ **Guideline on accountability of governance arrangements**

Given the recent law for credit bureaus, registration and control standards for these institutions are being created by the supervisory body. This will promote greater responsibility in business management and data and consumer protection.

▾ **Guideline on transparency of governance arrangements**

Credit bureau transparency is moderate. Not all of them publish information regarding their services, data usage, nor shareholder composition for primary owners.

The law does not prohibit financial institutions from owning shares in credit bureaus. Therefore, some cooperatives and MFI federations are shareholders of Infored, with a maximum of 20% of the shares. A bank also holds a minority share of Equifax.

▾ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

The supervisory entity's recent regulation regarding the credit bureaus will reduce the bureaus' risks.

▾ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

According to the credit bureaus, all users have the same right to access data. However, restrictions stem from the country's regulatory framework (See *Guidelines on non-discrimination*).

There appear to be no conflicts of interest based on ownership even though both bureaus have shareholders in the regulated and non-regulated financial systems (see *Context*).

General Principle 4: Legal and Regulatory Environment (See definition in Annex 3)

▾ **Guidelines on clarity and predictability**

In El Salvador there is a law regarding credit bureaus but it is fairly new. Therefore, there are still issues that need to be regulated and interpreted by the supervisory body. The consequences for failure to comply with these regulations are expected.

Few efforts have been made by the authorities to inform citizens of their rights. However, authorities have disseminated information regarding other financial topics, for example the use of credit cards.

Of the analyzed countries, Peru is a good example of dissemination; various measures visible to customers are used, such as videos, posters, and mass media: radio, TV, etc.

↘ **Guidelines on non- discrimination**

In credit bureaus there is discrimination against non-regulated loan providers; according to the banking law they are not permitted to access data from the regulated financial system.

This situation does not respect a balance of rights, as regulated institutions have access to information from the regulated and non-regulated financial systems as well as from the non-financial sector.

The lack of information for the non-regulated financial and non-financial sectors does not allow for a comprehensive analysis of the debtor, increasing the risk of borrower's over-indebtedness, particularly considering that there are far more unregulated loan providers than regulated. This also violates the reciprocity principle, decreasing trust in the credit reporting system.

↘ **Guidelines on proportionality**

In the country's current regulations there are moderate proportionality and balance.

The regulations can easily be complied with by all members of the credit reporting system, and the penalties imposed by the authorities for failure to adhere to these standards are reasonable.

However, limiting data retention of canceled debt to three years overprotects the debtors and is a disadvantage to financial institutions because it erases one of the most important data points for credit analysis, the debtor's payment behavior. Also, the removal of addresses and telephone numbers has subtracted two important elements in locating the debtor.

↘ **Guidelines on consumer rights and data protection**

The new credit bureau law covers legal gaps of data and consumer protection, but in some cases overprotects the debtor (*See Guidelines on proportionality*).

The regulations include minimal debtor rights, such as: being informed as to why their data is being collected, processed and distributed, as well as periodic access to their information and the ability to make claims.

Banking privacy has always existed for borrowing and lending. Consequently, the debtor's authorization is needed to report and consult their information.

Quarterly audits performed by Equifax help to maintain banking privacy. In these audits, reporting institutions are required to show the debtor's signed authorization with the goal of maintaining trust in the credit reporting system.

↘ **Guidelines on dispute resolution**

The recent loan data protection law has strengthened the claims mechanisms that up until now had been working in an acceptable manner. It will take time to implement the new regulation and measure its effectiveness.

Annex 1 **El Salvador**

For now, within the regulated system it is required that each institution have a customer claims department. Furthermore, the customer can approach the customer protection department of the supervisory body, the credit bureau, or the government's consumer protection agency²¹. This agency handles claims from all economic sectors. Despite some delays, claims presented before this agency are resolved and customers are protected.

To make things easier for the debtor, the law set the requirement that credit bureaus must have offices in at least each of the three geographic areas in the country.

There are also various ways to make claims in the non-regulated system. Users can go to the financial institution where the error occurred, directly to the credit bureaus, or to the government's consumer protection agency.

²¹ Consumer Protection Ombudsman.

CONCLUSIONS

This section organizes the conclusions based on the principles outlined in the body of this report:

General Principle 1: Data

- ▶ The public credit registry and credit bureaus' data accuracy is good. MFIs have been reporting with minimal errors.
- ▶ The data of the public the credit registry and credit bureaus is not timely. Data updates are usually monthly, causing a data gap of about 50 days.
- ▶ There are technological limitations with both regulated and non-regulated institutions that negatively affect the timeliness of data.
- ▶ Data accuracy for the regulated financial sector is good, but due to legal restrictions it is not good for the non-regulated financial and non-financial sectors. Non-regulated financial institutions and the non-financial sector do not have access to data from the regulated financial system.
- ▶ Data collection by loan providers to the low-income segment of the population is moderate. Approximately 50% of them report to credit bureaus. There is also moderate data collection from private entities and minimal participation from public entities with relevant information.
- ▶ Data retention in the public registry is good, though not in credit bureaus. Three years for canceled debt is too short of a period to analyze debtors' payment behavior.

General Principle 2: Data Processing: Security and Efficiency

- ▶ Data security measures for the microfinance sector's credit reporting system are moderate because it is mostly unregulated.
- ▶ The country trusts the services of the public credit registry and credit bureaus.
- ▶ Overall efficiency is moderate. Despite the good services provided by credit bureaus, prices are the highest seen in the studied countries.

General Principle 3: Governance and Risk Management

- ▶ Given the recent credit bureaus law, the supervisory body is still in the process of developing registration and control regulations.
- ▶ Credit bureaus' transparency regarding their business is moderate. They do not generally publish information about their services, data usage, or shareholder composition.
- ▶ The recent regulation of credit bureaus by the supervisory body is positive, as it will reduce risks.
- ▶ According to the credit bureaus, all users should have the same rights to access their information, however, there are restrictions in the country's regulatory framework (*See Guidelines on non-discrimination*).

General Principle 4: Legal and Regulatory Environment

- ▶ El Salvador has a credit bureau law, but it is very recent. Therefore, there are still issues to be regulated and interpreted by the supervisory body. The penalties for failure to comply with these rules are expected.
- ▶ Credit bureaus discriminate against non-regulated MFIs and the non-financial sector since they do not have access to data from the regulated financial system, according to the Banking Law.
- ▶ The current standards are moderately proportional and balanced. However, limiting data retention of canceled debt to three years overprotects the debtor and fails to protect financial institutions.
- ▶ After many years of working on a credit bureau law, a law was recently passed that regulates bureaus and protects data and consumer rights. While it covers legal gaps, in some cases it overprotects the debtors (See Guidelines on proportionality).
- ▶ The recent law on loan data protection has strengthened the existing claims mechanisms that had been operating in an acceptable manner. The new regulations are very recent and it will take time to implement and measure their effectiveness.

RECOMMENDATIONS

This section outlines recommendations by categories.

Legal

- ▶ In order to improve data adequacy in the non-regulated financial system, it is recommended that all credit bureau users be granted access to data from the regulated system. This would allow for better services, products, and lower prices.
- ▶ Require all of the financial system, regulated and non-regulated, to share positive data.
- ▶ Motivate public institutions with relevant information, to share data with credit bureaus at a reasonable cost in order to benefit the country's credit system.
- ▶ Expand the retention of canceled data to five years to allow for an acceptable assessment of the debtor's historical payment history.

Regulatory

- ▶ To improve the timeliness of data, the supervisory body and credit bureaus should study the feasibility of increasing the frequency of data updates.
- ▶ Establish mechanisms to mitigate the conflicts of interest that could arise from financial institutions owning shares of credit bureaus.
- ▶ Regulate the obligation to adhere to the reciprocity principle in using and reporting data to credit bureaus.

- ▶ To improve credit bureau transparency, it is recommended to regulate credit bureaus' publication of their services, use of data, and their shareholder composition, among other topics of interest for users.

Government Policies

- ▶ Motivate loan providers of the non-financial sector to participate in credit bureaus and to contribute in improving the debtor's credit evaluation.
- ▶ Disseminate the rights and obligations of the consumer in relation to credit bureaus through effective public venues.

Techniques and Training

- ▶ Provide technological resources to the financial system that would allow for the daily updating of information would be a modest investment compared to the positive impact that it would have on the development of microfinance institutions.
- ▶ Motivate credit providers to the low-income segment of the population to join networks, which can support their strengthening and training on credit bureaus.
- ▶ Motivate non-regulated MFIs to follow regulations similar to those of the regulated sector regarding data security and general microfinance business risk management.
- ▶ Motivate the MFI networks to create contracts with the credit bureaus to increase the number of consultations and thereby reduce the cost.
- ▶ As much as possible, incorporate the following additional data into credit bureaus' credit reports:
 1. Address
 2. Telephone number
 3. Criminal proceedings (legally restricted)
 4. Data from public service companies, such as water and electricity
 5. Tax debt (legally restricted)
 6. More information from the public and non-financial sectors
 7. Chamber of Commerce information.

▾ EXECUTIVE SUMMARY

Guatemala's microfinance sector has a long way to go in order to have an excellent credit reporting system. The lack of microfinance, credit bureau, and consumer protection regulations has led to high distrust in credit bureaus and low MFI participation.

Most credit providers to the low-income sector of the population are small, non-regulated, and have minimal data security measures. This has resulted in a lack of data accuracy and timeliness.

The public credit registry does not share data with credit bureaus. Not requiring mandatory reporting to credit bureaus, even of regulated institutions, and the ability to decide on reporting negative or positive data, types of products, and data retention periods has led to data inadequacy.

The low participation of reporting institutions (including that of large Mexican actors such as Compartamos and Banco Azteca) has resulted in low scale of credit bureau operations, excessive flexibility, and the acceptance of low quality and untimely data from MFIs.

Banrural, the largest credit provider in the microfinance sector, has majority ownership in one of the credit bureaus, causing fears of unfair competition.

Lack of regulation regarding consumer protection strongly affects the debtor; there are no processes or entities to submit claims to regarding data inaccuracy and unjust retention periods.



UNDERSTANDING THE GUATEMALAN MICROFINANCE SECTOR IN RELATION TO THE PUBLIC CREDIT REGISTRY AND CREDIT BUREAUS

Despite the presence of large and old microfinance institutions, the microfinance sector in Guatemala is generally immature and unregulated, though increasingly competitive.

In the regulated sector there are banks that provide loans to the low-income population segment. The largest of which are Banrurual, Banco Antigua, Banco Industrial, Banco Azteca, G & T, and the Banco de los Trabajadores (Workers Bank), all with numerous offices in the country. In the non-regulated system there are also large actors such as Génesis Empresarial, Finca, Fundea, Raíz, and Compartamos, as well as many NGOs and cooperatives. The total is unknown, but they are estimated at approximately 300. Most institutions offer village banking loans.

New MFIs continue to emerge, creating a more difficult environment for existing MFIs. Guatemala has many geographic areas that are vulnerable to natural disasters, mainly heavy rains. There are 22 languages in the country and indigenous communities often have their own languages and customs, and also frequently govern themselves with their own laws. Furthermore, in urban areas there is a lot of extortion against citizens and micro-entrepreneurs, causing their migration to other cities or countries, deteriorating the financial institutions' portfolio quality.

Although there are many credit providers to the low-income segments of the population, most do not participate in networks. There are more than six networks that group these institutions (including cooperatives), all with few members and limited union activity. The network with the largest number of affiliates is REDIMIF,²² with 15 members mainly in rural areas. The networks form a larger network called CONAMIF²³.

There is no regulatory framework for microfinance institutions. In 2011, an inter-institutional²⁴ commission promoted the design of a law that would regulate unregulated microcredit providing institutions in order to create a strong microfinance sector. Currently, it is in the final stages of discussion before being approved by the relevant authorities and being pushed to Congress. The new government's desire to pass this law is positive.

There is a public credit registry managed by the regulatory body²⁵ but it does not share information with credit bureaus due to legal restrictions. There are three national credit bureaus, one local bureau (Coingua), and one bureau solely for cooperatives (Micoope). It is believed that there may be groups of MFIs that share data with among themselves.

Among the national credit bureaus are Transunion (headquartered in the United States) and Crediref²⁶ with majority participation from Banrural²⁷ and Infornet, S.A. of C.V. of Guatemalan private capital. The latter has offices in three Central American countries.

²² Guatemalan Network of Microfinance Institutions.

²³ National Council of Microfinance Institutions.

²⁴ Formed by the Bank of Guatemala, the Superintendence of Banks, and the Ministry of Economy, supported by the United States Department of Treasury.

²⁵ Bank Superintendence.

²⁶ Credit References Corporation.

²⁷ The network REDIMIF and the Cooperatives Federation are minority shareholders.

The big challenge facing MFIs is reducing the risk of over-indebtedness, which is difficult given that many MFIs do not report to credit bureaus. Even large actors such as Banco Azteca and Compartamos (from Mexico) do not report to credit bureaus; and Finca, though strong in village banking, only shares individual borrowers.

Because there is no credit bureau law, each bureau defines its own regulations, which do not always favor the debtor. In general, the financial consumer and other participants of the credit reporting system are not legally protected.

This has led to distrust in reporting to credit bureaus. Consequently, there is a growing over-indebtedness risk since loans are being disbursed without knowledge of the borrower's credit history.

GUATEMALAN MICROFINANCE SECTOR'S ALIGNMENT WITH THE WORLD BANK'S GENERAL PRINCIPLES FOR CREDIT REPORTING

Drawing from the General Principles for Credit Reporting published by the World Bank in September 2011, the diagnosis of the Guatemalan Microfinance sector is as follows:

General Principle 1: **Data** (See definition in Annex 3)

↘ **Guidelines on accuracy of data**

While the public credit registry provides relatively accurate data, there is strong doubt of the credit bureaus' data accuracy. One of the main causes is the insufficient security measures of some non-regulated MFIs, which are greater in number than the regulated microcredit providers (See *Guideline on security measures*).

Since the public credit registry does not share information with credit bureaus, financial institutions send information directly to credit bureaus. Credit bureaus perform validation processes, but are not strict in asking MFIs to correct errors for fear of delayed responses or of losing the client. Rather, they try to identify and correct errors themselves.

The inconsistencies that MFIs find when consulting borrowers are related to the accuracy of balances, court dates, or data presentation (See *Guidelines on timeliness of data*). Some debtors complain that they have paid their debts, while in credit reports they appear as unpaid.

Although credit bureaus perform validation processes, there are not enough safeguards for non-regulated MFI databases (See *Guidelines on security measures*). It is possible that weak IT systems do not identify inconsistencies in non-regulated MFIs and credit bureaus validation systems.

Some MFIs do not have a unique database for borrowers; instead they need to consolidate different databases from their agencies or products. Very small MFIs work with Excel and generally one administrative or accounting person prepares the data.

Within this context, some non-regulated MFIs do not fill out the credit bureaus' forms properly or completely. Also, because there is no credit bureau law, MFIs design their own criteria to present data and decide its retention. In an attempt to facilitate the filing of data, credit bureaus initially work with MFIs to facilitate the process.

Moreover, in some MFIs that serve the village banking sector in rural areas, the credit officers do not report payments the same day, causing a delay in the computer system. These MFIs do not manage cash counters; they use the services of banks, where the debtors – primarily those with village banking loans – cancel their debts. In some cases, updating the MFIs' balances takes a few days, which is why outdated balances are reported to credit bureaus at the end of the month.

Another cause of inaccuracy is the absence of legal penalties for MFIs that report errors (See Guidelines on consumer rights and data protection). In most of the countries studied in this report, a strict regulatory framework that penalizes errors has forced MFIs to submit correct information.

Only recently did Guatemala start a unique citizens national identification registry²⁸. Previously, each municipality issued IDs and much of the information was repeated. For example, the same person could have various identification numbers or the same number could corresponded to numerous people, depending on the town where they were born. Since the deadline to sign up for the national registry expires in January 2013, very few citizens have a unique identification, which affects data accuracy.

Meanwhile, the public credit registry has its own validation process that identifies errors with greater certainty. One of them is the intersection of the borrower's balance with the regulated institution's balance. If an inconsistency is identified, the report is sent to the reporting institution for correction and is not added to the database until it is corrected.

↘ **Guidelines on timeliness of data**

The timeliness of data is not good for users. The data gap is approximately 60 days, which significantly affects the borrower's credit risk analysis and generates user dissatisfaction with credit bureaus.

One of the reasons for these delays is some MFIs' lateness in submitting information to the credit bureaus, including a few cases of MFIs that submit data that is delayed up to six months. Some of the reasons for these delays are technological weaknesses (See *Guidelines on accuracy of data*), lack of pressure from credit bureaus, and the absence of a regulatory framework. Credit bureaus do not usually discontinue service to MFIs for fear of losing them as reporting institutions.

In contrast, in several of the other countries in this study, the regulations require the timely and accurate reporting of borrower data. Otherwise, the bureaus will discontinue service after two months of no reporting.

It is important to note that many MFIs offer village bank loans with weekly repayments. All bureaus update information monthly, meaning that there is a lag of up to four weeks of paid installments not reported to credit bureaus.

Of the studied countries, Brazil holds the record of daily reporting negative data, while Mexico updates most of its data weekly. This has proven to be a good practice in improving data timeliness.

²⁸ National Citizen Registry.

Annex 1 Guatemala

The process of updating credit bureau databases is slower in Guatemala than in other countries. While it takes two to three days to upload data in Guatemala, it takes approximately six hours in other Latin American bureaus. This conveys the need for more use of technology in the Guatemalan financial system, including credit bureaus and MFIs.

Credit bureaus make information available to MFIs approximately 30 days after the month's closing, totaling an average of 60 days without data updates. For example, until May 30th, the available information was dated March 31, 2012. The public credit registry is apparently faster since it has shorter deadlines to receive monthly data.

The lack of data timeliness limits the microfinance sector's credit analysis, though borrowers still have fast access to small loans, without collateral, from various MFIs.

The daily registration of a borrower's attempt to acquire credit from other financial institutions (loan request footprint) mitigates this risk. This information is immediately identified and is provided as an alert about the borrower's behavior during the information gap.

▾ Guidelines on sufficient data – including positive

Data sufficiency in credit bureaus is poor²⁹. Although the public credit registry publishes positive information (i.e. all of the borrower's data, whether they make timely payments or not), it is up to the financial institutions, according to the deals made with the credit bureaus, whether they publish positive or negative data. This is because financial institutions' (including regulated) reporting to credit bureaus is voluntary (*See Guidelines on collection of data on a systematic basis from all relevant and available sources*).

The length of arrears reporting to credit bureaus is also agreed upon (varying from 30, 60, 90, or 180 days past due), as is the type of products. Furthermore, some MFIs do not report certain data because they do not have it in their systems.

One factor that influences the decision to share positive or negative information is trust in the chosen credit bureau. There is a strong fear that credit bureaus will incorrectly use data. Some participants raised concerns that the lack of data security in credit bureaus will allow other credit providers to attain unauthorized data.

Another factor that discourages the sharing of positive data is the failure to adhere to the reciprocity principle, meaning that credit bureaus allow institutions that do not report to access data. In other cases they allow institutions that only report negative data to access positive data. In countries like Brazil, the reciprocity principle is one of the pillars of a strong system, where trust in reporting institutions is high and considered fair for all.

A motivational tactic in Guatemala that could be used is to determine the price of service based on the number of consultations and the amount of data provided to credit bureaus. This has been successful with Transunion, where most institutions provide positive data.

A positive factor is that loan balances are reported from one quetzal (approximately US\$0.13), which provides MFIs with data about even the smallest loans. However, credit bureaus do not publish data on collateral, adding to the credit analysis gap.

Some bureaus report balances of loans given in local currency in amounts equivalent in dollars. Furthermore, not all show the name of the financial institution, hindering the standardization of data.

²⁹ See "Scale" in the Glossary.

A positive aspect of some credit bureaus is the reporting of important data for the microfinance sector, for example, the quota amount and payment frequency, which is not common among other countries in this study.

Moreover, InforNet is the only one that publishes data on legal proceedings, which is public information. This provides a competitive advantage against other credit bureaus. Based on the interpretation of the Law on Public Access to Data of 2012, Transunion stopped reporting this type of data.

Considering that the majority of loans are group loans, it is important that Crediref directly publishes the borrower's individual balance and balances of the guarantors of these loans.

In general, it would be useful to have the following additional information to improve credit analysis:

1. Positive and complete data from all reporting MFIs.
2. Methodology type (group or individual).
3. Debtor rating (this is only reported in the public credit registry).
4. Collateral (this is only published in the public credit registry).
5. Basic utility company information, such as water and electricity.
6. Chamber of Commerce data.
7. More data from the non-financial sector.
8. Data from public institutions, such as tax debt.

▾ **Guidelines on collection of data on a systematic basis from all relevant and available sources**

Data collection in Guatemala is poor. The public credit registry does not share its data with credit bureaus. Few MFIs and not all banks report to credit bureaus, causing widespread data dissemination. Participation from the non-financial sector is moderate and nearly non-existent for the public sector.

The public credit registry collects data from regulated institutions and makes it available to them monthly, free of charge. Because of legal restrictions, this database is not sent to credit bureaus, as is done in Peru.

Most banks voluntarily report to the credit bureau of their choice. Banco Azteca, an important actor in the microfinance sector, does not report to credit bureaus. Each bureau receives data from only some institutions.

The data from non-regulated institutions that report is also dispersed among the three credit bureaus. Although Crediref is owned by the MFI network Redimif, not many of its affiliates report to them. Furthermore, Compartamos³⁰, one of the fastest growing credit providers in the country, does not report to any credit bureau.

In general many credit providers to the low-income segment of the population (including cooperatives) do not report to any credit bureaus. This presents a high risk because there are more unregulated MFIs than regulated institutions that serve the same niche. Though they do not take public deposits, the unregulated system could affect the regulated system if it does not control its credit risk.

³⁰ Mexican Bank not regulated in Guatemala.

Annex 1 Guatemala

MFIs fear losing borrowers and exposing their private information to uncontrolled risks. Consequently, the decision to not report or to report only negative information to credit bureaus is based on the perception of unreliability of credit bureaus (*See Guidelines on sufficient data - including positive*). Guatemala has the highest level of distrust out of the studied countries. It should be noted that Guatemalan participants (of this study) showed more trust in Transunion, which translated into it having more reporting institutions with positive information.

Some participants expressed fears in reporting to Crediref because Banrural is a majority shareholder. Banrural is the largest loan provider in the microfinance sector.

Although the price per consultation is similar to those in the studied countries (averaging US\$1.00), some reporting institutions believe that reporting is expensive, not only for the price of consultation, but also the investment necessary for the software and personnel needed to prepare the database before submission. Many small MFIs have weak IT systems (sometimes Excel spreadsheets), which lead to manual work with errors and a high cost for quality review.

Some unregulated MFIs dedicated to group loans do not consider reporting to credit bureaus to be important. These institutions believe that the borrowers know each other and are responsible to each other. Global experience invalidates this belief, since even in group methodology there is risk of over-indebtedness.

Furthermore, many MFIs are immature and are not regulated. Their boards and managers lack thorough knowledge of the microfinance sector's risks and of methodologies different from group methodology, leading to their ignoring the importance of credit bureaus. In this context, more training and alerts at the managerial and directive level are required.

It should be noted that when compared to other countries, the work of MFI networks in Guatemala has not been effective. In contrast, in Bolivia and Peru, their work has been successful in incorporating many non-regulated MFIs into credit bureaus. Another good example is the Colombian code of ethics where affiliates commit to report to at least one credit bureau.

It is possible that with the Microfinance Act under scrutiny (*See Context*), some MFIs (approximately ten) will be incorporated into the regulated system and will therefore be required to report to the public credit registry. This will somewhat reduce the over-indebtedness risk of the microfinance sector, as these MFIs would have access to data from the regulated system. However, many small MFIs (estimated at 140, not including cooperatives) would still not be reporting and it would be a challenge to incorporate them.

It remains difficult to include companies from the non-financial sector as reporting institutions because few report and those that do only offer negative data.

Public institutions that have relevant data also need to be included, such as the tax authority. It seems that there is still a lack of awareness in the public sector of the benefits of sharing such data.

Infonet has been collecting public data on lawsuits, somewhat covering this gap. Apparently, it is a legal challenge to collect this data; however, not updating debt balances poses a risk, possibly hurting the borrower, because this data remains in the database for ten years or until the borrowers requests its removal.

All bureaus are making efforts to include more MFIs into their user base, which has been difficult. Crediref, has prepared a software to donate to small MFIs to help them manage their operations and to report more easily. Other efforts include offering free services for a month or two, so that institutions experience the benefits of reporting.

▾ Guidelines on retention of data

Data retention in credit bureaus is poor because there are no laws on this topic; each bureau has its own internal policies. Transunion retains unpaid debt data for three years, Crediref shows all data indefinitely, and Infornet retains data for ten years, or until the borrower asks for their information to be corrected.

Also, each MFI makes its own decision regarding how long the debt is reported to credit bureaus. In some cases, the MFI makes an agreement with the credit bureau that reporting negative data from one month erases the data of the previous month, meaning removing the borrowers who have already paid. In other cases, they agree to retain an arrears footprint. Thus, some balances are up to date while others are from previous months.

Because there are no consumer protection regulations, there are no complaint mechanisms used by debtors regarding their data retention in credit bureaus.

The public credit registry retains unpaid debts indefinitely, but only shows on them credit reports for five years, which is reasonable.

General Principle 2: Data Processing: Security and Efficiency (See definition in Annex 3)

▾ Guideline on security measures

Data security measures in the credit reporting system of the Guatemalan microfinance sector are moderate, mainly because it is mostly unregulated.

Recently the supervisory body for regulated institutions implemented data security measures, including external auditory systems and business continuity plans in case of disasters.

Because credit bureaus are not supervised, there is strong distrust in the ways that they protect consumer information. Transunion mitigates risks with internal security regulations and audits from its headquarters in the United States.

The consequences for distrust in security measures are serious. Few reporting institutions submit positive data, which hurts the credit analysis of the entire financial sector.

Furthermore, given their nature, unregulated MFIs' data security regulations are not supervised. This creates a large gap considering that there are a lot more unregulated institutions than regulated. Contracting credit bureau services does not mitigate this risk since the bureaus are not demanding in terms of quality and continuity of data.

Due to the low number of reporting institutions in Guatemala, there is a risk of credit bureau sustainability if they discontinue service because of poor data quality. Credit bureaus even try to find solutions to the inconsistencies that they find, in order to avoid inconveniences and delays to the reporting institutions. In other countries credit registries and credit bureaus send inconsistencies back to the reporting institutions to correct. Usually if the amount of errors is high service is discontinued.

Annex 1 **Guatemala**

↘ **Guideline on reliability**

There is insufficient reliability of service in credit bureaus. In some cases there have been technical difficulties that do not permit access to some credit bureaus' websites, which shows the weakness of the IT systems. In other cases internet service and electricity have failed, mainly in rural areas.

↘ **Guideline on efficiency**

Service efficiency in Guatemala is moderate. The cost per consultation is acceptable, although, given the data insufficiencies, credit bureaus in Guatemala are unable to offer special services as bureaus in other countries in this study do.

The most common channel offered to access credit reports is via the credit bureau's website. Data can also be physically delivered.

Data insufficiency (See Guideline on sufficient data - including positive) and the reduced number of reporting institutions have limited the possibilities of creating special products, such as scores, monitoring, special portfolio analysis, etc. Transunion recently began offering a scoring service, however, it is too expensive for MFIs.

The price per consultation is within the average for the studied countries (US\$1.00). It should be noted that credit bureaus incur high costs for collecting data from various nationwide sources since public credit registries do not provide data from the regulated system to credit bureaus, as occurs in Peru. The low scale of credit bureaus' operations in Guatemala also increases the cost of consultation.

Despite the acceptable price, certain MFIs try to reduce costs by consulting only some high risk loans, which represents a gap in credit analysis.

Regulated institutions have free access to the public credit registry.

General Principle 3: **Governance and Risk Management** *(See definition in Annex 3)*

↘ **Guideline on accountability of governance arrangements**

Guatemala is one of the few countries in this study where credit bureaus are not supervised. Credit bureau responsibility to third parties is moderate.

The lack of responsibility to third parties is mitigated by self-regulation, including internal, external, and systematic audits, as well as reporting to headquarters abroad, as done by Transunion.

↘ **Guideline on transparency of governance arrangements**

Credit bureau transparency regarding its business is moderate.

Generally credit bureaus rely on their websites to describe their business and products. However, not publishing their shareholder composition limits transparency, generating distrust over unfair competition. This is particularly important in Guatemala, given MFIs' strong distrust of credit bureaus.

Because there is no regulatory framework for consumer claims on data errors, there is no clear guide for borrowers to follow in case there are errors.

↘ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

There are no regulations or supervision of business risks for credit bureaus.

↘ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

There are no regulations related to rights of access to credit bureau data.

In practice, there are no limitations to participating in credit bureaus, as MFIs decide where they report. However, there are concerns regarding Banrural's 50% ownership of Crediref. Banrural is the largest bank in the microfinance system and is semi-state property. The fact that this bank only reports to Crediref causes a large gap for the loan providers that participate in other credit bureaus.

General Principle 4:

Legal and Regulatory Environment *(See definition in Annex 3)*

↘ **Guidelines on clarity and predictability**

Guatemala does not have a credit bureau law and there is insufficient clarity regarding the few regulations on data protection. Dissemination efforts are minimal and therefore the consequences for non-compliance are unknown.

The lack of clarity over regulation on accessing public data *(See Context)* has impacted credit bureaus. Interpretation doubts caused Transunion to stop reporting data on lawsuits in 2010.

↘ **Guidelines on non-discrimination**

There are no non-discrimination laws in Guatemala, however, in practice there is discriminatory treatment because the reciprocity principle is not respected. Meaning, while some institutions are offered services only if they report data, other MFIs – because of their importance – are allowed to access data without reporting.

Low participation in credit bureaus has led to these measures being taken, in order to protect the bureaus' sustainability.

↘ **Guidelines on proportionality**

In the credit reporting system there is no proportionality or balance in the treatment of borrowers and MFIs. Because there are no laws regarding credit bureaus and consumer protection, financial institutions report the data that benefits their businesses *(See Guidelines on sufficient data - including positive)*. Citizens' rights are partially respected, as their permission is required to report and consult their data.

Annex 1 **Guatemala**

Credit bureaus have their own policies that in some cases can hurt the borrower's record, as can the data retention period (see data retention guide). Moreover, institutions are not penalized for errors, nor are borrowers compensated for the harm done to their credit history.

↘ **Guidelines on consumer rights and data protection**

Guatemala has few regulations regarding data and consumer rights protection. The participants of this study have the perception that even these few regulations are not met. Although there is a government agency that oversees consumer protection in all sectors, apparently it is not effective.

In 2010 a law that regulates access to public data was approved, from which some articles were taken that require borrower's authorization to report and consult their data.

↘ **Guidelines on dispute resolution**

Due to insufficient claims resolution regulations, each credit bureau adopts their own ways to resolve borrower claims. They receive claims from either the borrowers or from the financial institution. However, the credit bureaus only have one office in the capital, which does not help borrowers in the interior.

To cater to the regulated financial system's debtors, the supervisory body has a complaints unit; however, they only have two national offices, so filing is difficult for citizens from the interior.

CONCLUSIONS

This section organizes the conclusions based on the principles outlined in the body of this report:

General Principle 1: Data

- ▶ While the public credit registry provides reasonably accurate data, there is strong doubt about the credit bureaus' data accuracy. One reason is the insufficient data security measures of some unregulated MFIs, which are greater in number than the regulated financial institutions serving the same niche.
- ▶ Credit bureau data is not timely for enough for users. The data gap is of approximately 60 days, which significantly impacts the borrower's credit risk analysis and generates user dissatisfaction of credit bureaus.
- ▶ There are technological limitations in regulated and unregulated institutions, as well as in credit bureaus, that hinder data accuracy, timeliness, and sufficiency.
- ▶ Data adequacy in credit bureaus is weak. Reporting and defining data type is voluntary: positive or negative, types of products, and age of debt.
- ▶ Data collection is poor. The public credit registry does not share data with credit bureaus. Few MFIs and not all banks report to credit bureaus, which causes widespread dissemination of data. Participation from the non-financial sector is moderate and that of the public sector is almost inexistent.
- ▶ Data retention in credit bureaus is weak because there is no regulation; each bureau applies its own internal policies.

General Principle 2: Data Processing: Security and Efficiency

- ▶ Data security measures in Guatemala's credit reporting system are moderate since it is mostly unregulated.
- ▶ There is insufficient trust in credit bureau's services.
- ▶ Credit bureau services are moderate. The cost for consultation is acceptable, although because of data insufficiency, there are no specialized products offered as seen in other countries.

General Principle 3: Governance and Risk Management

- ▶ Guatemala is one of the few countries in this study where credit bureaus are not supervised. Credit bureau responsibility to third parties is moderate.
- ▶ Credit bureau transparency about its businesses is moderate, as they do not publish data regarding shareholder composition or user complaints.
- ▶ There is no regulation or supervision regarding credit bureaus' business risks.
- ▶ There are no established regulations related to rights for accessing credit bureau data. However, there are fears of conflicts of interest regarding Banrural's 50% ownership of Crediref.

General Principle 4: Legal and Regulatory Environment

- ▶ There is no credit bureau law in Guatemala and there is little clarity about the few existing regulations on data protection. Outreach efforts are minimal and therefore the consequences for non-compliance are unknown.
- ▶ There are no regulations protecting against discrimination. Discrimination is prevalent as the reciprocity principle is not respected.
- ▶ There is no proportionality or balance in the treatment of borrowers and MFIs in the credit reporting system. As there is no regulatory framework, credit bureaus and MFIs have their own policies that in many cases hurt the borrower's image.
- ▶ There are few regulations on data and consumer protection. Furthermore, participants of this study believe that the existing ones are not met.
- ▶ Because of the limited complaint resolution regulations, each credit bureau accepts various ways of resolving borrower claims; however, borrowers do not have the necessary resources to make them effective.

RECOMMENDATIONS

This section outlines recommendations by category.

Legal

- ▶ Accelerate the adoption of a microfinance law to strengthen the microfinance sector.
- ▶ Approve a credit bureau law to strengthen credit bureaus.
- ▶ Approve a data and consumer protection law.
- ▶ Establish mechanisms that mitigate the perception of conflicts of interest regarding banks' shareholder participation in credit bureaus in order to reduce distrust of credit bureaus' unfair competition.
- ▶ Require that credit bureaus respect the reciprocity principle to avoid the discrimination against reporting institutions by credit bureaus.
- ▶ Regulate the publishing of positive and negative data and of all products by regulated and non-regulated MFIs in at least one credit bureau to improve data sufficiency.
- ▶ Regulate the publishing of shareholder composition to improve credit bureau transparency.

Regulatory

- ▶ To improve data timeliness, it is recommended that the supervisory body study the feasibility of increasing the frequency of data updates.
- ▶ Clarify the scope of the Access to Public Data Law to define the legality of disclosing lawsuits and other public data to credit bureaus.

Políticas de gobierno

- ▶ Motivate public entities that have relevant data to share information with credit bureaus at a reasonable cost.
- ▶ Motivate credit providers of the non-financial sector to participate in credit bureaus to contribute to improving the evaluation of borrowers' credit.
- ▶ Motivate the effective participation of MFI networks in supporting the incorporation of more unregulated MFIs in credit bureaus.
- ▶ Disseminate consumer rights and obligations related to credit bureaus through effective public venues.
- ▶ Strengthen the public body that monitors compliance with consumer protection regulation. Penalties for errors should be effective, as should compensation for damage caused to the borrowers.
- ▶ Require MFIs that receive government funding or that benefit from training or other services to report to credit bureaus.
- ▶ It is recommended to create the necessary infrastructure to achieve trusted official records about the number of microfinance institutions in the country.

Techniques and Training

- ▶ Provide technological resources to the financial system that would allow for the updating of data daily would be a modest investment compared to the positive impact that it would have on the development of microfinance institutions.
- ▶ Provide more training to MFIs while stressing the benefits it brings to the financial system in order to improve the accuracy and timeliness of credit bureau data.
- ▶ It is recommended that credit bureaus incorporate stricter data quality and timeliness clauses into their contracts with MFIs (and enforce them) to improve accuracy and timeliness of data.
- ▶ While incorporating a larger number of MFIs into the regulated sector, it is recommended that networks motivate unregulated MFIs to follow the prudential regulations of the financial system on data quality control and risk management.
- ▶ In order to warn of the risk of over-indebtedness and to use credit bureaus to mitigate this risk, it is recommended that MFI networks more effectively train non-regulated MFIs.
- ▶ In order to improve credit risk analysis, it would be useful to include the following data in credit bureaus:
 1. Positive and complete data from all reporting MFIs.
 2. Methodology type (group or individual).
 3. Original loan amount.
 4. Credit term.
 5. Borrower rating (this is only reported in the public credit registry).
 6. Collateral (this is only reported in the public credit registry).
 7. Data from utility companies, such as water and electricity.
 8. Chamber of Commerce data.
 9. More data from credit providers from the non-financial sector.
 10. Data from public institutions, such as tax debts.

▾ EXECUTIVE SUMMARY

Despite progress in data timeliness, the credit reporting system in Mexico's microfinance sector has a moderately long path to follow before achieving an excellence.

Many unregulated credit providers for the low-income segment of the population do not report to credit bureaus³¹. Although in terms of asset size they represent a low percentage of the financial system, they may share borrowers with the regulated microfinance institutions and consequently would share the risks of not consulting the borrower's credit history.

There are also opportunities to improve data accuracy and sufficiency. Because of the microfinance sector's immaturity there are many small credit providers with IT and organizational weaknesses, affecting data accuracy. The lack of a reliable national identification document and precise home addresses contributes to the low data quality. This causes some MFIs to not meet the quality standards required by credit bureaus and, as a result, local bureaus where only MFIs report are being created.

The absence of a public credit registry means that there is no unique database for the regulated financial sector. Ownership of credit bureaus by large financial institutions that serve the same niche has caused fear of unfair competition.

Despite the clear and adequate credit bureau and consumer protection regulations, these are poorly disseminated. Furthermore, inadequate facilities for making complaints limit the consumer's ability to exercise their rights.



³¹ Because of the possible confusion caused by the credit bureau called "Credit Bureau", in this Annex on Mexico, the names of the Mexican credit bureaus are written in quotations.

UNDERSTANDING THE MEXICAN MICROFINANCE SECTOR IN RELATION TO THE PUBLIC CREDIT REGISTRY AND CREDIT BUREAUS

The Mexican microfinance sector has a large number of regulated institutions but is still immature. The lack of official data about the number of credit providers for the low-income segment of the population is a strong deficiency. The supervisory body³² estimates that in the total assets and number of borrowers, 75% of the sector will be regulated by the end of 2012. Currently there are four specialized banks, 43 SOFIPO³³, 69 credit companies (including banks and cooperatives) and 123 credit unions.

In the non-regulated microfinance sector, it is estimated that there is variety in credit providers, for example more than 3,000 SOFOM³⁴ and more than 6,000 pawn shops. Therefore, the microfinance sector based on the number and types of institutions is largely unregulated.

A few years ago, SOFOMs were created by a regulation that sought to remove institutions that use their own capital to grant loans from the regulatory body's scope because depositor and investor's money was not put at risk.

Growth was explosive and now it is unknown how many are in operation. The low equity required (approximately US\$4,000) encouraged private initiatives following the attractive profitability achieved by the sector. Many of them have managerial and executive teams that lack experience in the microfinance sector and others have been transformed from existing businesses. SOFOMs provide various types of loans but primarily offer microenterprise, consumer, and agricultural loans.

The level of competition is increasingly higher. Micronegocios Azteca, originating from Grupo Elektra, one of the largest regulated consumer credit providers, emerged providing group loans. It should be noted that group methodology and consumer credit comprise an important portion of the microfinance sector.

Mexico does not have a public credit registry but has three regulated credit bureaus: "Credit Circle," "TransUnion of Mexico," and "Dun & Bradstreet." The latter two operate under the name "Credit Bureau." This section uses "Credit Bureau" to refer to both.

With the explosive growth of the microfinance sector, "Credit Circle" emerged, seeking to cover data gaps in the microfinance sector created by "Credit Bureau." Today, both count on MFI data as an important part of their business.

Both bureaus have financial institutions as shareholders; "Credit Circle" has Grupo Elektra and Coppel, among other providers of consumer credit, and "Credit Bureau" has some banks and TransUnion, LLC as shareholders. This bureau, because of its longevity (1994), has a greater number of reporting banks.

The regulated non-banking sector has an additional supervisory body, with oversight delegated from federations and confederations, and regulations that are more flexible than banking regulations. Institutions must consult at least one credit bureau; however, there are many non-regulated credit providers that do not report, thereby increasing credit risk.

³² National Banking and Securities Commission (CNBV).

³³ Popular Finance Companies, regulated entities.

³⁴ Multiple Purpose Financial Companies.

Annex 1 **Mexico**

There are diverse MFI networks, such as ASOFOM³⁵, AMSOFIPO³⁶, and ProDesarrollo³⁷. These networks try to alleviate common problems, but they include few institutions from the existing total of MFIs.

With the creation of the unsupervised SOFOMs there is a risk that if the credit risk of the unregulated system is not controlled it could affect (for now on a small scale) the regulated system.

To mitigate this risk, the supervisory body is trying to become familiar with their operations, requiring unregulated SOFOMs to report operations through a money laundering prevention norm.

Also, in accordance to legal regulations, all savings banks need to regulate themselves this year.

MEXICAN MICROFINANCE SECTOR'S ALIGNMENT TO THE WORLD BANK'S GENERAL PRINCIPLES FOR CREDIT REPORTING

Drawing from the General Principles for Credit Reporting published by the World Bank in September 2011, the diagnosis of the Mexican microfinance sector is as follows:

General Principle 1: **Data** (*See definition in Annex 3*)

▾ **Guidelines on accuracy of data**

Banking institutions' data accuracy is reliable, but this is not the case for MFI data (especially for the non-regulated institutions). One of the main causes has to do with small credit providers' weak IT and organizational systems (of which there are many in Mexico). Another reason is the lack of a reliable national identification number. In addition there are homes without assigned addresses, mainly in rural areas. Both data sets are important in verifying the borrower's basic information.

Because there is no public credit registry, all institutions send data directly (with a prior contract) to one or both credit bureaus. These in turn perform validation procedures, and while they try to be strict, they do not identify all inconsistencies. It should be noted that credit bureaus require a minimum quality standard before accepting data from financial institutions.

Inconsistencies are usually related to the accuracy of the balances, court dates, or the presentation of data. Even though both bureaus say that they update data according to the frequency of payment (generally weekly), some borrowers complain that they have paid their debts, though on credit reports they appear as unpaid

It is important to emphasize that for the most part, MFIs offer village banking loans with weekly repayment schedules. In the cases where data is updated monthly there is a lag of four paid installments that have not been reported to credit bureaus. Other times, the court dates do not correspond to the last month reported by all institutions, but instead to previous months. Credit bureaus usually accept a two-month lag before discontinuing service to the MFI, which is also results in outdated data.

³⁵ Association of Multiple Purpose Financial Companies in Mexico A. C.

³⁶ Mexican Association of Popular Financial Companies.

³⁷ National Network of Financial Services Providing Institutions.

The data validation done by some unregulated MFIs prior to submitting data to credit bureaus is not strong (See Guideline on security measures). It is possible that the weak IT systems do not identify inconsistencies and neither do the credit bureaus' validation systems.

Some MFIs do not have a consolidated borrower database; instead they have to consolidate different databases from various agencies or products. Other very small MFIs work in Excel and are generally run by a single accountant or administrator who prepares the data.

In order to facilitate the filling of data forms, credit bureaus provide an electronic file to some MFIs with poor IT systems. Some do not fill out the forms required by the credit bureaus correctly and therefore their information is not accepted. MFIs need better training on data submission and the importance of accuracy and timeliness.

Many MFIs do not have cash counters; instead they use the services of banks, where borrowers, usually of village banking loans, cancel loans. In these cases, data updates of MFI balances usually take a few days, which is why outdated balances are reported to credit bureaus.

Because most small MFIs operate in rural areas with village banking methodology usually visit clients in their homes, some loan officers do not report payments the same day, causing a delay in the reporting system.

Another relevant factor that affects data accuracy is the lack of a reliable national identification document³⁸. This data is optional when reporting to credit bureaus, but can fill a void, validating borrower data with full name, address, and date of birth. However, these validations are complicated for rural borrowers, who do not have an exact address. Their address is reported as "known address." All of this leads to duplicate debtors in the system and credit history errors.

The various cases of inaccuracy lead MFIs to either believe the borrower or request the necessary documents to justify their claims, as making official claims is complicated (see claim resolution guide). This leads to a database that does not get corrected despite the known errors.

Credit bureaus have made efforts to seek alternatives to mitigate these inconsistencies, but there is still room to continue working on this topic.

↘ **Guidelines on timeliness of data**

Data timeliness is good³⁹. Both bureaus update data as the loans are repaid (weekly, bi-weekly, or monthly), although not all MFIs do this.

"Credit Circle" estimates that 70% of loans are updated weekly. Despite improving data timeliness, Mexico has yet to achieve Brazil's record, where negative data is reported daily.

Credit bureaus offer discounts for submitting timely and accurate data. Also, regulations give them the power to discontinue service upon failure to report data. Both elements motivate institutions to report in a timely manner.

³⁸ Although there is a "Population Registry Code," it is not a reliable national identification document.

³⁹ See "Scale" in the glossary.

However, there are MFIs that do not meet deadlines, possibly because of their weak IT systems or staff shortages (*See Guidelines on data accuracy*). This data lag is mitigated by the daily record of attempts made by the borrower to attain loans from other financial institutions (“loan request footprint”), which alerts MFIs about borrower behavior during this lag time. However, because of financial data dispersion between the two credit bureaus (*See Guidelines on collection of data on a systematic basis from all relevant and available sources*), the loan request footprint provides only partial information if the MFI only used the services of one credit bureau.

↘ Guidelines on sufficient data – including positive

Data sufficiency in credit bureaus is moderate. Although they have a vast amount of data, by law the name of the financial institution is not published in the credit reports obtained by credit providers. Furthermore, financial institutions do not voluntarily report collateral data.

In Mexico, positive data (all borrower activity, be it timely payments or not) is reported.

Financial institutions report credit amounts from one Mexican peso (approximately US\$0.08), which is good because data from borrowers of even the smallest loans available to MFIs.

Credit bureaus present loan balances by institution, but legally they cannot give the name of the financial institution to loan providers. Therefore, only the type of institution is presented, i.e. banking, financial, NGO, or cooperative.

This deficiency causes difficulties because the borrower cannot identify balance errors in the credit reports obtained from the credit providers, and if they do, they do not know what institution reported the error. In order to investigate the error they must first approach the credit bureau and obtain more information from a personal special report (*See Guidelines on dispute resolution*).

Furthermore, although it is permissible to publish collateral information, it is not required. As a result, financial institutions do not report it, creating a gap in credit analysis.

Despite these two major gaps, Mexican credit bureaus have significant amounts of data. “Credit Circle” has worked closely with MFIs to determine the specific data needs for the sector and has created a specialized credit report for MFIs. Some of the data includes payment frequency, payment quota, and type of methodology, specifying group loans. This last piece of information is important since many MFIs offer village banking methodology.

In general, it would be useful to have the following additional information to improve credit analysis:

1. Name of the financial institution⁴⁰.
2. Individual balance of the group loan (only the group balance assigned to each member of the group appears).
3. Data from basic utility companies such as water and electricity.
4. Chamber of Commerce data (bounced checks, protested promissory notes).
5. More data from credit providers from the non-financial sector.
6. Data from public institutions, such as tax debt, criminal proceedings (only “Credit Bureaus” reports this).

⁴⁰ Although this data is reported to credit bureaus, only the borrower has access through a special report, but not financial institutions.

↘ Guidelines on collection of data on a systematic basis from all relevant and available sources

Data collection in Mexico is moderate. There is no public credit registry that focuses on data from the regulated financial system. There are many non-regulated credit providers that do not report to any credit bureau. Although in total assets they represent a low percentage of the financial system, if they share borrowers from the regulated microfinance institutions, they are subject to risk by not consulting the borrower's credit history. Moreover, in comparison to other countries included in this study, there is a lack of credit providers from the non-financial sector and more relevant data from the public sector.

Regulated institutions report independently to the credit bureaus of their choice. This causes the two credit bureaus to have only some of the institutions as users. Some institutions use both bureaus' services in order to have complete data from the regulated financial system.

To fill this gap, authorities tried to force the two credit bureaus to share data with each other, but a legal claim has invalidated this measure. Now they only share overdue balances greater than 30, 60, or 90, days, depending on the product, as well as all the operations that are reported as fraudulent.

Because "Circle Credit" was created to cover the gap left by "Credit Bureau" regarding the microfinance sector, they have more data on this sector; however, there are many unregulated MFIs that do not report to either bureau.

There are many reasons why unregulated MFIs do not report; one of them is low data quality that does not meet the standards of credit bureaus and would increase data inaccuracy (*See Guidelines on data accuracy*).

This has led to unregulated MFIs sharing data locally. Currently, there are three initiatives that have been working for approximately three years in some states, though they are not yet recognized by the authorities. The MFIs affiliated with these local bureaus continue consulting the national credit bureaus, which increases operating costs.

Some reporting institutions believe it is expensive to report to credit bureaus because of the investment needed for software and a staff member to prepare the database for submission. There are many small MFIs that have weak IT systems (use Excel spreadsheets for reporting), resulting in manual work with errors and a high cost for quality revision.

Some unregulated SOFOMs do not believe that reporting to credit bureaus is important. Many work with group loans where borrowers know each other and are responsible to each other. However, global experiences invalidate this belief since even in group methodology there is a risk of over-indebtedness.

Others provide loans with payroll discounts (called payroll loans). Because the employer guarantees the loan, MFIs do not believe it is necessary to consult the borrowers. There are also small MFIs that fund closed groups, such as farmers or other unions where the borrowers are already known and are therefore not consulted.

Also, because of the high profitability of the Mexican microfinance sector there is less care about operation and provision costs, compared to mature markets. In Mexico, there is not a thorough analysis of competitors and of the risk of sharing borrowers.

In contrast, in Bolivia, with one of the lowest lending rates of the global microfinance sector, MFIs try to keep all costs low. In that country, there is no doubt that credit bureaus are an efficient tool in reducing credit risks and general costs.

Generally, SOFOMs are relatively new institutions (in the last five years) and, in many cases, their boards and management lack in-depth knowledge of the microfinance sector, so they ignore the importance of credit bureaus. Therefore, more training and alerts at the executive and management level are necessary.

Although credit bureaus are regulated in Mexico, there are cases where MFIs are distrustful of reporting to credit bureaus because some of the shareholders work in the same niche as the microfinance institutions. This fear is exacerbated given that the two bureaus' offer a market analysis (in the aggregate) at the request of any institution. MFIs perceive the cost as high and fear that only large MFIs have access to these services, gaining an advantage over the smaller ones. This has caused some MFIs to believe there is unfair competition.

It is worth noting that some countries restrict credit bureau data only to credit risk analysis, prohibiting their use for any other activity.

On the other hand, banks are obliged to consult 100% of the borrowers while regulated non-bank microfinance institutions only consult for loan amounts greater than US\$500 (approximately). This amount does not include many debtors of MFIs whose loan portfolio primarily comprises village banking loans, where the average loan size is lower, nor does it motivate the microfinance sector to use credit bureaus.

In contrast, ProDesarollo, the development bank, and some international funders have demanded that MFIs report to credit bureaus. This has been successful and various MFIs have been incorporated to at least one credit bureau.

Including more reporting institutions from the non-financial sector that serves the low-income niche of the population remains a challenge. Though there are many reporters from this sector, participating MFIs mentioned that there are still many that do not report, yet they offer loans to the same segment as the MFIs, making it important to incorporate them.

Public institutions with relevant data still need to be included. Greater awareness of the benefits brought about by sharing data is needed.

▾ Guidelines on retention of data

Data retention in credit bureaus is very good.

Unpaid debt remains in credit bureaus for six years. Canceled debts also remain in credit bureaus for six years.

General Principle 2: Data Processing: Security and Efficiency *(See definition in Annex 3)*

▾ Guideline on security measures

Data security measures in the microfinance sector are insufficient because the sector is largely unregulated. Regulated financial institutions have strong data security measures established by the supervisory body.

There is also regulation and supervision of credit bureau security measures. Credit bureaus have developed strong data security measures based on their own initiatives. “Credit Bureau” also follows the security measures of its shareholder TransUnion LLC, which has ample international experience.

Due to their nature, unregulated MFIs’ data security measures are not supervised. The risk that this implies is mitigated by credit bureaus’ data quality requirements, although this is insufficient in detecting all data inconsistencies (*See Guidelines on data accuracy*).

↘ **Guideline on reliability**

In Mexico there is trust in credit bureau service, which is generally continuous. Good internet connections, mainly in urban areas, and bureaus’ preventative measures allow this level of service. In some rural areas there have been electronic and internet service interruptions, but to a lesser extent.

↘ **Guideline on efficiency**

Credit bureau service efficiency is good. The cost per consultation is similar to the average of the other studied countries.

The channel most used to access credit reports is online via the credit bureau’s website. There is also dedicated service (server to server), where the MFI can organize its reports according to internal criteria.

There are specialized microfinance units within both bureaus that collect the necessary data for the sector and provide services similar to those of other countries, such as scores and early alerts.

The specialized market analysis (in the aggregate) service is perceived as expensive by microfinance institutions and has poor results in the microfinance sector because of insufficient data and the dispersion of data in the two bureaus.

The price per consultation is similar to the average of the other studied countries (US\$1.00). Furthermore, reporting institutions get discounts (up to 30%) if they meet the reporting and quality deadlines and pay in a timely manner. Another factor to consider with regards to the price is the amount of data provided and the number of inquiries.

Credit bureaus incur high costs in collecting data from various nationwide sources due to the lack of a public credit registry that provides data on the regulated system for free, as is the case in Peru.

To reduce the cost of consultations, credit bureaus have signed agreements with MFI networks. Affiliate institutions get a lower price than non-affiliates, but the agreements are made with the individual MFIs. The networks work with both credit bureaus, which is advantageous because they both have data from the sector.

In contrast, an MFI network in Peru made similar agreements but accepted a clause to report to only one credit bureau. This created a predominance of that bureau, which translated into higher prices for the large amount of data that it had.

General Principle 3: Governance and Risk Management *(See definition in Annex 3)*

▾ **Guideline on accountability of governance arrangements**

Credit bureaus are accountable for controls, both internal and those of the supervisory body. This promotes high responsibility in the management and protection of data and consumers.

▾ **Guideline on transparency of governance arrangements**

Credit bureau transparency is good, although it could improve if credit bureaus published their shareholder compositions on their web pages.

Generally, credit bureaus use their websites to describe their business and services, but not their shareholder composition. “Credit Circle” shows its shareholder composition in the proposals it sends its users.

Transparency regarding ownership is more necessary in Mexico because both bureaus have financial institution shareholders, some of them even serving the microfinance sector. There are fears of conflicts of interest among MFIs due to financial institutions’ ownership of credit bureaus (see guide to government efficiency regulations to ensure that all users have equal access to data).

▾ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

The supervisory body provides regulations and supervises credit bureau risk management, thereby mitigating business risk.

▾ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

All users have the same right to access credit bureau data.

The risk of conflict of interest caused by both bureaus having financial institutions as shareholders is mitigated by regulations that limit the shareholding to 18%, preventing participants from having majority shares.

General Principle 4: Legal and Regulatory Environment *(See definition in Annex 3)*

▾ **Guidelines on clarity and predictability**

Credit bureau regulations are clear and the consequences for non-compliance are predictable. However, there is not enough dissemination of these regulations.

While the consumer protection agency⁴¹ publishes regulations on its website, this is not a broadcast medium commonly used by the consumer.

Of the studied countries, Peru is a good example of dissemination where they use various visual venues: in offices through the use of videos and posters, and mass media, such as the radio, television, etc.

↘ **Guidelines on non- discrimination**

All of the reporting institutions and users of credit bureaus have the same legal obligations. Generally the reciprocity principle is respected, meaning that only the reporting institutions may consult credit bureaus.

However, with the goal of facilitating MFI assimilation, credit bureaus sometimes allow MFIs to consult without reporting during the period when MFIs are attempting to reach the quality and sufficiency standards required.

↘ **Guidelines on proportionality**

There is moderate proportionality and balance in the existing regulations.

Regulations can be met by all members of the credit reporting system. However, the borrower cannot identify the name of the financial institution that reported their data in the credit reports. To learn this information they must go to the credit bureaus (whose offices are only in the capital) and request a personal and detailed report with the names of the institutions.

Although there is a claims process on the credit bureaus' websites, consumers in rural areas generally do not have access to computers, nor do they know how to submit claims in this manner.

Consequently, consumers cannot easily identify errors, nor can they make the necessary claims.

Penalties for non-compliance to regulations are reasonable.

↘ **Guidelines on consumer rights and data protection**

There are enough data and consumer protection laws in Mexico.

Banking privacy is observed for lending and borrowing operations, which is why authorization is required in order to access data. Credit bureaus perform biannual audits regarding compliance with this norm and if breaches are detected, they are reported to the corresponding authorities. If the percent incomplete is significant, service is discontinued.

Regulations include minimum consumer rights such as being informed of the purpose, processing, and distribution of the collection of their data, as well as periodic access to data and the possibility of making claims.

Condusef is the state agency responsible for ensuring compliance with these regulations. It specializes in protecting the consumer from the financial system, both from regulated and unregulated institutions. There is also another entity (Profeco⁴²) for businesses that offer credit outside of the financial system (stores, public service providers, such as water and electricity, etc.).

⁴¹ National Commission for the Protection and Defense of Financial Service Users (Condusef).

⁴² Federal Consumer Attorney.

▾ **Guidelines on dispute resolution**

Although there are claims regulations, they are not sufficiently known, nor is there enough logistical support for the borrower.

During interviews for this study, there was no uniformity in participant responses, which proves that regulations are not disseminated for both MFIs and consumers.

If a financial institution finds an error in the credit report, the consumer must approach the credit bureau⁴³ or the government agency for consumer protection, to obtain a personal report where the names of the financial institutions are shown.

The credit bureau initiates the investigation process with the financial institution. If the institution does not resolve the claim by the deadline, the claim is understood to be in favor of the consumer.

Some consumers approach Condusef, the government agency for consumer protection. However, though Condusef has offices in most areas of the country, they are insufficient given the many small cities in each state. Consequently, the borrower is forced to travel to other cities.

⁴³ Although legally MFIs can provide this report (based on previous agreements with credit bureaus), very few offer this service.

CONCLUSIONS

This section organizes the conclusions based on the principles outlined in the body of this report:

General Principle 1: Data

- ▶ Data accuracy for banking institutions is reliable, though not for MFIs (especially for unregulated institutions). One of the reasons is the weak IT and organizational systems of small MFIs (of which there are many in Mexico). Another reason is the lack of a trusted national identification number. Furthermore, there are homes without addresses, mainly in rural areas. Both sets of data are important for borrower identification.
- ▶ Data timeliness is good. Both bureaus update data based on the frequency of the loan's repayment (weekly, bi-weekly, or monthly), although not all MFIs do so.
- ▶ Data adequacy in credit bureaus is moderate. Although there is a vast amount of data, by law the name of the financial institution is not published in the credit reports obtained by credit providers. Also, MFIs do not voluntarily report collateral data.
- ▶ Data collection is moderate. There is no public credit registry that consolidates data from the regulated financial system. There are many unregulated credit providers that do not report to credit bureaus. Although in total assets they represent a low percentage of the financial system, if they share borrowers from the regulated microfinance institutions, they are subject to risk by not consulting the borrower's credit history. Moreover, in comparison to other countries included in this study, there is a lack of credit providers from the non-financial sector and more relevant data from the public sector.
- ▶ Data retention in credit bureaus is very good.

General Principle 2: Data Processing: Security and Efficiency

- ▶ Data security in the microfinance sector is insufficient because the sector is mostly unregulated.
- ▶ Credit bureau service is reliable.
- ▶ Credit bureau efficiency is good. The cost per consultation is average among the studied countries.

General Principle 3: Governance and Risk Management

- ▶ Credit bureaus are accountable for controls, both internal and those of the supervisory body
- ▶ Credit bureau transparency is good, although it could be better if credit bureaus published their shareholder composition on their websites.
- ▶ Credit bureau business risks are mitigated by the regulation and supervision of risk management from a regulatory body.
- ▶ All users have the same rights to access data from credit bureaus.

General Principle 4: Legal and Regulatory Environment

- ▶ Credit bureau regulations are clear and the consequences for non-compliance with them are predictable. However, there is insufficient dissemination of these regulations.
- ▶ All reporting institutions and users of credit bureaus have the same legal obligations.
- ▶ There is moderate proportionality and balance in the existing regulations.
- ▶ There are sufficient regulations regarding data and consumer rights protection.
- ▶ Despite the existence of consumer claims regulations, they are not sufficiently known. There is also not enough logistical support for borrowers.

RECOMMENDATIONS

This section outlines recommendations by category.

Legal

- ▶ If reliable records of citizen identification and address were established, data accuracy would improve substantially.
- ▶ Requiring credit reports to include collateral and the names of financial institutions would improve data accuracy and sufficiency.
- ▶ Making the use of credit bureaus mandatory for credit providers would improve data adequacy.

Regulatory

- ▶ Regulating the publication of shareholder composition would improve credit bureau transparency.
- ▶ To reduce distrust and fear of unfair competition caused by MFI ownership of credit bureaus, it is recommended that mechanisms be established to mitigate the perception of conflicts of interest.

Government Policies

- ▶ Motivate public entities with relevant data to report to credit bureaus at a reasonable cost, therefore benefitting the country's credit system.
- ▶ Encourage credit providers of the non-financial sector to report to credit bureaus to improve borrower's credit evaluation.
- ▶ Disseminate consumer rights and obligations regarding credit bureaus through effective public venues.
- ▶ Strengthen the public body that supervises compliance with consumer protection norms. While regulations are ample, in practice consumers do not have adequate support.
- ▶ It is recommended that the necessary infrastructure to attain reliable official records on the number of credit providers (including MFIs) in the country be created.

Techniques and Training

- ▶ Providing technological resources to the financial system that would allow for the updating of data daily would be a modest investment compared to the positive impact that it would have on the development of microfinance institutions.
- ▶ To improve data accuracy and timeliness, MFIs should receive more training on data reporting and the benefits that credit bureaus provide to the financial system.
- ▶ To improve data accuracy, it is recommended that MFI networks motivate unregulated affiliates to follow the prudential regulations of the financial system for quality control and general risk management.
- ▶ In order to improve credit risk analysis it would be useful to include the following data in credit bureaus:
 1. Name of the financial institution.
 2. Individual balance of the group loan (only the group balance assigned to each group member is reported).
 3. Data from utility companies, such as water and electricity.
 4. Chamber of Commerce data.
 5. More data from credit providers from the non-financial sector.
 6. Data from public institutions: such as tax debts and criminal proceedings (only "Credit Bureau" reports this).

▾ EXECUTIVE SUMMARY

Despite the broad participation of microfinance institutions (MFIs) in credit bureaus, the microfinance sector in Nicaragua has a long way to go to develop an excellent credit reporting system. There are opportunities for improvement in the accuracy and adequacy of data, as well as the regulatory framework.

The majority of microfinance institutions are not regulated. Weaknesses in computer information systems and data control lead to data that is not precise or timely.

Data sufficiency is moderate. Information from the financial system is reported to two separate credit bureaus. In most cases, the name of the financial institution is not published. Some institutions report positive information to the bureaus, and others only report negative information. This makes analyzing credit risk difficult.

On the other hand, there is a perception that participants are not complying with standards for consumer protection. These standards have not been disseminated widely, and there are few facilities for making claims, preventing consumers from exercising their rights.

Despite the weaknesses mentioned, the system has protected MFIs by enabling them to identify those involved in the No Payment Movement. Since the 2008 crisis in the microfinance sector, MFIs have increased the number of inquiries they make, using credit bureaus as a way to strengthen their portfolios. Now there is no doubt about the importance of credit bureaus in Nicaragua. The regulation of microfinance NGOs, now in place, is expected to strengthen the sector, enforcing prudential norms and improving the performance of the credit rating system.



UNDERSTANDING THE NICARAGUAN MICROFINANCE SECTOR IN RELATION TO THE PUBLIC CREDIT REGISTRY AND CREDIT BUREAUS

The microfinance sector is improving after the severe economic crisis of 2008. High levels of borrower indebtedness culminated in the No Payment Movement (MNP). Many MFIs reduced their portfolios and lost capital due to rapidly deteriorating portfolio quality. The country's largest microfinance bank collapsed. This chain of events made Nicaragua's crisis one of the worst microfinance crises worldwide.

Although the government supported and encouraged the MNP during the first several years, it was silent during the country's electoral campaigns, weakening the movement. Today, MFI portfolios are no longer deteriorating from the MNP. Nevertheless, it is difficult to collect debts from borrowers who participated in the movement.

Credit bureaus have been essential in reducing the risk of over-indebtedness and identifying members of the MNP. A public credit registry and two credit bureaus, Transunion and Sin Riesgo, operate in Nicaragua. The first focuses mainly on the banking sector. The second is owned by NGOs affiliated with the ASOMIF network⁴⁴. As a result, it is focused on the microfinance sector.

After the microfinance crisis, the number of borrowers decreased significantly, and the number of inquiries increased. This indicates increased awareness about the importance of using credit bureaus to reduce the risk of over-indebtedness.

The public credit registry is managed by the Superintendence of Banks and Other Financial Institutions (SIBOIF). It collects information on all regulated financial institutions and makes the information available to them for free.

The credit bureaus do not receive information from the public credit registry. Their database is fed by data delivered independently by regulated and unregulated financial institutions and the non-financial sector.

Nicaragua has only a few years of experience with credit bureaus. The supervisory body issued standards for these bureaus in 2005. In March 2012, it approved a law for the protection of consumer data, though the law's scope does not reach the financial sector. This law overprotects the debtor, allowing them to ask the reporting institution to erase their history of cancelled debts.

On the other hand, Nicaraguan law requires banks to publish the names of debtors undergoing judicial proceedings in the newspaper. This is a deterrent not seen in other countries.

In 2011, the country passed a law to regulate microfinance NGOs. This law eliminates the interest rate cap (previously established by the government), promotes good corporate governance, and increases consumer protection. Nevertheless, it does not allow these MFIs to collect deposits and will regulate them through a majority government organization, National Microfinance Commission (CONAMI), rather than the bank regulatory agency. Without the ability to collect deposits, these institutions' options for growth are limited. Nevertheless, the supervisory agency has the potential to strengthen microfinance NGOs by applying prudential standards.

There are only three regulated MFIs; the other 21 MFIs are NGOs under the ASOMIF network's umbrella. The network's indicators show that the negative trend in portfolio quality seen over the last three years has been halted. As of June 2012, average portfolio at risk was estimated to be 6%.

⁴⁴ Network is made up of 21 unregulated MFIs.

ALIGNMENT OF NICARAGUA'S MICROFINANCE SECTOR WITH THE WORLD BANK'S GENERAL PRINCIPALS FOR CREDIT REPORTING

Using the General Principals for Credit Reporting published by the World Bank in September 2011 as a reference, this report presents the following analysis of the Nicaraguan microfinance sector:

General Principle 1: Data *(See definition in Annex 3)*

↘ **Guidelines on accuracy of data**

While the public credit registry presents reasonably accurate data, there is uncertainty about the accuracy of the credit bureaus' data.

Although the credit bureaus have processes for validating data, oversight of unregulated MFIs' databases is insufficient (*See Guideline on security measures*). This is worrisome given that the majority of MFIs are not regulated.

Some institutions do not fill out the forms required by the credit bureaus correctly. At the same time, because the regulatory framework has gaps, MFIs establish their own criteria for certain data and determine its timeframe.

The absence of robust information systems is one possible source of errors. For example, some MFIs do not have a central database of borrowers; instead they must consolidate multiple databases from different branches or products. To fill this gap, the ASOMIF network has designed software for MFIs. This software still needs to be certified by an independent specialist, however.

The absence of a strict legal framework that penalizes MFIs for errors in reporting (*See Guideline on consumer rights and data protection*) also leads to inaccuracy. In the majority of countries evaluated in this study, a strict regulatory framework that penalizes MFIs for errors has compelled MFIs to send accurate information.

At the same time, credit bureaus are not stringent about the quality and timeliness of information. Some participants noted doubts about the date information had been updated. More training at the MFI level on the importance of accurate and timely data is necessary.

Errors are generally identified by MFIs when they analyze the creditworthiness of a borrower. It is difficult for the borrowers to spot an error because the credit bureaus provide records of individuals' debts, but not the names of the corresponding financial institutions. Similarly, the public credit registry tracks total debt rather than individual debt by institution (*See Guideline on sufficient data - including positive*).

The public credit registry has validation procedures which reduce errors. One of them is a cross-check of borrowers' balances with their balances in regulated institutions.

▾ Guidelines on timeliness of data

The data the credit bureaus provide to users is not timely. Data is updated monthly, leaving a 50 day gap on average. This impacts the analysis of borrower credit risk and generates dissatisfaction among credit bureau users.

Delays in the delivery of information by unregulated MFIs to credit bureaus are one cause. In some cases, MFIs do not have robust automated processes; instead, they rely on manual data processing often done by a single person. Many MFIs do not have a single centralized database and spend significant time consolidating data from different branches and products.

At the same time, the credit bureaus in Nicaragua update their databases more slowly than their counterparts in other Latin American countries. While it takes between two and three days to enter the information in Nicaragua, other credit bureaus enter this information in 6 hours on average. Brazil has a very rapid system where negative information appears online daily. This suggests that the Nicaraguan financial system would benefit from more advanced technology.

The public credit registry as well as the private credit bureaus make information available to users approximately 20 calendar days after the end of the month, generating a 50 day lag between updates on average. For example, until May 20th, information is available from March 31st, 2012.

Lack of timely data is a risk given that borrowers have quick access to small loans from multiple MFIs without collateral. A daily register of the number of times a borrower attempts to access credit from other financial institutions (loan request footprint) mitigates this risk. This number, published with the name of the institution, alerts institutions to the borrowers' behavior during the gap between data updates.

▾ Guidelines on sufficient data – including positive

The public credit registry and the credit bureaus have moderate data sufficiency⁴⁵.

The public credit registry does not present debt by institution, but in aggregate, indicating the number of financial institutions where the borrower has debt. Although the credit bureaus provide balances by institution, they do not generally share the name of the institution. This deficiency means that the borrower cannot identify errors in their balance and if they do identify them, they do not know which institution reported it, forcing them to request it from the regulatory entity or the credit bureau (*See Guidelines on dispute resolution*).

Legally institutions can report positive information, which includes all the borrower's activities, whether payments are punctual or not. Nevertheless, given that regulated institutions send information to credit bureaus voluntarily, some of them only share negative information (*See Guidelines on collection of data on a systematic basis from all relevant and available sources*). Other regulated institutions only report some types of loans. Also, based on their contracts with the credit bureaus, they may or may not publish the name of the financial institution.

Unregulated MFIs generally publish positive information but without their name for fear of losing their clients. In this case, they report the type of institution: bank, finance institution, NGO, or cooperative. Additionally, some MFIs do not report the full set of data required by the credit bureaus because they do not collect the data in their information systems.

⁴⁵ See "Scale" in the glossary

Annex 1 **Nicaragua**

The public credit registry only reports the borrower's status for the previous month because it does not have the technological capacity to build a database covering multiple periods. This suggests that technological support is needed. The credit bureaus provide information for the past 24 months.

The institutions report loans from one Córdoba (approximately US\$0.05); this is laudable in that it provides information to MFIs on borrowers with even the smallest loans.

Despite the gaps, Nicaragua's credit bureaus fully provide the minimum data required by the General Principals for Credit Reporting published by the World Bank.

Additionally, the bureau Sin Riesgo reports the exact number of days past due, information rarely provided in the countries studied. Other countries report the number of days past due in ranges, which provides less information. The public credit registry reports only the maximum number of days past due as it tracks the borrower's aggregate debt.

Identifying borrowers participating in the No Payment Movement (see Context) in the credit bureaus with a special code was invaluable for MFIs recovering from the 2008 crisis. All of the country's financial institutions closed their doors to these borrowers.

In general, having the following additional data would be useful for improving the analysis of credit risk:

1. Name of the financial institution.
2. Type of lending methodology (group or individual).
3. Group balance for solidarity lending (only the individual balance appears).
4. Borrower credit score.
5. Information from public sector service providers, such as water and electricity.
6. Information from Chambers of Commerce.
7. More information from the non-financial sector.
8. Information from public institutions, such as tax claims, criminal proceedings, etc.

↘ **Guidelines on collection of data on a systematic basis from all relevant and available sources**

Although MFI participation in the credit bureaus is very good, the participation of the productive sector and public sector is low compared to other countries studied. The public credit registry does not share its database with the credit bureaus. They collect information in parallel and, through private contracts, make agreements with the financial institutions establishing the information to be reported.

Regulated financial institutions report independently and only to the credit bureaus they select. This means that the credit bureaus do not receive information from all regulated institutions. Some unregulated institutions use the services of both bureaus in order to have complete information from the regulated financial sector.

Because the NGOs affiliated with the ASOMIF network own the credit bureau Sin Riesgos, they generally report to this bureau. Very few of these institutions report to Transunion. There are few unregulated MFIs that do not report to any bureau.

Contracts that mandate exclusive reporting to a single credit bureau are prohibited in Nicaragua. This prevents microfinance data from being concentrated in a single credit bureau.

Until the microfinance crisis in 2008, there were still MFIs that did not report any information. After the crisis there was no doubt of the importance of reporting to credit bureaus.

Incorporating more credit providers from the non-financial sector remains a challenge. One positive factor is that warehouses report positive information, a practice not common in other countries where they predominantly report only negative information.

Likewise, public agencies with information on criminal proceedings, tax debt, and other relevant data are not included in the system.

The sector also lacks understanding of the benefits of sharing this type of information.

However, the bureau Sin Riesgos is filling this void to some extent by collecting information from cases brought by banks and records of alimony payments. This information is especially important in Nicaragua, where a large number of debtors are under judicial proceedings after the recent microfinance crisis.

Additionally, Sin Riesgos uses case information published in newspapers by banks (*See Context*). Although it is legal to collect public information, there is a risk that balances are not up-to-date, which can hurt the borrower. This occurs because data is erased five years after it is entered in the database.

Some public institutions cannot report to the credit bureaus because they do not have complete information --they may identify citizens by a self-reported name, which may be incomplete, instead of using a national identification document.

A number of years ago, the country standardized the use of national identification, and MFIs have been adding this information to their databases. Nevertheless, some MFIs still report information by the client's name, which makes it difficult to search for a particular borrower and impacts the accuracy of data.

↘ **Guidelines on retention of data**

The credit bureaus' data retention is good.

Unpaid debt (the balance or write-off) is listed until it is cancelled or reaches the ten year period prescribed by the civil code.

The history of cancelled debt is published for two years and remains in the credit bureaus' databases for five years. Even though credit bureaus are regulated, supervision to verify compliance with the data retention period is limited.

The public credit registry keeps records of unpaid debts indefinitely.

General Principle 2: **Data Processing: Security and Efficiency** *(See definition in Annex 3)*

▾ **Guideline on security measures**

Data security measures in the country's microfinance sector are insufficient because the sector is largely unregulated.

The supervisory agency has established strict data security measures for regulated institutions.

In contrast, although there are regulations for credit bureaus, the supervisory agency does not enforce them due to personnel shortages. Mitigating this risk, Transunion observes internal standards for security and audits set by its headquarters in the United States. Similarly, both bureaus conduct informational audits using firms authorized by the supervising agency.

Given their nature, unregulated MFIs do not have standards for data security. This is a significant gap given that they are much more numerous than regulated financial institutions. This risk is not mitigated by the credit bureaus' service contracts as they are not very strict in terms of quality and consistency of information.

▾ **Guideline on reliability**

The country's credit bureaus are reliable.

In general, service is continuous. This level of service is possible because of strong internet connections, particularly in urban areas, and the preventive measures taken by the credit bureaus. Some rural areas have experienced service interruptions from power outages, but not generally from internet interruptions.

▾ **Guideline on efficiency**

The efficiency of the credit bureaus' service is moderate. The cost per query is average for the group of countries studied, but there are no specialized services for the microfinance sector.

Credit bureaus offer online access through their webpage as the most common channel for accessing credit reports. In-person information delivery is also offered.

Currently, insufficient data has reduced opportunities for creating specialized products for the microfinance sector (See Guidelines on sufficient data - including positive). Neither bureau offers products such as credit scores or early alerts, similar to other countries.

The specialized service of customizing credit analysis and analyzing the borrower group is expensive and does not provide accurate results given data insufficiencies. The cost per query (US\$1.00) is average for the group of countries in this study.

Regulated institutions access the public credit registry at no cost.

General Principle 3: Governance and Risk Management *(See definition in Annex 3)*

▾ **Guideline on accountability of governance arrangements**

The credit bureaus are accountable to the public supervisory authority, promoting responsible business management and the protection of data and consumer rights.

▾ **Guideline on transparency of governance arrangements**

The credit bureaus' transparency about business activities is good. However, they do not publish information about their shareholder composition.

The credit bureaus generally have a webpage describing their business and products. Nevertheless, they do not publish information about their shareholders, which limits transparency and leads to conflicts of interest in some countries. This is necessary because Nicaraguan law allows financial institutions to own credit bureaus. As a result, MFIs affiliated with ASOMIF own the credit bureau Sin Riesgo.

Also, because the country does not have a strong regulatory framework for consumer claims, it does not publish clear directions on the process for resolving data errors.

▾ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

Although there are standards for risk management, supervision of the credit bureaus by the supervisory agency is not strict in comparison to the oversight of MFIs.

▾ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

All users have equal rights to access the credit bureaus' information.

Currently, there are no conflicts of interest in terms of ownership even though the MFIs affiliated with ASOMIF own Sin Riesgos. Even the partners who own the credit bureau do not receive preferential prices.

General Principle 4: Legal and Regulatory Environment *(véase la definición en el anexo 3)*

▾ **Guidelines on clarity and predictability**

Standards related to the credit bureaus are clear. Nevertheless, these standards have not been disseminated, and participants are not fully aware of the consequences of noncompliance.

Anexo 1 **Nicaragua**

Although the supervising entity publishes standards on its web page, consumers don't use this mode of communication frequently. Peru provides an example of good dissemination practices. The country uses a variety of media, focusing on those accessible and visible to borrowers: videos and posters in offices, and mass media such as radio, TV, etc.

↘ **Guidelines on non-discrimination**

All information providers and users of the credit bureaus have the same legal obligations.

Observance of the principle of reciprocity is positive. For example, when a bank only reports negative information, it can only access negative information from its competitors.

↘ **Guidelines on proportionality**

The current standards lack proportionality and balance. These standards can be met by all the participants in the credit reporting system. However, financial institutions report only the information that is convenient for their business (See Guidelines on sufficient data - including positive), without observing consumer rights. Effectively, the consumer cannot identify the financial institution's name from the credit reports. As a result, the borrower cannot identify errors or access mechanisms for making claims.

Institutions are not penalized for errors and borrowers are not compensated for damages.

↘ **Guidelines on consumer rights and data protection**

Nicaragua has standards for data protection and consumer rights. Nevertheless, participants in this study stated that standards are not observed even though there is a government agency responsible for ensuring compliance.

There are standards for banking privacy in lending and borrowing transactions. Reporting and viewing credit information requires borrower authorization.

↘ **Guidelines on dispute resolution**

Neither the regulated nor unregulated financial system applies the necessary mechanisms to handle consumer claims.

When an institution identifies an error, the borrower should ask the supervising entity or the credit bureau for the name of the financial institution responsible for the error (a cumbersome process for the debtor).

Additionally, there are no facilities for making claims. The supervisory agency's offices and the credit bureaus are located in the country's capital, leaving consumers in the interior without facilities.

Only a few financial institutions have internal processes for resolving consumer claims. Even when they exist, service is slow and not monitored by an external entity.

CONCLUSIONS

En esta sección se clasifican las conclusiones según los principios expuestos en el cuerpo del reporte.

General Principle 1: Data

- ▶ Although the public credit registry provides reasonably accurate data, there is doubt about the accuracy of the data from the credit bureaus. One of the causes is insufficient data security measures in unregulated MFIs, which are greater in number than regulated MFIs.
- ▶ The data in the country's credit bureaus is not timely. The practice of updating data monthly leads to a 50 day gap in data on average.
- ▶ Limitations in the Nicaraguan financial system's computer-based information systems impair the accuracy and timeliness of data.
- ▶ Data sufficiency in the public credit registry and the credit bureaus is moderate. There are gaps in information needed for the evaluation of credit risk, such as the name of the lending institution. The public credit registry does not report balances by institution; it only reports the borrower's consolidated balance.
- ▶ Although MFI participation in the credit bureaus is very good, the participation of the non-financial and public sectors is low compared to other countries studied. The public credit registry does not share its database with the credit bureaus. They collect information in parallel and, through private contracts, make agreements with the financial institutions establishing the type of information to be reported.
- ▶ The credit bureaus' data retention is good.

General Principle 2: Data Processing: Security and Efficiency

- ▶ Data security measures in the country's microfinance sector are insufficient because the sector is largely unregulated.
- ▶ The credit bureaus' service in the country is reliable.
- ▶ The efficiency of the credit bureaus' service is moderate. The cost per query is average for the group of countries studied but there are no specialized services for the microfinance sector.

General Principle 3: Governance and Risk Management

- ▶ The credit bureaus are accountable to the public supervisory authority, promoting responsible business management and the protection of data and consumer protection.
- ▶ The credit bureaus' transparency regarding business activities is good. However, they do not publish information about their shareholder composition.
- ▶ Although there are standards for risk management, supervision of the credit bureaus by the supervisory agency is not strict in comparison to the oversight of MFIs.
- ▶ All users have equal rights to access the credit bureaus' information.

General Principle 1: Legal and Regulatory Environment

- ▶ Standards related to the credit bureaus are clear. Nevertheless, these standards have not been disseminated, and participants are not fully aware of the consequences of noncompliance.
- ▶ All information providers and users of the credit bureaus have the same legal obligations.
- ▶ The current standards lack proportionality and balance. Financial institutions report the information that is convenient for their business and the borrower cannot identify errors or access mechanisms for making claims.
- ▶ Nicaragua has standards for data protection and consumer rights. Nevertheless, participants in this study stated that standards are not met even though there is a government agency responsible for ensuring compliance.
- ▶ Neither the regulated nor unregulated financial system applies the necessary mechanisms to handle consumer claims.

RECOMMENDATIONS

This section groups recommendations by type.

Legal

- ▶ With the objective of improving the accuracy and sufficiency of data, it is recommended that the government standardize the obligatory publication of positive information and include the name of the financial institution and individual balances by institution. In general, revising the balance of rights between debtors and financial institutions is suggested.

Regulatory

- ▶ With the objective of improving the timeliness of data, it is recommended that the supervisory authority study the feasibility of increasing the frequency of updating data.
- ▶ It is recommended that the supervisory body in charge of enforcing the oversight of the credit bureaus perform its function more effectively.
- ▶ With the objective of improving the credit bureaus' transparency, regulating the publication of their shareholder composition is recommended.
- ▶ Establish mechanisms to mitigate any conflicts of interest that could result from the financial institutions' ownership of the credit bureaus.

Government Policy

- ▶ Encourage public agencies with relevant data to share it with the credit bureaus, at a reasonable cost, to benefit the country's credit system.
- ▶ To improve borrower credit assessment, encourage lenders in the non-financial sector to report to the credit bureaus.
- ▶ Disseminate borrower rights and responsibilities through effective public channels.

- ▶ Strengthen the public institution that monitors compliance with consumer protection standards. Penalties for errors should be enforced and compensation should be provided to borrowers for damages.

Techniques and Training

- ▶ Provide the financial system with technological resources that would allow them to process necessary information daily. It would be a modest investment relative to the positive impact it would have on the development of microfinance.
- ▶ With the objective of improving the accuracy and timeliness of data, increasing training for MFIs on the benefits provided by the financial system is recommended.
- ▶ In order to improve the accuracy and timeliness of data, it is recommended that credit bureaus incorporate in their contracts (and enforce) more stringent terms for MFI compliance.
- ▶ While supervision of CONAMI is being consolidated, it is recommended that the network encourage unregulated MFIs to follow the financial system's prudential standards for control of data quality and risk management.
- ▶ In general, having the following additional information would be useful for improving the analysis of credit risk:
 1. Name of the financial institution.
 2. Type of lending methodology (group or individual).
 3. Group balance for solidarity lending (only the individual balance appears).
 4. Borrower credit score.
 5. Information from public service companies, such as water and electricity.
 6. Information from Chambers of Commerce.
 7. More information from the non-financial sector.
 8. Information from public institutions such as tax claims, criminal proceedings, etc.

↘ EXECUTIVE SUMMARY

The credit reporting system in Peru is good. The accuracy and adequacy of its data is outstanding, but it is not timely.

The Peruvian supervisory agency⁴⁶ is unique among the countries studied; it provides 'all'⁴⁷ its database to the credit bureaus and to the regulated financial institutions. This reduces systemic risk and the cost to the institutions.

Despite the absence of some basic information such as original amount and loan term, the Peruvian system possesses the great advantage of having information from public institutions such as on taxes and other areas, which is rarely seen in other countries. However, limited retention of cancelled debt data is very short.

The MFIs show a lack of conformity since they don't have current information to conduct credit analyses of the debtors. On the other hand, the strong competition among the credit bureaus has contributed to the offering of lower prices per query compared to the other countries studied.

The coordination between Copeme⁴⁸ and the credit bureau, Equifax, has been important for engaging a good number of MFIs in reporting and using credit bureaus.

The consumer protection regulations are strong in the financial system and communicated by strong distribution efforts through effective channels. However, the lack of banking privacy in lending transactions leads to debtor vulnerability by not seeking permission to access or manage their credit information.



⁴⁶ Superintendencia of Banking, Insurance and AFP

⁴⁷ Bolivia only offers some loan products to credit bureaus and only through online individual queries to other countries.

⁴⁸ The Consortium of Private Organizations Promoting Small and Microenterprise Development.

UNDERSTANDING THE PERUVIAN MICROFINANCE SECTOR IN RELATION TO THE PUBLIC CREDIT REGISTRY AND CREDIT BUREAUS

The Peruvian microfinance sector is mature. In fact, Peru is first in the global ranking of countries with the best economic environment for microfinance development.⁴⁹

The sector operates with specialized regulations and has been aligned with Basel II since July 2010. There are forty regulated MFIs, between the banks, municipal savings banks (CMAC), financieras, small and micro-enterprise development entities (edpymes) and rural savings banks. Furthermore, there are one hundred and sixty non-regulated cooperatives, but very few specialized in microfinance. They complement the offerings of nineteen microfinance NGOs, according to a March 2012 report issued by Copeme on microfinance in Peru.

In recent years, the level of competition in the microfinance sector has increased substantially. In several MFIs, a deterioration of portfolio quality has been observed due to greater client indebtedness.

Some banks have penetrated the microfinance sector through the purchase of MFIs, or by developing business areas in microfinance. A growing number of entities and commercial shops have also joined in by offering consumer loans.

The financing of the sector comes largely from public entities, though also from a greater number of private banks.

The credit reporting system is very competitive. There are five credit bureaus and one public credit registry managed by the supervisory agency. In addition, there are various public and private institutions that are used by MFIs as an information source to evaluate the credit risk of their debtors.

The supervisory agency collects information on the institutions in the regulated system to process and validate it. Then, the information is made available to these institutes and the credit bureaus.

The credit bureaus are Data Crédito, Equifax, Informa del Perú Sentinel, and Xchange Perú. These bureaus are not regulated. They consolidate the information about the regulated system from the public credit registry with the information obtained by independently, in accordance with the special agreements with the non-regulated financial, commercial, and public institutions.

Facing strong competition between MFIs, the current measures for reducing over-indebtedness risk (such as consulting the debtor in the public credit registry and credit bureaus) appear inadequate. The MFIs are increasingly becoming more flexible with their loan requirements, which leads to larger amounts, longer loan terms, and quick renewals, among others.

⁴⁹ Global Microscope on the microfinance business environment for 2011.

ALIGNMENT OF THE PERUVIAN MICROFINANCE SECTOR TO THE WORLD BANK'S GENERAL PRINCIPLES FOR CREDIT REPORTING

Using the General Credit Reporting Principles published by the World Bank in September 2011 as a reference, the following is a diagnostic of the Peruvian microfinance sector.

General Principle 1: Data *(See definition in Annex 3)*

↘ **Guidelines on accuracy of data**

The information issued by the public credit registry and the credit bureaus is reliable. The complaints regarding accuracy are minimal. One factor that contributes to this level of accuracy is the strict validation by the supervisory agency responsible for the public credit registry, and where all of the institutions of the regulated financial system report. The forms are designed to collect information are easy for the MFIs to fill out.

Likewise, the credit bureaus have reliable validation systems and private contracts, where they require quality information. The few cases of mistakes come primarily from non-regulated MFIs and other reporting institutions with less robust information systems.

↘ **Guidelines on timeliness of data**

Data timeliness of the public credit registry and the credit bureaus is moderate⁵⁰. The information is usually updated on a monthly basis, which results in period of approximately fifty-five days in which there is a gap in information. This significantly affects the analysis of the debtor's credit risk and produces dissatisfaction among the users.

The information for the public credit registry (later distributed to the credit bureaus) is sent monthly as an annex to the balance sheet. It should be sent after being validated by reporting institutions within a maximum timeframe of 15 calendar days after the end of the month. Among the countries studied, the Bolivian supervisory agency takes less time, but allows only two business days to receive the information.

Then, the Peruvian supervisory agency performs strict validation processes and makes the information available to the credit bureaus eight days later. The credit bureaus take one or two days to process and make the information available to the MFIs. For example, until May 25, information was available only from as late as March 31, 2012.

The lack of information timeliness limits credit analysis in the microfinance sector considering that Peru is a strong competitive market where the debtors have quick access to loans of small amounts without guarantees from various MFIs.

The supervisory agency and the credit bureaus are making efforts to reduce the information gap. For example, some MFIs report to credit bureaus weekly with negative information (debt in arrears).

⁵⁰ See "Scale" in the glossary.

Of the countries studied, Brazil provides a good example of timeliness, where negative information is reported online daily, making use of strong technology. This demonstrates the need for a greater use of information technology in the Peruvian financial system.

Some non-regulated MFIs do not have robust automatic processes, rather they have manual processes and dedicated personnel for reporting, resulting in additional efforts by credit bureaus due to more time spent on the validation process.

↘ **Guidelines on sufficient data – including positive**

The adequacy of information in the public credit registry and the credit bureaus in the country is good, though it is necessary to incorporate some important data for credit analysis.

The information reported is positive as all of the activities of the debtor are reported, whether they were punctual in paying their debts or not.

A positive factor is the report on the credit amounts from one sol (approx. US\$0.33), which is commendable given it makes information on even small loans to MFIs.

Unlike the other public credit registries, where the amount of information is minimal, the Peruvian supervisory agency excels in providing the credit bureaus with large amounts of information from all the regulated institutions' debtors. Furthermore, it is the only one in the countries studied that provides the entire databases of regulated institutions and some public institutions, making Peru the only country studied where there is "alignment" of the debtor's rating⁵¹ (i.e. the debtor ranking given their credit situation within all of the financial system.) This practice reduces systematic risk and costs to the institutions. In the other countries, the regulated financial institutions can only make queries about individuals through the website, therefore alignment cannot take place.

Mexico and Peru are the only two countries studied where the credit bureaus include information about tax debt in credit reports, which is useful in credit analysis.

Despite having important information, it is necessary to include some additional information to expand the credit risk analysis. Among them:

1. Original loan amount.
2. Balance in default.
3. Quota amounts.
4. Frequency of payments.
5. Loan term.
6. Methodology type (group or individual).
7. Group balance for group loans (only shows individual balance)
8. Information from public service companies, such as water and electricity.

To incorporate this data, there are no legal limitations, only technical limitations of the MFIs and the supervisory agency, as well as the State institutions' decision to provide information.

⁵¹ In the Dominican Republic, the supervisory agency performs internal debtor alignment but does not provide the databases to the regulated institutions.

↘ **Guidelines on collection of data on a systematic basis from all relevant and available sources**

Information collection by the credit bureaus is good. After receiving information from the public credit registry, the credit bureaus independently collect information on the non-regulated MFIs, commercial stores, and companies such as telephone, cable etc., all through private agreements.

Copeme⁵² and Equifax have had an agreement since 1998 with the aim of including a larger number of non-regulated MFIs in the credit bureaus. Initially, the agreement included reporting exclusively to Equifax. Despite the fact that now the majority of MFIs report to various credit bureaus, there are various cooperatives that are not reporting to any of them. This is also the case with other loan providers, such as pawn shops, loan providers to the non-financial sector, etc.

Currently, the supervisory agency has been working on a pilot program to evaluate the feasibility of non-regulated MFIs and savings and loan cooperatives reporting to the public credit registry, with the goal of all credit bureaus having information on the regulated and non-regulated financial system to reduce over-indebtedness risk.

In this case, the main difficulties of some institutions are technical and qualified personnel in the area of information systems. Usually, the small non-regulated MFIs are not the owners of the information systems, instead using external providers. As a result, they are not able to make internal changes required by the supervisory agency and to make requests to a providers is a significant investment. Furthermore, the database provided by the public credit registry is massive and requires computers with ample capacity to back it up and manage it.

On the other hand, there is a project being carried out by Copeme and Equifax focused on the rural sector, whose objective is to bring together irrigation councils, seed and insecticide providers, crop production associations, etc. that are important and could influence the evaluation of rural credit risk.

There are still idiosyncrasies of some non-regulated credit providers (among them many cooperatives), who do not report to the credit bureaus because of fear of losing their debtors.

There is no banking privacy for lending transactions in Peru. However, the risk of unfair competition is mitigated by the decision of the credit bureaus to not share information that encourages this type of behavior among financial institutions.

↘ **Guidelines on retention of data**

Retention of information in the public credit registry and credit bureaus is moderate.

The public credit registry keeps unpaid debt information indefinitely. Unpaid debts that are no more than five years old may be reported to the credit bureaus. The disparity among retention times of this debts forces financial institutions to consult both sources. In addition, the records of cancelled debt in the credit bureaus only show debt for up to two years. This period is extremely short in comparison to other countries, which show cancelled debt history for five years.

⁵² The Consortium of Private Organizations Promoting Small and Microenterprise Development.

General Principle 2: Data Processing: Security and Efficiency

(See definition in Annex 3)

↘ Guideline on security measures

Data security measures in the credit reporting system are good. There are strict information security measures for regulated MFIs, out of which came the requirement that the supervisory agency have an information security officer.

Despite the existence of a credit bureaus law with standards regarding important aspects of information security, there is not a supervisory agency to ensure compliance. However, these credit bureaus have strong internal controls and enforce them on their reporting institutions through service contracts, which include minimum controls to ensure information quality and continuity.

Given their nature, a supervisory agency that controls information security for non-regulated MFIs does not exist, but the Peruvian microfinance sector is, for the most part, regulated.

↘ Guideline on reliability

The public credit registry within the country and credit bureaus service is reliable.

In general, the service is continuous. The internet connection is good, largely in the urban areas, and the security measures in the public credit registry and credit bureaus allow this level of service.

↘ Guideline on efficiency

The credit bureau service is good. The prices per query are the lowest among the countries in this study.

The most common way to access credit reports is online through the credit bureaus' webpage. The physical delivery of information is also available.

The participation of five credit bureaus in the country has resulted in improved services for users, including the creation of specialized microfinance units.

There is strong price competition, which has resulted in a range of US\$0.10 to US\$0.70 per query (the average of the countries studied is US\$1.00).

An agreement between Copeme and Equifax resulted in lower prices for non-regulated MFIs. At the beginning of the project, the prices were almost 50% of the norm, but required exclusive reporting to the credit bureau offering the discount. This initial exclusivity caused Equifax to dominate the microfinance market. Now, the consultation prices are higher than their competitors (but lower than that of other countries).

In Nicaragua, regulations prohibit exclusive contracts to avoid the predominance of a single credit bureau.

On the other hand, the Sentinel credit bureau made an agreement with another MFI network to achieve a greater volume of group queries, without requiring exclusivity. This has resulted in prices as low as US\$0.06 per debtor per month (indefinite queries in the month). This price is the lowest in the countries studied.

General Principle 3: Governance and Risk Management *(See definition in Annex 3)*

↘ **Guideline on accountability of governance arrangements**

Despite the existence of a credit bureau law, Peru is one of a few countries in this study, where the credit bureaus are not supervised. The risk of irresponsibility by third parties is mitigated due to the fact that some of them belong to an international credit bureau. In addition, the credit bureaus are accountable to the government organization for consumer protection (Indecopi), which monitors compliance of these standards.

↘ **Guideline on transparency of governance arrangements**

The transparency of the credit bureaus regarding their businesses is good, although they do not publish information regarding their shareholder composition.

Generally, the credit bureaus have websites where they describe their business, products, and consumer complaint systems. However, there is not enough information regarding the ownership of these companies, limiting transparency.

The law does not prohibit ownership by financial institutions in credit bureaus. In this context, there are two banks that are minority owners in Equifax (Banco Crédito del Perú and Scotia Bank).

↘ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

Despite the existence of a credit bureau law, they are not supervised and do not have regulations related to risk management that must be met before the supervisory agency. However, there are strong organizations that have strict information protection measures.

↘ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

All users have equal access to information in the credit bureaus.

The fact that the dominant credit bureau (Equifax) has two big banks as shareholders has apparently not resulted in evidence showing conflicts of interest in accessing information.

General Principle 4: Legal and Regulatory Environment *(See definition in Annex 3)*

↘ **Guidelines on clarity and predictability**

There are legal regulations related to credit bureaus which are clear for the participants in the credit reporting system. Furthermore, there is clarity about the consequences in case of noncompliance. The supervisory agency and the government organization in charge of consumer protection are strict in enforcing the compliance of laws and corresponding sanctions.

Among the countries studied, Peru excels in the dissemination of standards. There are great efforts made by the government and the MFIs to educate consumers about their rights and data protection in accordance with current regulations. Various means visible to the debtors are utilized. In the offices of the regulated institutions, videos and posters are used; as well as mass media, such as radio and television.

However, more information is still necessary, primarily in the non-regulated system, which is evident due to the lack of compliance with certain rules and debtor complaints due to lack of knowledge.

▾ **Guidelines on non- discrimination**

All reporting institutions and credit bureau users have the same legal obligations.

The reciprocity principle is followed in the credit bureaus, where only the institutions that report have access to consultations.

▾ **Guidelines on proportionality**

The current regulations have moderate proportionality and balance.

The standards can be fulfilled by all members of the credit reporting system and penalties from the authorities in case of noncompliance are reasonable.

However, the fact that the information on canceled debt is only available for up to two years excessively protects the debtor and disfavors the financial institutions since the most important information in the credit analysis (payment behavior of the debtor) is removed. In general, the countries studied display canceled debt information for five years.

Likewise, the banking privacy in Peru only exists for borrowing transactions. Consequently, approval by the debtor is not required to report or use lending transaction information. This represents a potential risk for consumer data protection.

▾ **Guidelines on consumer rights and data protection**

There are sufficient rules on data protection and consumer rights in Peru.

The rules include the debtor's minimum rights, including being informed about the purpose of information collection, processing, and distribution, as well as periodically accessing their information and making complaints.

▾ **Guidelines on dispute resolution**

There are legal mechanisms to address consumer complaints in the regulated and non-regulated system. In general, consumers exercise their rights. Complaints are minimal, demonstrating the accuracy and reliability of the information.

Since the authorities are strict in monitoring rule compliance, the MFIs are complying with processing debtor complaints within established timeframes. .

CONCLUSIONS

This section organizes conclusions according to the principles outlined in the body of this report:

General Principle 1: Data

- ▶ The information issued by the public credit registry and the credit bureaus is reliable. The complaints due to accuracy are minimal.
- ▶ The timeliness of the public credit registry and the credit bureaus is moderate. Information is generally updated on a monthly basis, which results in a gap of information of approximately fifty-five days.
- ▶ There are technical limitations of the regulated and non-regulated institutions, as well as of the regulatory agency, which jeopardize the timeliness of the information.
- ▶ Data adequacy in the public credit registry and the credit bureaus is good, but it is necessary to incorporate some additional important information for the credit analysis.
- ▶ Data collection in the country's credit bureaus is good, even though there is still a lack of participation, particularly by cooperatives and State organizations.
- ▶ Data retention in the public credit registry and credit bureaus is moderate.

General Principle 2: Data Processing: Security and Efficiency

- ▶ The information security measures in the credit reports of the Peruvian microfinance sector are good.
- ▶ There is excellent service reliability in the public credit registry and credit bureaus.
- ▶ The credit bureau service is efficient; the prices per query are the lowest among the countries in this study.

General Principle 3: Governance and Risk Management

- ▶ Despite the existence of credit bureau laws, Peru is one of the few countries in the study in which the bureaus are not supervised. This risk is mitigated because some of them belong to an international credit bureau.
- ▶ Transparency in the credit bureaus regarding their business is good, although they do not publish information regarding shareholder composition.
- ▶ Due to the fact that credit bureaus are not supervised, they do not have risk management standards to be fulfilled before the supervisory agency. However, the organizations are strong and have strict measures to protect information.
- ▶ All users have equal access to the credit bureau information.

General Principle 4: Legal and Regulatory Environment

- ▶ There are legal rules related to the credit bureaus, which are clear to the participants in the credit reporting system. The consequences in case of noncompliance are predictable. Information is well disseminated among consumers.
- ▶ All the reporting institutions and users of the credit bureaus have the same legal obligations.

- ▶ Within the current regulations in Peru, there is proportionality and balance.
- ▶ There are sufficient rules regarding data protection and consumer rights.
- ▶ In the regulated and non-regulated financial system, there are legal mechanisms to address consumer complaints. In general, consumers exercise their rights. The complaints are minimal, demonstrating the accuracy and reliability of the information.

RECOMMENDATIONS

This section classifies recommendations according to their type.

Legal

- ▶ Study the feasibility of incorporating banking privacy in lending transactions.
- ▶ In order to improve credit bureau responsibility before third parties, it is recommended that the feasibility of regulating them be studied.

Regulatory

- ▶ In order to improve data timeliness, it is recommended that the supervisory entity study the feasibility of increasing the frequency with which information is updated.
- ▶ To improve the transparency of the credit bureaus, a regular publication of their shareholder composition is recommended.
- ▶ Establish mechanisms that mitigate conflicts of interest that may arise from ownership by financial institutions of credit bureaus.
- ▶ Prohibit contracts, agreements, or exclusive practices that limit the reporting of information to only one credit bureau.

Techniques and training

- ▶ Provide technological resources to the financial system allowing for the daily processing of information; this would be a modest investment compared to positive impact that it would have on the healthy development of microfinance.
- ▶ To improve the awareness of the standards and benefits of the credit reports and increase the participation of the non-regulated credit providers and State entities, it is recommended that there be a greater distribution of information regarding the benefits of credit bureaus in the country.
- ▶ Despite having important information, it is necessary to incorporate additional information to expand credit risk analysis. Including:
 1. Original loan amount.
 2. Balances in default.
 3. Quota amount.
 4. Frequency of payment.
 5. Loan term.
 6. Methodology type (group or individual).
 7. Group balance for group loans (only the individual balance is shown).
 8. Information on public service businesses, such as water and electricity.

Dominican Republic

↘ EXECUTIVE SUMMARY

The Dominican microfinance sector has a very good credit reporting system. The considerable base of reporting institutions from the financial, non-financial, and public sectors is outstanding. The biggest challenge for the Dominican microfinance sector is to improve data timeliness.

Though the public credit registry does not share information with the credit bureaus, there is a strong culture of reporting by organizations with relevant information. Even more important is that many of the participants in the system report to both credit bureaus, though they may only consult one. The use of credit bureaus in the country extends even to renting and employment, a practice not normally seen in other countries in this study.

The microfinance sector is primarily not regulated (in number of MFIs). The largest NGO microfinance institutions report to the credit bureaus but there are still many credit providers to the low income population that do not. Though these are numerous, they represent a small percentage of the financial system's portfolio.

The large number of reporting institutions from diverse sectors allows the credit bureaus to compete with various products, but the cost is high in comparison with the average of the other countries included in this study.

The legal framework is clear, though it is poorly disseminated. Consumer claims from the regulated financial system are handled acceptably. However, the challenge remains to adequately attend consumers within the unregulated financial system.



UNDERSTANDING THE DOMINICAN MICROFINANCE SECTOR IN RELATION TO THE PUBLIC CREDIT REGISTRY AND CREDIT BUREAUS

The Dominican microfinance sector is large in number of MFIs (mostly unregulated), though only moderately competitive.

The regulated financial system is comprised of 16 full service banks, 29 savings and loan banks⁵³, 18 savings and loan associations (“mutuales”), and 18 loan corporations (“financieras”), in addition to exchange and remittance agents. Of all these institutions, only four large savings and loan banks are dedicated to microfinance. There are also full service banks that are beginning to enter the sector through specialized microfinance departments.

There are many loan providers that serve the low income segment of the population. They are estimated at more than 1,000, including MFIs and cooperatives.

There are only 20 MFIs are affiliated with Redomif⁵⁴. This network has only been in existence for a few years and has regulated and unregulated affiliates, as well as a network of cooperatives. It has been actively training its affiliates.

Stemming from the banking crisis of 2003, during which three large banks collapsed, there has been a more strict standardization for the financial sector. The supervisory entity has made significant advances in the sector’s transparency and in risk management regulation. Much information is required to comply with regulations, which are strictly monitored.

In addition to the public credit registry, there are two private credit bureaus: Transunion and Datacrédito, which are regulated by the supervisory body. Transunion’s headquarters is in Chicago (U.S.) and Datacrédito’s shareholders are Dominican. The first is more focused on the banking system and the second on all sectors, but with many reporting institutions from the microfinance sector.

There is a law specifically for the credit bureaus, which balances the rights of the consumers and the financial institutions. There is a government organism and a specialized unit within the regulatory body to monitor the law’s compliance.

Despite the credit bureaus’ recent entry into the country (approximately in the year 2000), the Dominican system has achieved a significant volume of reporting institutions, reaching a level comparable to Brazil, where credit bureaus were introduced in the 1950s. The credit bureaus have worked hard to incorporate a large number of reporting institutions. The Dominican Republic’s culture of reporting and using credit bureau information is impressive.

The public credit registry does not share information with the credit bureaus, but the financial and non-financial sectors report to the credit bureaus voluntarily, often to both bureaus though they may only consult one.

Datacrédito’s strong marketing efforts, which include sales representatives in every city, have identified approximately 1,000 small loan providers that do not report to the credit bureaus.

Despite the credit bureaus’ great achievements, the challenge remains to continue increasing the number of reporting institutions from the microfinance sector.

⁵³ Financial institutions that cannot offer foreign trade services or checking accounts.

⁵⁴ Dominican Microfinance Network.

ALIGNMENT OF THE DOMINICAN MICROFINANCE SECTOR TO THE WORLD BANK'S GENERAL PRINCIPLES FOR CREDIT REPORTING

Using the General Credit Reporting Principles published by the World Bank in September 2011 as a reference, the following is a diagnostic of the Dominican microfinance sector:

General Principle 1: Data *(See definition in Annex 3)*

↘ **Guidelines on accuracy of data**

The public credit registry and the credit bureaus' data accuracy is very good⁵⁵.

The supervisory entity manages the public credit registry, where all of the regulated financial system's institutions report. There are strict data validation processes, resulting in only minimal errors. Only regulated institutions can consult the information from the public credit registry.

These institutions also voluntarily and simultaneously report positive information (*see glossary*) to the credit bureaus, as do institutions in the unregulated financial, non-financial, and public sectors.

The data collection forms are easy to fill out. There are few errors, demonstrating that data accuracy is not sacrificed by reporting directly to the credit bureaus, as is thought in other countries such as Bolivia and Peru.

↘ **Guidelines on timeliness of data**

The credit bureaus' data timeliness is moderate. As data is typically updated monthly, there is an information gap of approximately 42 days. This significantly impacts the microfinance sector, where loans can be awarded within as little as 24 hours.

The credit bureaus collect positive information monthly (with a cutoff date of the 15th or the 30th of each month). These bureaus give less time to submit data than the public credit registry. As a result, their data is available more quickly, though still with a considerable time gap. For example, for institutions with a cutoff time at the end of the month, up until the 12th of May, information was only available from March 31st, 2012.

Some banks with strong technological capacity report all of their positive information more frequently than monthly, but they are few. Institutions that lack the technological capacity to report more frequently are limited in this regard. Also, given that the majority of MFIs' loans have monthly payments, there has not been pressure on their part to report data more frequently.

In contrast, Mexico -with a greater number of MFIs providing group loans with weekly payments- mostly updates information on a weekly basis. Further, Brazil updates negative information daily, achieving the record for data timeliness among the countries studied.

⁵⁵ See "Scale" in the glossary.

The public credit registry updates information monthly, though with a greater delay than the credit bureaus.

As with the other countries studied, data timeliness in the Dominican Republic can be mitigated by consultation of the debtor's loan request footprint, but the service is expensive. These registries include the debtor's loan request attempts in other institutions during the data gap. The information is offered by the credit bureaus as an option in addition to a regular credit report though, given the high cost, it is generally not used by the MFIs.

Regarding the debtor, the absence of a loan request footprint in the credit reports prohibits them from verifying if there are businesses requesting their information without their approval.

↳ **Guidelines on sufficient data – including positive**

The credit bureaus' data sufficiency is very good. The amount of information from the financial, non-financial, and public sectors is impressive. However, it is still necessary to incorporate additional important data to improve credit analysis.

Positive information is reported, meaning all of the debtor's activity, whether they make punctual payments or not. This is obligatory in contracts provided by the credit bureaus, though not by law.

Loans are reported from one Dominican peso (approximately US\$0.025), which is laudable given that it provides MFIs with information on debtor's with even the smallest loans.

Credit reports contain ample information. The detail and information analysis is outstanding, including necessary data for the microfinance sector, such as the quota amount, electricity and water payments, etc.

The good data sufficiency is achieved by the high participation of reporting institutions that report to both credit bureaus (See Guidelines on collection of data on a systematic basis from all relevant and available sources), making credit bureaus compete on data quality and analysis.

Within this study, only credit reports from Brazil and the Dominican Republic present information on basic services such as water and electricity, which is useful information in microcredit analysis. Further, Mexico, Nicaragua, and the Dominican Republic are the only countries with data on criminal proceedings.

There is a lot of information from the non-financial and public sectors. The most relevant information, which is not seen in other countries, includes information on pharmacy debts, traffic violation fines, etc. However, tax debt information is not available due to legal limitations.

The information provided by the public credit registry is rather basic, and far from the level of detail provided by the credit bureaus. It only shows information consolidated by product, without individually detailing debt by financial institution. It is expected that more information will be provided in the coming months.

Though the credit bureaus provide ample information, it would be useful to have the following additional information in order to improve credit analysis:

1. Frequency of payments.
2. Loan term.
3. Loan type.
4. Debtor classification (only shown in the public credit registry).
5. Collateral.
6. Name of guarantor.
7. Tax debt.

↘ **Guidelines on collection of data on a systematic basis from all relevant and available sources**

The credit bureaus' data collection is very good. There is high participation from organizations in the financial, non-financial, and public sectors with relevant information. The largest MFIs and most of those affiliated with Redomif report to the credit bureaus, though there are many small MFIs that do not.

It is not obligatory for any institution to report to credit bureaus, regulated or not. In contrast with other countries, the culture of reporting and consulting with credit bureaus is very good. The reporting to both credit bureaus is outstanding even though only one is often consulted.

All of this has been achieved by the private work of the credit bureaus, which arduously worked for these accomplishments since their creation. Currently, Datacrédito has 50 salespeople (distributed in different cities), a high number given the size of the country. This bureau also has a department dedicated only to microfinance. Continuing visits to the MFIs is appreciated by the reporting institutions, who also contribute suggestions for product improvements.

The majority of NGOs and cooperatives affiliated with Redomif report to and use credit bureaus. However, there are still many credit providers to the low income population that do not report for fear of losing their borrowers. Though these institutions are great in number, they represent only a small percentage of the financial system.

↘ **Guidelines on retention of data**

Data retention in the public credit registry and credit bureaus is good, though relatively excessive. The public credit registry stores unpaid debt for 10 years and the credit bureaus keep it indefinitely until it is cancelled by the debtor, or until it is reported by the financial institutions. Mexico's timeframe for keeping this data is 6 years, which appears more acceptable as it allows the debtor the possibility to reinsert themselves into the financial system.

The credit bureaus can maintain cancelled debt history for up to 7 years. This period is also relatively long compared with the other countries studied, which maintain this information for five years.

General Principle 2: **Data Processing: Security and Efficiency** *(See definition in Annex 3)*

↘ **Guideline on security measures**

Security measures in the Dominican microfinance sector's credit reporting system are moderate given that the sector is largely unregulated.

There are strict data security measures and on site supervision for regulated MFIs.

Though the supervisory body monitors the credit bureaus, the data security supervision is minimal. The credit bureaus follow their own internal regulations. Transunion is governed by the security standards set by its headquarters in Chicago.

Given their nature, there is no supervisory agency to control security measures in unregulated MFIs, which constitutes a large gap considering that there are many of them in comparison with the regulated MFIs.

↘ **Guideline on reliability**

Credit bureau service in the Dominican Republic is reliable.

Generally, the service is continuous; the few instances where it has been interrupted have been for internet connection problems.

↘ **Guideline on efficiency**

The credit bureaus' service is very good despite their prices being rather high compared to the other countries in this study.

Given that the majority of the reporting institutions provide information to both credit bureaus, the bureaus compete on diversity of services and price.

The credit bureaus offer various standard services for all of the financial system. They also offer personalized services for the institutions according to agreements, such as credit prequalification, alerts, scores, etc.

The most common channel to access credit reports is online through the credit bureaus' websites.

The credit bureaus' price per query (on average US\$2) is high in comparison with the other countries in this study (whose average price is US\$1). However, the price is reduced significantly according to the number of consultations, reaching as low as US\$0.50 per query.

Transunion's service is much more expensive than that of Datacrédito. As such, most MFIs use Datacrédito's services, resulting in a predominance of this credit bureau within the microfinance sector.

The public credit registry's service for the regulated institutions is free. The supervisory body does not provide the public credit registry's information to the credit bureaus, as is the case in some of the other countries in this study. As a result, credit bureaus must make efforts to collect this information individually on a national level, increasing their operating costs.

General Principle 3: **Governance and Risk Management** (*See definition in Annex 3*)

↘ **Guideline on accountability of governance arrangements**

The credit bureaus respond acceptably to third parties. The organizations are well structured and accountable towards the supervisory agency. Additionally, Transunion is responsible to its foreign headquarters.

Annex 1 **Dominican Republic**

↘ **Guideline on transparency of governance arrangements**

The credit bureaus' transparency regarding their businesses is good, though they do not publish their shareholder composition.

The credit bureaus generally describe their business, products, and debtor claim system on their website.

↘ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

There is a regulation regarding risk management of the credit bureaus enforced by the supervisory body, which mitigates business risks.

↘ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

All users have the same rights to access information from the credit bureaus.

The credit bureau law in the country prohibits financial institutions from holding shares in credit bureaus.

General Principle 4: **Legal and Regulatory Environment** *(See definition in Annex 3)*

↘ **Guidelines on clarity and predictability**

There are sufficient legal regulations related to credit bureaus in the Dominican Republic. These regulations and the consequences in case of noncompliance are clear, though there have been few efforts by the authorities to educate consumers about them. Rather, the credit bureaus have made efforts to share this information with consumers, publishing it on their websites and thereby promoting effective consumer education.

Among the countries studied, Peru excels in the dissemination of standards. There are great efforts made by the government and the MFIs to educate consumers about their rights and data protection in accordance with current regulations. Various means visible to the debtors are utilized. In the offices of the regulated institutions, videos and posters are used; as well as mass media, such as radio and television.

↘ **Guidelines on non-discrimination**

It appears that there is no discrimination within the credit bureaus. All users have the same right to report and use data.

The reciprocity principle is respected, where only institutions that report may consult information.

↘ **Guidelines on proportionality**

In the country's existing norms, there is proportionality and balance. Consumers are protected and financial institutions have sufficient information to perform a credit risk analysis.

All of the participants in the credit reporting system can comply with the regulations.

↘ **Guidelines on consumer rights and data protection**

There are sufficient regulations regarding data protection and consumer rights in the regulated financial sector. However, these regulations are perceived to be insufficient, or unknown, for the unregulated financial system.

The regulated financial system's norms include minimal debtor rights, such as to be informed about the reasons for data collection, processing, and distribution, as well as periodic access to their information and the ability to make claims.

There is banking privacy for lending and borrowing transactions. Consequently, authorization from the debtor is required to report and consult their information.

↘ **Guidelines on dispute resolution**

Consumer claims are resolved acceptably by regulated financial institutions, credit bureaus, and the supervisory body responsible for monitoring these regulations. However, consumer in the unregulated financial system are not attended to with the same effectiveness by the government's consumer protection agency.

Debtor claims are resolved in a timely manner through effective processes in the regulated financial system and the regulatory body has a specialized consumer protection unit; however, there have been few claims given the limited diffusion of regulations.

On the other hand, there is room for improvement in attending consumers in the unregulated financial system. There is a consumer attention organization⁵⁶ that attends to the rest of the economy's sectors, including those of the unregulated financial system. The participants' perception is that claims are not attended in an effective manner.

Within the studied countries, Peru stands out in this area, as they oblige each financial institution to have an independent unit to receive and process consumer claims with strict policies and timeframes. Financial consumers have the ability to appeal to the government's consumer protection organization or to the regulatory body's specialized unit for a second occurrence. The established penalties are rigorously applied.

⁵⁶ Consumer Protection.

CONCLUSIONS

This section organizes conclusions according to the principles outlined in the body of the report:

General Principle 1: Data

- ▶ The credit bureaus' data accuracy is very good.
- ▶ The credit bureaus' data timeliness is moderate. As data is typically updated monthly, there is an information gap of approximately 42 days. This significantly impacts the microfinance sector, where loans can be awarded within as little as 24 hours.
- ▶ There are technological limitations for some regulated and unregulated institutions, reducing data timeliness.
- ▶ The credit bureaus' data sufficiency is very good. The amount of information from the financial, non-financial, and public sectors is impressive. However, it is still necessary to incorporate additional important data to improve credit analysis.
- ▶ The credit bureaus' data collection is very good. There is high participation from organizations in the financial, non-financial, and public sectors with relevant information. The largest MFIs and most of those affiliated with Redomif report to the credit bureaus, though there are many small MFIs that do not.
- ▶ Data retention in the public credit registry and credit bureaus is good, though relatively excessive.

General Principle 2: Data Processing: Security and Efficiency

- ▶ Security measures in the Dominican microfinance sector's credit reporting system are moderate given that the sector is largely unregulated.
- ▶ Credit bureau service in the Dominican Republic is reliable.
- ▶ The credit bureaus' service is very good despite their prices being rather high compared to the other countries in this study.

General Principle 3: Governance and Risk Management

- ▶ The credit bureaus respond acceptably to third parties.
- ▶ The credit bureaus' transparency regarding their businesses is good, though they do not publish their shareholder composition.
- ▶ There is a regulation regarding risk management of the credit bureaus enforced by the supervisory body, which mitigates business risks.
- ▶ All users have the same rights to access information from the credit bureaus.

General Principle 4: Legal and Regulatory Environment

- ▶ There are sufficient legal regulations related to credit bureaus in the Dominican Republic. These regulations and the consequences in case of noncompliance are clear, though there have been few efforts by the authorities to educate consumers about them.
- ▶ It appears that there is no discrimination within the credit bureaus. All users have the same right to report and use data.
- ▶ In the country's existing norms, there is proportionality and balance. Consumers are protected and financial institutions have sufficient information to perform a credit risk analysis.
- ▶ There are sufficient regulations regarding data protection and consumer rights.
- ▶ Consumer claims are resolved acceptably by regulated financial institutions, credit bureaus, and the supervisory body responsible for monitoring these regulations. However, consumer in the unregulated financial system are not attended to with the same effectiveness by the government's consumer protection agency.

RECOMMENDATIONS

This section classifies recommendations according to their type:

Regulatory

- ▶ In order to improve data timeliness of the public credit registries, it is recommended that the supervisory entity study the feasibility of increasing the frequency with which information is updated.
- ▶ It is recommended that consumer protection norms be diffused by financial institutions through effective channels.

Government Policy

- ▶ Diffuse consumer rights and obligations related to credit bureaus through effective public channels.

Techniques and training

- ▶ With the goal of improving data timeliness, it is recommended that Redomif motive affiliate MFIs to increase the frequency with which they report to the credit bureaus. Banco Ademi is a good example, where data is sent bi-weekly.
- ▶ Provide technological resources to the financial system allowing for the daily processing of information; this would be a modest investment compared to positive impact that it would have on the healthy development of microfinance.
- ▶ To increase participation of a greater number of unregulated loan providers in credit bureaus, more training and informing about the benefits provided by credit bureaus in the reduction of credit risk is recommended.
- ▶ To mitigate the lack of data timeliness in the microfinance sector, it is recommended that the credit bureaus include the “loan request footprint” in their regular credit reports.
- ▶ Though the credit bureaus provide much information, it would be useful to have the additional following information to improve credit analysis:
 1. Payment frequency.
 2. Loan term.
 3. Type of loan.
 4. Debtor classification (only shown in the public credit registry).
 5. Collateral.
 6. Name of guarantor.
 7. Tax debt.

COMPARATIVE ANALYSIS OF THE ANALYZED COUNTRIES' ALIGNMENT TO THE WORLD BANK'S GENERAL CREDIT REPORTING PRINCIPLES⁵⁷

REPORTING FROM THE WORLD BANK	COUNTRIES	Bolivia	Brazil	Colombia	El Salvador	Guatemala	Mexico	Nicaragua	Peru	Dom. Rep.
General Guideline 1: Data										
↳ Guidelines on accuracy of data	**	****	****	***	*	**	**	*****	*****	
↳ Guidelines on timeliness of data	**	*****	***	**	*	****	**	**	**	**
↳ Guidelines on sufficient data – including positive	**	*	***	**	*	**	**	****	*****	
↳ Guidelines on collection of data on a systematic basis from all relevant and available sources	****	*****	**	**	*	**	***	****	****	
↳ Guidelines on retention of data	****	*	***	**	*	*****	***	**	****	
General Guideline 2: Data Processing: Security and Efficiency										
↳ Guideline on security measures	***	****	**	**	**	**	**	****	**	
↳ Guideline on reliability	*****	*****	*****	*****	**	*****	****	*****	*****	
↳ Guideline on efficiency	****	****	***	**	**	***	**	*****	***	
General Guideline 3: Governance and Risk Management										
↳ Guideline on accountability of governance arrangements	****	**	***	***	**	****	***	**	***	
↳ Guideline on transparency of governance arrangements	*****	***	***	***	*	***	***	***	***	
↳ Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business	***	***	***	***	*	***	***	***	***	
↳ Guideline on effective governance arrangements ensuring that all users have fair access to information	****	*****	*****	*****	***	***	*****	*****	*****	
General Guideline 4: Legal and regulatory environment										
↳ Guidelines on clarity and predictability	***	*****	***	**	*	***	**	*****	***	
↳ Guidelines on non-discrimination	**	*****	*****	*	*	*****	*****	*****	*****	
↳ Guidelines on proportionality	***	*****	****	**	*	**	**	**	*****	
↳ Guidelines on consumer rights and data protection	**	*****	*****	***	*	*****	**	*****	****	
↳ Guidelines on dispute resolution	**	*****	****	**	**	**	*	*****	***	

⁵⁷ The scale includes 5 stars as the highest grade of alignment to the principle, and one star as the lowest.

GENERAL PRINCIPLES FOR CREDIT REPORTING FROM WORLD BANK

The principles and guides for the credit reporting system are outlined in the document published by the World Bank in September 2011. This study only contains 4 (of 5) principles.

General Principle 1: Data

Credit reporting systems should have accurate, timely and sufficient data - including positive - collected on a systematic basis from all relevant and available sources, and should retain this information for a sufficient amount of time.

▾ Guidelines on accuracy of data

Data collected and distributed should be, to the extent possible, free of error, truthful, complete and up to date.

To ensure that data accuracy is achieved on a continuous basis, credit reporting system participants should consistently apply appropriate data-supplying rules and procedures to all data providers with similar characteristics.

▾ Guidelines on timeliness of data

Credit reporting service providers and data providers should apply clear and detailed rules for the updating of information. Such rules should ensure that updates be performed on the basis of pre-defined schedules and/or specific trigger events. At a minimum, this should include prompt action in the event of error adjustments and ideally in case of relevant changes in credit exposures, arrears, fraud, defaults and bankruptcies.

Data should be available for users of the credit reporting system in a prompt manner to enable them to carry out their functions without unnecessary delays.

↘ Guidelines on sufficient data – including positive

Credit reporting service providers should be able to collect and process all the relevant information needed to fulfill their lawful purposes. Relevant information comprises both negative and positive data, as well as any other information deemed appropriate by the credit reporting system, consistent with the considerations described in the other General Principles.

Credit reporting service providers should set up clear rules on minimum data inputs and optional data inputs. Data elements to be collected should include, at a minimum: identification information, information on the credit including original amount, date of origination, maturity, outstanding amount, type of loan, default information, arrears data and transfer of the credit when applicable. Ideally this would also include credit risk mitigation instruments such as guarantees, collateral and an estimate of their value.

↘ Guidelines on collection of data on a systematic basis from all relevant and available sources

Credit reporting service providers should be able to gather information from all relevant data providers, within the limits established by the law.

Credit reporting service providers should be able to access other data sources of relevance, within the limits established by the law.

↘ Guidelines on retention of data

Data collected by credit reporting systems should be available to users for a period of time that is consistent with the purpose for which the data is used.

Clear rules should be in place regarding the method to determine the specific date or event when distribution of data should be discontinued.

General Principle 2: Data Processing: Security and Efficiency

Credit reporting systems should have rigorous standards of security and reliability, and be efficient.

↘ Guideline on security measures

Credit reporting system participants should protect data against any loss, corruption, destruction, misuse or undue access.

↘ Guideline on reliability

Credit Reporting Service providers should implement appropriate business continuity measures to ensure that their services will be available to users without any significant disruptions.

↘ **Guideline on efficiency**

Credit reporting service providers should strive to be efficient both from an operational as well as from a cost perspective, while continuing to meet users' needs and high standards for service levels.

General Principle 3: Governance and Risk Management

The governance arrangements of credit reporting service providers and credit reporting data providers should ensure accountability, transparency and effectiveness in managing the risks associated with the business and fair access to the information by users.

↘ **Guideline on accountability of governance arrangements**

Credit reporting service providers and credit reporting data providers should be subject to mechanisms that ensure proper accountability of management and, where applicable, of board members. This should include independent audits or reviews.

↘ **Guideline on transparency of governance arrangements**

Governance arrangements for credit reporting service providers and credit reporting data providers should ensure timely and accurate disclosure of relevant matters related to the entity and its activities.

↘ **Guidelines on the effectiveness of governance arrangements in ensuring appropriate management of the risks associated with the business**

The management of credit reporting service providers and data providers should identify all relevant risks faced by the organization. The outcomes of this risk analysis should be reported periodically to the organization's top governing body.

To properly address and mitigate risks, credit reporting service providers and credit reporting data providers should establish sound internal controls and risk management mechanisms.

↘ **Guideline on effective governance arrangements ensuring that all users have fair access to information**

Governance arrangements of credit reporting service providers should promote all users having access to information under equitable conditions. This objective should not be affected by the ownership structure of the service provider.

General Principle 4: Legal and Regulatory Environment

The overall legal and regulatory framework for credit reporting should be clear, predictable, non-discriminatory, proportionate and supportive of data subjects and consumer rights. The legal and regulatory framework should include effective judicial or extrajudicial dispute resolution mechanisms.

↘ Guidelines on clarity and predictability

The legal and regulatory framework should be sufficiently precise to allow service providers, data providers, users and data subjects to foresee the consequences that their actions may entail.

The terminology used throughout the legal and regulatory framework, including the rules and other norms, should be consistent at the domestic level.

Public awareness of the laws and rules of credit reporting operations contributes to the clarity and predictability of the legal and regulatory framework.

↘ Guidelines on non- discrimination

Data supplying and data access should be established in a fair manner, responding to impartial rules regardless of the nature of the participants.

Obligations on data quality, security measures and consumer rights should be equally applicable to all credit reporting service providers, data providers and users.

↘ Guidelines on proportionality

The legal and regulatory framework should not be overly restrictive and burdensome relative to the possible issues it is designed to tackle.

Laws and regulations should be practical and effective as to ensure a high degree of compliance.

↘ Guidelines on consumer rights and data protection

Rules regarding the protection of data subjects/consumers should be clearly defined. At the minimum these rules should include:

- i) the right to object to their information being collected for certain purposes and/or used for certain purposes:
- ii) the right to be informed on the conditions of collection, processing and distribution of data held about them.
- iii) the right to access data held about them periodically at little or no cost:
- iv) the right to challenge the accuracy of information about them.

The legal and regulatory framework for credit reporting should address all relevant issues related to data subjects' privacy, especially if such issues are not covered by a personal data protection law or other similar law.

↘ Guidelines on dispute resolution

The process for solving disputes should be established in the law(s) governing credit reporting activities or in substantive regulations when such laws do not exist.

Credit reporting service providers and data providers should flag to all users cases where data subjects are involved in a dispute with the data provider in connection with the subject's data.

Annex 3

Credit reporting service and data providers should cooperate in reaching an expeditious solution to disputes.

The legal framework should provide suitable enforcement mechanisms, including redress for data subjects harmed.

- ▶ **Buró de crédito:** prCredit bureau: service provider whose primary objective is to improve the quality and availability of data to make credit decisions, consolidating data from different credit providers and other sources.
- ▶ **Public credit registry:** service provider whose primary objective is to assist in the supervision of the regulated financial system and improve the quality and availability of data from regulated financial institutions in order to improve the quality of their loan portfolios.
- ▶ **Consultation:** investigation of a natural or legal person by a credit provider or other natural or legal person, using information from credit bureaus or public credit registries.
- ▶ **Consumer:** see Information holder.
- ▶ **Credit Scoring:** statistical method to evaluate the probability of a potential borrower's completion with respect to their financial obligations associated with a loan.
- ▶ **Debtor:** natural or legal person that has a financial obligation with a credit provider.
- ▶ **Supervisory entity:** government organism that regulates the regulated financial system. In some countries, it is a superintendence and in others the Central Reserve Bank performs these functions.
- ▶ **Scale:** MicroRate used a five level scale for this study: Excellent, Very good, Good, Moderate and Weak.
- ▶ **Negative Information:** information regarding defaults or arrears and bankruptcy. It can also include information on lawsuits, liens, and judgments obtained by courts or other official sources.
- ▶ **Positive Information:** information regarding the level of compliance with a contract. It includes detailed information on outstanding loans, loan amounts, payment patterns, assets and liabilities, as well as guarantees or collateral. The extent to which positive information is collected depends on the national legislation, including the data protection regulation. For the purposes of this report, when "positive information" is mentioned, it also includes "negative information."
- ▶ **Microfinance institution (MFI):** organization that provides microfinance services and whose loan operations are primarily microcredit.
- ▶ **Microcredit:** loans of small amounts used for productive purposes, where the decision to offer the loan is not predominantly based on collateral.
- ▶ **Microfinance:** basic financial service offerings, such as microcredit, savings, money transfers, and microinsurance to low income individuals or those with limited access to financial services. The transaction amounts are relatively small.
- ▶ **Credit reporting system participant:** any natural or legal person that takes part in one or more of the steps in the cycle of collecting, saving, processing, distributing, and finally using information to support lending decisions and financial supervision.

⁵⁸ This glossary used the document "General Credit Reporting Principles," published by the World Bank in September 2011, as a reference. However, some terms were adjusted to the language commonly used in the Latin American financial sector.

- ▶ **Borrower:** see Debtor.
- ▶ **Data protection:** discipline with the objective of creating adequate security measures to prevent the misuse of individuals' personal information. It is comparable to consumer protection.
- ▶ **Credit provider:** someone who is owed a financial obligation. Also, a natural or legal person that is dedicated to the business of lending money or selling goods for which immediate pay is not required but where there is an obligation to pay in the future.
- ▶ **Credit provider to the low income segment of the population:** credit provider that attends the low income niche of the population with loans of small sizes, but not necessarily with a majority of productive credits as with MFIs (see Microfinance institutions). For example, cooperatives, pawn shops, appliance stores, etc.
- ▶ **Reciprocity:** mutual interchange of information.
- ▶ **Reporting institution:** credit providers or other institutions that provide information to public credit registries or credit bureaus proactively and in a structured manner.
- ▶ **Credit reports:** reports provided by public credit registries and credit bureaus with information about a natural or legal person regarding lending decisions.
- ▶ **Microfinance sector:** subsector of the financial system dedicated to microfinance.
- ▶ **Non-financial sector:** includes the commercial, service, and industrial sectors.
- ▶ **Credit reporting system:** includes institutions, individuals, norms, procedures, standards, and technology that enable relevant information flow for credit-related decisions.
- ▶ **Information holder:** natural or legal person whose information may be collected, processed, and provided to third parties in a credit reporting system.
- ▶ **User:** natural or legal person that uses public credit registries or credit bureaus or other related services, typically under predefined conditions and rules.



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