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# **Transparency in the Ugandan Microfinance Industry:**

**A Key to Sustainability**

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**AMFIU**

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## The Author

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# 1 What does transparency mean and why is it important?

## 1.1 Introduction

The rapid growth in the microfinance industry of Uganda offers opportunities to providers and consumers, but it also poses new challenges. On one hand, consumers are lacking information and good money management skills and thus are constrained in their ability to make informed choices. On the other hand, most MFIs have a capacity gap to direct the consumers on how best to access their services and to develop/deliver market-driven products respectively.

Transparency has been prevalent in literally every discussion on Microfinance in Uganda in the recent years. Yet, there is no other approach that has addressed it as directly and thoroughly as the Consumer Financial Education programme that AMFIU runs supported by European Union and DFID/FSDU. Consumer Financial Education is one of the three pillars of AMFIU transparency programme, the others being performance monitoring and institutionalized product and pricing comparisons. The performance monitoring system that is in the process of technical establishment will provide mainly financial ratios. Other elements of performance monitoring of both MFIs and consumers are complaint handling and credit reference, which are yet to be conceptualized under the AMFIU transparency programme. A national database on Microfinance Products and publishing total costs (interest rates and fees) will be addressed in 2008/9.

The purpose of this paper is to define transparency from the perspective of the microfinance industry and highlight the reasons why a growing industry needs to promote transparency in order to realize objectives of a market driven industry, knowledge sharing, making a choice and promoting rights and responsibilities. In addition the paper explains the reasons for institutionalizing transparency in the microfinance industry as well as the various efforts by the key players in its promotion.

## 1.2 Definition

Many people define or explain transparency in many ways. Some term it as being open, accountable, honest, truthful and trustful. The Chief Executive Officer of Mid North Private Sector Promotion Center explained it precisely as “seeing through a glass”.

Transparency is either of the above and it is crucial for any contractual arrangement. Transparency begins with us, our spouses in our homes, families and our institutions/ organizations that we serve. It touches every segment of our daily lives and is key if trust is to be sustained in any arrangement.

## 1.3 Transparency and Outreach

The microfinance industry is growing and hence becoming more customer-oriented in its design and delivery of financial services and products. Growing arrays of players now compete to provide financial services and products to the poor and the un-banked. Accordingly, it is not surprising that the voice of the micro-entrepreneur is growing louder and more insistent on asserting her rights as a consumer of financial products and services. However, in Uganda the current state of the relationship between the MFIs and the consumers is not yet very transparent.

Consumers as well as MFIs in most cases do not know that they have rights under the law of the country. Transparency enables MFIs and consumers understand their rights and obligations. By understanding their rights and obligations MFIs and their clients will go a long way in improving transparency in the microfinance industry. These amongst others include rights to information, dignified treatment, legal appeal, redress, and integrity. Understanding of rights and obligations enables both clients and MFIs to make informed decisions before going into any contractual arrangement.

As the range of financial products and services offered to the poor and the un-banked grows and the number and the diversity of providers of these services also increase, it is likely that the concerns about transparency will only intensify and raise issues relevant to marketing and customer relationship management that go beyond the delivery and collection of “traditional” micro-credit.

## 1.4 Transparency and Sustainability

Both Microfinance institutions and consumers have grown both in capacity as well as in number. They have diverse and potentially conflicting interests. These are potentially conflicting in the short run, and may even give incentive for unsound loan appraisal which is dangerous for both of them. In the long run, consumer and MFI interests are much more aligned. Although there is always a bias to evade

competition on the side of the MFI, a long-term strategy realizes such through high productivity rather than compromising quality (**table one**).

**Table 1: Different interests of consumers and MFIs**

Short term consumer interest	Short term MFI interest
Take small loans that meet immediate needs	Would want to give out big loan amounts
Get free from debt	Continue as a credit client and reduce drop outs
Shop around for the institution that responds to the immediate needs	“Lock-in” of customer, e. g. through quick disbursement without thorough appraisal
Lowest total cost of loan	Highest returns on services

Long term consumer interest	Long term MFI interest
Be transparent to avoid over-indebtedness	Be transparent on fees and interest rates to create trust, i. e. long-term relationship
Sustain a relationship of trust with the MFI to maintain easy access to services	Maintain a relationship of trust with the client to maintain good portfolio quality
Use different services to meet personal needs in the most effective way	Offer a variety of products
Shop around to be informed about the range of services and their best prices available in the market	Maximize efficiency and productivity in order to retain customers and increase the market share

Educating both MFIs and consumers has a role in building their capacity to formulate strategic goals for themselves, i.e. take the long-term perspective. It will also encourage them to become proactive, use information and resources to improve economic status, and for the latter to effectively use financial services corresponding to the former establishing demand-driven products.

## 2 Transparency in the Microfinance Industry

### 2.1 Contract Partners

In the microfinance industry transparency involves informing consumers of the importance of understanding and respecting loan contracts. The target of the MFIs basically constitutes clients who have low literacy levels and sometimes do not know how to read and write. This is a big challenge to MFIs as most of these people do not understand the contracts and as a consequence do not respect them. This is a major cause of default and for poor business relation between the consumers and MFIs - especially in case of repossession. The need to translate the contracts into local languages is of high importance as well as simplification and a standardization of contracts for all MFIs. The implication of a guarantor to the contract is also not well understood and needs deeper explanation to both the consumer and the guarantor.

### 2.2 Costs

It is AMFIU’s aim to ensure MFIs and consumers are transparent in the way they conduct business with each other. Currently most MFIs do not disclose total costs of the services they offer. Interest rate calculation is also another issue of concern. The commonly used methods of interest rate calculation include flat rate and declining rate. AMFIU research among the leading MFIs showed that many of them do neither share their interest rates nor the method of calculation, and most do not inform openly about their other fees (Schmidt 2007).

Most consumers are not at the same level of understanding with MFI staff. Despite the fact that some MFIs provided tariff guides of the cost of the products and services to consumers. In addition consumers need explanation of the guides along the challenges discussed in the previous section. Display and explanation on how total costs of the services are arrived at is key in promoting trust and choice in the microfinance industry.

## 2.3 Products

Transparency enables consumers understand the various choices at their disposal and use them wisely as they demand for financial services. Previous research and studies in Uganda show that consumers are not properly guided when they have to make a choice amongst institutions or products.

Transparency in Uganda's MFI industry is key in order to empower consumers who seek for information relevant for decision-making. At the same time, it entails educating customers of MFIs fulfill their obligations to financial institutions. Information on what MFIs offer is not easily accessible to the consumers. One of the few surveys in this regard was done by AMFIU in November 2006 (Schmidt 2007). Under AMFIU transparency programme, set-up of a national database on Microfinance products is envisioned for 2008. Knowledge sharing via consolidated product data analysis gives the customer the necessary information to enable them make informed decisions.

## 2.4 Performance of MFIs as well as

Transparency is essential if the microfinance industry is to expand and to sustain the expansion. Investors, donors and most importantly domestic savers will only place their funds where they can reliably assess risk and return on the basis of standardized, comparable information. That way, auditors and supervisors will be enabled to oversee the safety of the financial system which in turn gives additional confidence to investors in the industry. Institutions that provide financial services also need clear, standardized information to help them determine where they stand in relation to their peers or on a global basis. MFI managers that can benchmark their performance against other MFIs are better capable to improve performance and more interested in doing so.

The challenge to introduce sustainable transparency and institutionalize it is twofold: On one hand, the customers do not give enough and correct information to the MFI for them to make a well informed decision when appraising them. Consequently this creates a gap that leads to a loss on both sides through multiple borrowing and resulting into over-indebtedness and high default rates. On the other hand, MFIs hide information about costs and conditions as they focus on short-term turn-over, discussed in the previous sections.

## 3 Implementing Transparency

### 3.1 Transparency at MFIs - level

MFIs should provide skills and train individuals in customer care and improve corresponding employee performance. There are three highlights to assess customer experience over time. These are partnership, responsiveness and possessiveness. They are attributes that a customer expects from any organization today. Partnership is all about a partner attitude and trust from MFIs. Customers define responsiveness in an MFI as being timely, spontaneous and proactive.

People are the most important resource for any organization. The way they are treated is very important for MFIs' performance, its institutionalizing transparency and eventually economic success and sustainability.

**AMFIU is promoting the above in many ways and these include:**

#### *1) Developing Customer Care Materials and new channels of education*

AMFIU has developed various educative materials that address issues of consumer education, protection and advocacy as a way of promoting transparency in the industry. These materials include, posters, flyers, newspaper pull outs etc and they all address various issues that include savings, debt management, making choices, rights and responsibilities, as well as information on government programmes e.g. *bonna bagawale* etc.

In addition, a music, dance and drama (MDD) skip has been developed and translated in many local languages. MDD has proved to be more effective in promoting transparency to both the consumers and the MFIs. It's the easiest way of educating people within a very short time and in an entertaining manner. Further still MDD is entrenched in the African cultural set up hence fits well in the Ugandan society in promoting transparency.

#### *2) Customer Care Sessions*

For MFIs transparency leads to high retention levels of clients, stronger market drive for creating and

products and services, competitive edge compared to an MFI not carrying out CE. Further still it leads to re-orientation of staff to consumer issues and information. Through a Training of Trainers (ToT) AMFIU enables management staff of MFIs to educate their consumers and these include both potential and existing ones.

AMFIU has developed five modules on consumer financial education. These modules include “savings-You can do it”, “Budgeting- Use money wisely”, “Financial negotiation-communicate with confidence” and “debt management-handle with care”. So far a total of 50 participants have gone through the ToT on how to disseminate these to the end users. The participants are MFI staff, consultants, Associate members of AMFIU, Apex bodies, NGOs and District Private Sector Promotion Centres (for details see Asiimwe 2007).

### 3) *Customer Care Officer/desk*

Transparency would involve establishing an effective consumer redress system to handle consumers' complements and complaints. Customer care managers/officers assist consumers in answering queries as well as giving information to the consumers (existing and potential). Customers need to be listened to and their queries answered in the quickest possible time. Consumers need to instant proposed solutions to their problems. This encourages them to speak out as well as seek for more information in order to make informed choices on financial services.

### 4) *Customer Care Management*

Institutionalizing of market drive in a transparent microfinance industry means to make AMFIU member-MFIs understand that the interests of their clients depend on their own capability to satisfy them in a mutually supportive and constructive way. The MFIs attention has to be focused on being more consumer conscious in their operations. Therefore it is important lifting the profile of customer care at all levels of MFI-management (Asiimwe 2007). So far, as the orientation towards the market-driven operations has been weak to a certain extent. Some MFIs are more oriented towards donors and development agencies. Appointing customer care (alongside product development) as a defined task should become a Sound Practice for MFIs.

## 3.2 Systematic Transparency (MF)

### a) Pillars

#### 1) *Sector Standards (Consumer Code of Practice [CCP] for MFIs)*

As MFIs build partnerships with their customers and the microfinance sector grows more complex, it's getting increasingly important to define standards to ensure that microfinance services are provided in a manner that benefits and respects both clients and MFIs.

The major objective of the CCP is to promote transparency between the MFI and consumers within the microfinance industry in Uganda. It lays a general duty on MFIs to build relations with their customers on a basis which achieves a fair balance between the interests of both i.e. commercial freedom for MFIs and protection for the individual customer with weaker bargaining power.

The CCP for MFIs sets out standards of sound practices for the micro finance industry in Uganda. The CCP is intended to reassure consumers and service providers alike that they are doing business with a reputable organization. Though free competition can secure benefits for customers, it doesn't necessarily lead to adoption of sound practices. Signaling of behavioral and procedural standards is therefore another way in which a positive feedback-circle towards transparency can be triggered.

The CCP for MFIs sets out key commitments and principles which MFIs are expected to follow with good sense and in good spirit. The CCP covers all aspects of consumer credit and other services provided by MFIs regardless of amounts. There is also a provision on complaints handling procedures. It's a voluntary mutual code of conduct, which if adopted has contractual effects to the extent that it defines how to trade fairly. It also states the process of compliance, enforcement and review (for details see AMFIU 2006a).

## 2) Performance Monitoring of MFIs and Consumers

In a growing industry, consumers would be able to take advantage of competition to select among institutions and products that would serve them best. However, consumers

often lack education, awareness and access to information to make accurate choices. At the same time, many MFIs suffer from high customer fluctuations and in some cases from high arrears. These are often connected to over-indebtedness, which is a result of both uninformed choices and hidden multiple borrowing by consumers.

Transparency at both client and MFI level is assumed to lead to a situation where consumers are capable to make informed choices amongst MFIs and MFIs are capable to make informed choices amongst consumers hence a win-win situation is envisaged.

## 3) Inter-MFI-Complaint handling

The validity of transparency slogans is tested by concrete procedures and structures to handle requests, in particular complaints from customers. However there is no redress/complaint handling system in place so far apart from hotline at Uganda Consumers Protection Association (UCPA). UCPA is consumer advocacy body that advocates for consumer rights as well as emphasizes on consumer obligations.

Inter-MFI-redress handling – which may or may not be UCPA – would strengthen credibility of the whole system. Already today many customers turn their complaints to AMFIU rather than going directly through their MFI. Systematizing such an inter-MFI-redress handling offers a unique opportunity to monitor MFIs' customer care efforts as well as impact of transparency programmes.

Whereas an in-house-based complaint handling system for MFIs is needed because the complaints are a valuable source of management information, the inter-MFI-redress handling should be reserved for the most serious cases only.

## 4) Inter-MFI-Product Database

The product perspective is of strategic significance in the bid of expanding outreach of Microfinance. Yet, there is no systematic information available about Microfinance products to date. There are two exceptions: A financial products survey of UCPA (2004) looks at selected institutions of all tiers. An outreach survey of AMFIU in November 2005 looks at products of category A and B MFIs.

UCPA (2004, p. 14) concludes that “[i]t is clear from the survey that there exists a small variety of products, wide variations in transaction charges and other conditions of access to financial services. These aspects are only known to the institutions and consumers who get to know them when sourcing for services. This leaves consumers unaware and therefore incapable of making informed choices.”

The analysis of AMFIU's outreach survey finds that “product range is not as bad as it is sometimes cartooned, but it is surely non-satisfactory and non-sufficient. However, only few development partners have invested strongly into product development (although many claim they do), and GoU not at all. Correspondingly, the product perspective is under-mature among MFI managements.” (Schmidt 2007, p. 14).

Under its transparency programme, AMFIU will conceptualize a product database and collect the corresponding information. This shall be made available online, probably through AMFIU website.

## 5) Inter-MFI-rates and fees display

Access to and comparison of prices – the cost of the consumer – is a central milestone of transparency of any market. The display of fees and interest rates has been poor in the MF-industry so far. This has been a critical issue highlighted by key opinion leaders in the country. Display of total tariffs seeks to identify the technical hurdles and reasons for the perceived reservations of MFIs. Display of tariffs further promotes trust, encourages shopping around in order to make an informed decision by the consumer. This promotes information seeking before a choice is made by the consumer.

AMFIU transparency programme is to address this core issue in 2008/9 through sensitizing and organizing “buy-in” of MFIs and through collecting cost data for savings and loan products and publishing them for dissemination.

## **b) Players**

### **1) Government of Uganda (GoU) and Bank of Uganda (BoU)**

Government of Uganda has been on the forefront in promoting transparency in all its departments as well as the various structures from the central government to the local government levels. BoU as a supervisory body to various financial institutions is involved in ensuring that transparency is observed to the institutions under its mandate.

Through a policy for Tier 4-MFIs and enacting a SACCO-law, principles of transparency and SACCO-member education will be rooted in the legal framework of Uganda.

### **2) Association of Microfinance Institutions Of Uganda (AMFIU)**

AMFIU’s activities hinge on improving transparency of both MFIs and consumers and eventually systemic transparency of the microfinance industry. Transparency is both a means and an end. The latter as a property of decent, respectful MFI-consumer-relations, the former for building a market-driven, competitive Microfinance Industry. AMFIU aims at establishing and sustaining standards of transparency for market-driven MFIs and informed consumers in Uganda’s Microfinance Industry.

AMFIU’s experience of about two and half year of Consumer education programme has exceeded the expectations. The programme is widely appreciated and found more support and participation from MFIs, consumers, regional political leaders and other stakeholders than prognoses had proposed. Moreover, the slightly skeptical position of the donor community seems to be changing – e. g. in their comments for regulation of tier4-institution, the role of Consumer Education is prominently displayed (see e. g. AMFIU 2006b). Rather, consumer

education turned out to be a starting point for AMFIU embracing transparency as one of its core activity areas (**annex one**). AMFIU as an umbrella body for the industry is carrying out many activities to this effort as has been highlighted throughout the discussions of the previous sections. They are synopsised in the “House of Transparency” as displayed in **figure one**. In implementing transparency, AMFIU works with other networks e.g. UCA, UCSCU, SEEP and CGAP.

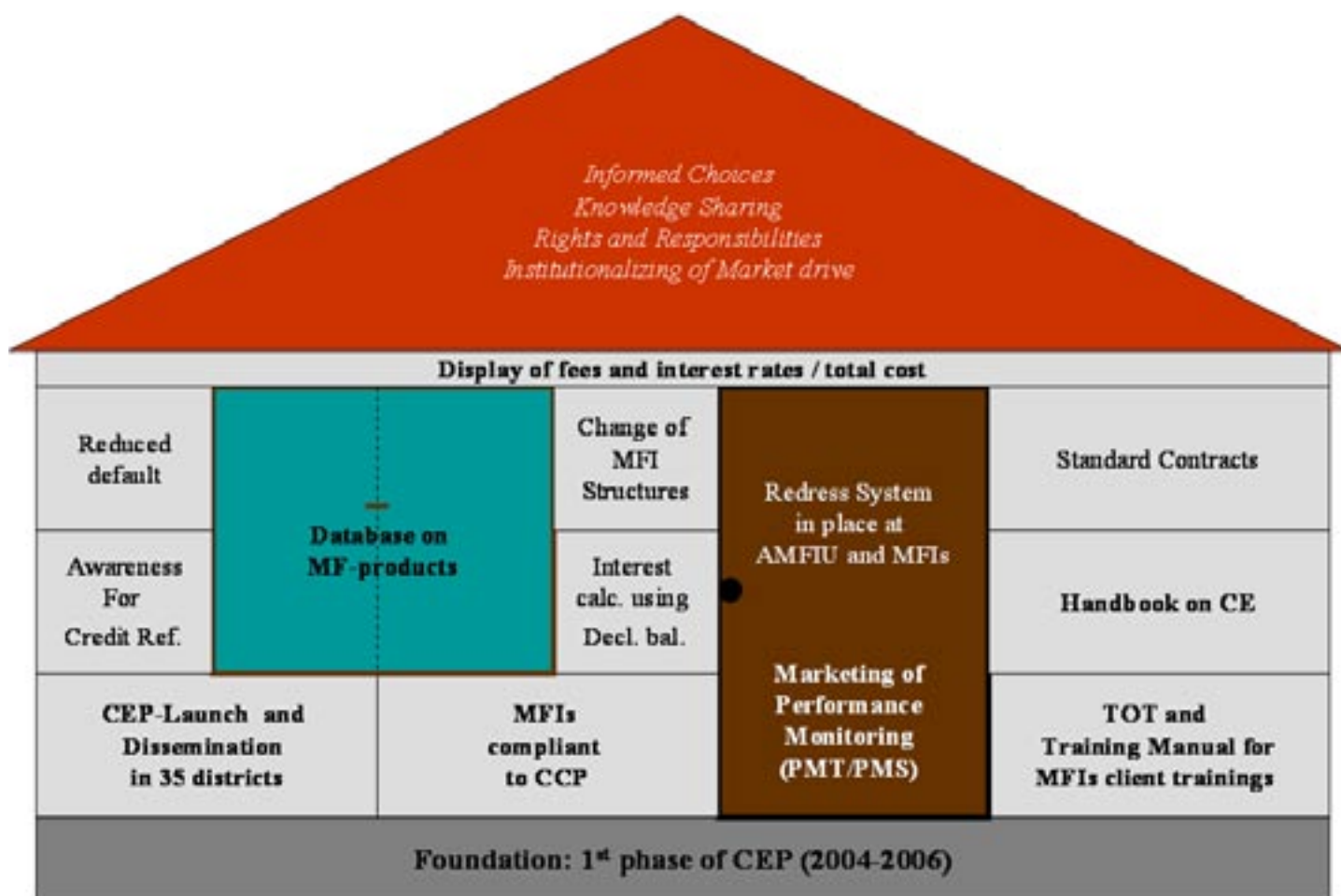
### **3) Rating Agency**

The other initiative to institutionalize transparency is a rating service for MFI. This initiative led by the GoU/EU-SUFFICE-Project is taking shape with 15 MFIs rated so far. The rating reports can be accessed online under [www.ratingfund.or.ug](http://www.ratingfund.or.ug). It has also influenced AMFIU’s recent research on governance (Schmidt/Sijtsma 2007, Sijtsma 2007). The ratings profit from AMFIU transparency programme, because they rely on a culture of knowledge sharing.

### **4) Other players**

Transparency in a growing industry cannot be implemented by only one player. AMFIU’s programme is complemented by the activities of UCPA (see section 3.2 a4) and by a mass-communication campaign run jointly by Straight Talk Foundation and CDFU. While this campaign applies the messages of AMFIU transparency programme as explained throughout this paper, it capitalizes on other channels, e. g. a free newspaper “Money World” disseminated through a wide network of health centers, district headquarters and the like.

**Figure 1: The House of Transparency**



*Italics* (“roof”): Overall objectives

**Bold**: Expected Results of AMFIU transparency programme (funded by EU/ACP-framework programme; DFID/FSDU)

Unbold: Project-elements awaiting funding/realization

**Foundation**: 1<sup>st</sup> phase of Consumer Education Programme 2004-2006 (funded by DFID/FSDU).

## 4 Conclusion

A systemic incorporation of a transparent culture in the institutions and minds of consumers and the industry at large is a long-term goal. It can only be achieved if the commitment towards transparency is regularly re-affirmed, and if this re-affirmation follows standardized procedures and pro-active structures. Or else achievements in transparency will remain ad-hoc and an isolated effort. The steps towards structurally embedding of regular procedures that enforce and re-affirm transparency need to be promoted at MFI-level, at industry-level and at consumer level. The strategic players are MFI-management and the national umbrella, which ideally re-assure their respective roles in a positive feedback-cycle.

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## Annex One

### How transparency grew into a core activity area of AMFIU

[...] In 2003, with the MDI-Act passed, membership standing at close to a hundred, and a secretariat of five technical staff, AMFIU was watching out for re-affirming and further developing its profile and “market share”. [...] Performance Monitoring was under way, with the PMT having been launched and the PMS being thought to be functional any moment. Around Performance Monitoring, a number of related issues “orbited” like enforcement of Code of Conduct, Complaint mitigation between MFIs and Customers, and Consumer Education such that the latter empowered to complain, to claim compliance with Code of Conduct, and generally to demand services according to their needs.

[...] Practically each of these issues was controversial: Be it Capacity Building, be it Regulation, be it Complaint handling, be it Consumer Education: Each of them were claimed for or appointed to AMFIU by some, and denied or rejected from AMFIU by others. To tap into each of them was a decision of highest strategic significance and demanded strong leadership to wrestle down or embrace those opposed, to communicate the evolving profile, and to deliver convincing results such that the move was proven factual.

[...] In 2004, AMFIU board approved the proposal for a 18month-Pilot Consumer Education Programme. The proposal was promoted by AMFIU Programme Manager (then acting ED) who participated significantly in developing the terms of reference. Development partners in the programme were the Financial Sector Deepening Project Uganda (FSDU) and British Department for International Development (DFID). A Consumer Affairs Specialist was recruited, to become the first officer on AMFIU payroll attached to a project assignment.

In 2005, AMFIU presented the programme in regional workshops to its members throughout Uganda. The vast majority of members welcomed the attempts to raise the education of consumers such that they would become better customers, i. e. they would default less, repay more steadily and offer long-term relationships. This would eventually improve MFIs’ image and clients’ awareness for the nature of MF-business, thus reducing risks of information asymmetry. Based on this positive feedback, AMFIU’s Programme Manager and Consumer Affairs Specialist designed a new programme: It was to address “Transparency” throughout the industry in a comprehensive manner, [...]

In 2006/2007, AMFIU affirmed its role towards “transparency” by rooting it both in the strategic (up to 2013) and tactical (up to 2009) framework. This has been communicated through various articles in the Microfinance Banker, through Annual Reports as well as AGM-presentations in 2005 and 2006, and shall be presented at the African Microfinance Conference planned for August 2007. Given the recognized major relevance of “transparency” it still has to be decided upon whether this programme will be belong to AMFIU’s core activities.

**(Source: De Boer 2007)**

## Annex Two

### Contents and Signatories of the Consumer Code of Practice (CCP)

No of chapter	Title of chapter
1	Key Commitments by MFIs towards the CCP
2	Information and Conditions
3	Lending
4	Data Protection and Confidentiality
5	Operation of Client's Account
6	Complaint Procedures
7	Suppliers of other Goods and Services

### The Key Commitments (chapter one of CCP)

1. Act fairly, reasonably and responsibly in dealing with customers.
2. Make sure that all services and products meet the Consumer Code of Practice hereby stated and relevant laws and regulations.
3. Adhere to the Consumer Code of Practice and all relevant laws and regulations.
4. Not to discriminate against a customer because of race sex, disability or ethnic background.
5. Help the customer when she/he needs information and guidance.
6. Keep customer's personal information confidential.
7. Correct mistakes and handle complaints quickly.
8. Consider cases of financial difficulty sympathetically and positively. We shall seek to comply with both the letter and spirit of these standards.
9. Ensure that all officers and employees are aware of and apply the standards outlined in this code of practice.
10. Display the CCP in our premises and make copies of the code freely and readily available.
11. Train staff to make sure that the procedures they follow reflect the commitments set out in this code.

#### Signatories:

*Regulated MFIs (Tier 1,2,3):*

**CERUDEB, Kampala; CMF Ltd, Kampala; FINCA (U) MDI, Kampala; Postbank, Kampala; Uganda Finance Trust MDI, Kampala;**

*Unregulated MFIs (Tier 4):*

**AGALI AWAMU SACCO, Luwero; Agaru SACCO, Pader; ADEVIN SACCO, Apac; Busimbi, Mityana; Blue Fox, Lira; EMESCO Devlp. Foundation, Kibaale; FAULU (U), Kampala; Feed the Children (U), Kampala; HOFOKAM, Kabarole; INCOFIN, Hoima; Kyanayenyi SACCO, Bushenyi; KALICADA SACCO, Kamwenge; Katweyombeke SACCO, Hoima; KIDEA SACCO, Hoima; KIWAFU SACCO, Entebbe; Kihihi Devlp. SACCO, Kabarole; Koka SACCO, Kaberamaido; Kalibaimukya SACCO, Kibaale; Kitgum SACCO, Kitgum; LYAMUJUNGU SACCO, Kabale; MEDNET, Kampala; MAMIDECOT, Masaka; MCDT, Kampala; Northern Recovery MF Services, Gulu;**

### Annex Three

#### Transparency Posters

## BUDGETING - Use money wisely



Know your income source, set a financial goal and plan how to spend wisely.



## FINANCIAL NEGOTIATION

Communicate with confidence



Negotiation helps you to get a manageable debt.



## FINANCIAL SERVICES

Know your options



There are many financial institutions providing various services. Choose the institution and services that best meet your needs



## SAVINGS

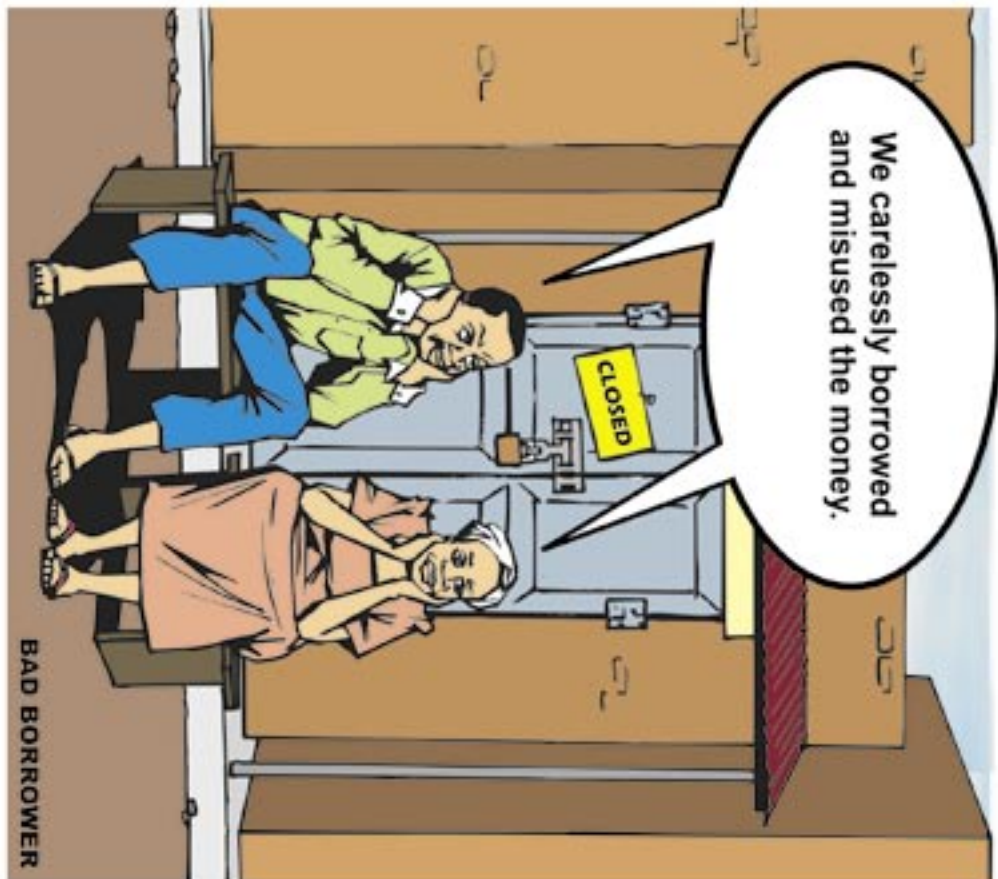
You can do it.



Savings can help you invest, pay school fees, prepare for emergencies, and avoid unnecessary debts.



# DEBT - Handle with care



**Make sure you understand your loan contract and pay back on time.**



AMFIU



EU-ACP Microfinance Framework Programme



AMFIU

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