

# SMART LENDING: CLIENT PROTECTION IN THE CREDIT PROCESS

An Overview for Incorporating Client Protection Practices  
into Individual Lending by Microfinance Institutions

[www.smartcampaign.org](http://www.smartcampaign.org)



Keeping clients first  
in microfinance

## INTRODUCTION

These guidelines are designed to help microfinance institutions (MFIs) with individual lending operations integrate good client protection practices into their credit processes. At each point in the individual lending process, the guidelines explain how MFI staff should incorporate client protection into policies and operations. The guidelines are largely focused on operational issues, with brief recommendations about setting up policies for the institution.

The guidelines are presented in the chart below and in the following pages. They walk the user through each major step of the individual lending process, organized into five phases: 1) Promotion and Sales, 2) Evaluation, 3) Approval, 4) Disbursement, and 5) Collections. The chart begins with an overview of the entire credit process and then provides greater detail on each of the five phases. At each appropriate step in the process, the guidelines identify where client protection practices can and should be incorporated. Each of those intersections is denoted with a client protection intervention point number (e.g. CP1, CP2 etc.). Guidelines for each CP include suggestions for how to model good practice in consumer protection for that portion of the credit process.

While the guidelines offer suggestions for operational steps and policy consideration, they are not a complete solution for implementing client protection in the credit process. They do, however, identify areas where additional steps may be necessary, such as staff training and institution-specific materials for how to address the points raised in the guidelines. Many of the guidelines would benefit from an additional, more in-depth tool to help field staff implement the ideas contained in the guidelines. For example, CP2 offers guidelines for the information that should be conveyed during the initial sales speech and what should be avoided when selling individual credit products to clients. An additional tool, such as a sample sales speech, could offer sample dialogues between the staff person selling the product and the client, with possible questions and answers that adhere to the Client Protection Principles. The Smart Campaign plans to develop several of these in-depth tools. Until then, we encourage MFI users of this tool to move forward with the implementation of client protection into existing operations and to share your feedback and experiences with The Smart Campaign.

[THE CLIENT PROTECTION PRINCIPLES](#) (short form listed below; for complete description, see [www.smartcampaign.org](http://www.smartcampaign.org)).

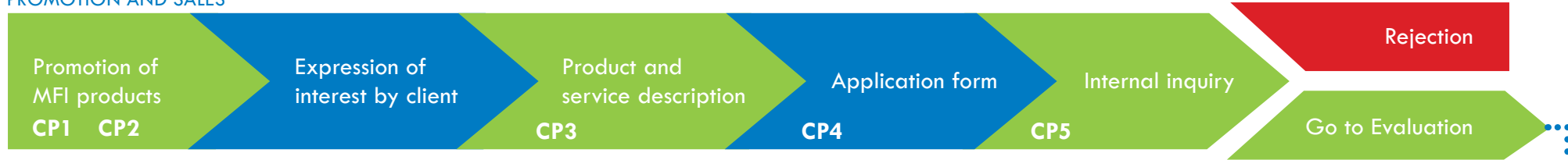
1. Avoidance of over-indebtedness
2. Transparent and responsible pricing
3. Appropriate collections practices
4. Ethical staff behavior
5. Mechanisms for redress of grievances
6. Privacy of client data

*Source: These guidelines are the result of collaboration between The Smart Campaign and the technical staff of ACCION International. This collaboration is ongoing and ACCION looks forward to sharing more such tools on related topics in the future.*

Special thanks goes to Susana Barton, Cara Forster, Raul Gomez, Valerie Kindt, Elisabeth Rhyne, and Victoria White.

# THE CREDIT PROCESS

## PROMOTION AND SALES



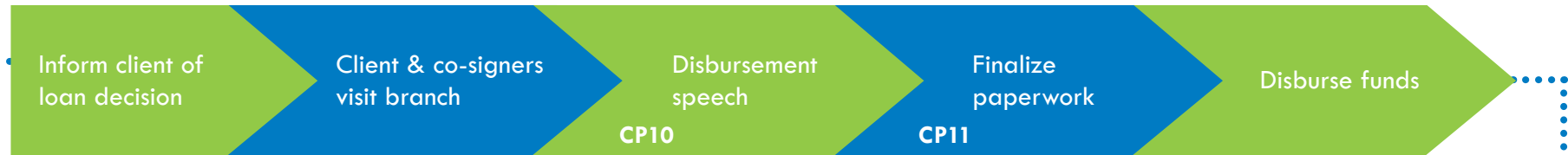
## EVALUATION



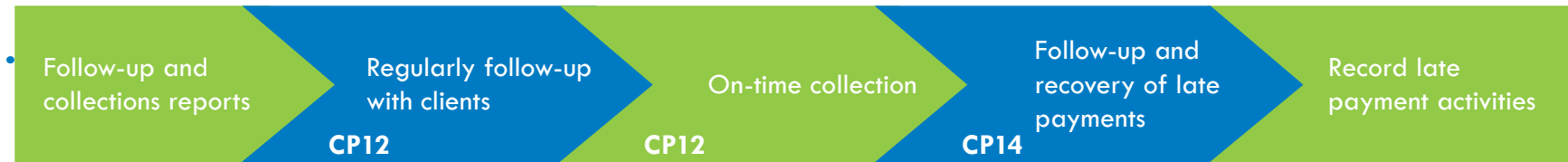
## APPROVAL



## DISBURSEMENT



## COLLECTIONS & RECOVERY



# 1. PROMOTION AND SALES



CP#	CP1	CP2	CP3	CP4	CP5
	<b>MARKETING MATERIALS</b>	<b>SALES PITCH</b>	<b>PRODUCT DESCRIPTION</b>	<b>APPLICATION FORM</b>	<b>COMMUNICATION OF RESULTS PROTOCOL</b>
<b>CP PRINCIPLES</b>	Transparency, Redress	Over-indebtedness, Transparency, Data Privacy	Over-indebtedness, Transparency	Transparency, Data Privacy	Transparency, Redress
<b>POLICY CONSIDERATIONS</b>	<p>Transparency in terms and conditions: The institution makes a commitment to transparency in product and services terms and conditions, including pricing.</p> <p>Responsible pricing practices: The total cost to the client must be affordable to the client and offer the potential for sustainability to the institution.</p> <p>Staff incentive policy for credit: Weigh PAR appropriately with growth, given risk environment (e.g., regional, macroeconomic conditions, etc.).</p>				
<b>OPERATIONAL CONSIDERATIONS</b>	<ul style="list-style-type: none"> <li>Develop promotional flyers in local language.</li> <li>Provide basic eligibility requirements on the flyer.</li> <li>Reserve space on calling cards and flyers for how to handle questions and/or complaints including the institution's phone number and address.</li> <li>If space, include basic information on product (e.g., purpose, payment information, etc.).</li> </ul>	<ul style="list-style-type: none"> <li>Sales speech should provide basic introduction to the institution and its products in local language.</li> <li>Product terms and conditions should be clearly stated, including topics such as eligibility requirements, documentation requirements, total cost to the client for accessing loan (with examples), minimum and maximum loan sizes, explanation of use of client data, and, for group loan products, a clear explanation of the meaning of joint liability.</li> </ul>	<ul style="list-style-type: none"> <li>Explain products, addressing which is most appropriate/best value/best fit.</li> <li>Provide a complete description of the product's costs, including price, interest rate, and all associated fees.</li> <li>Provide a complete description of the product's terms and conditions.</li> <li>Provide an explanation of upcoming evaluation process and inform the client of penalty fees, late payment fines, etc.</li> </ul>	<ul style="list-style-type: none"> <li>Inform the client on what demographic and business information is required and why.</li> <li>Explain how this information will be used and stored.</li> <li>Client consent to terms and conditions should be located on form and explained by loan officer (explain concept of credit bureau if necessary).</li> </ul>	<ul style="list-style-type: none"> <li>Communicate eligibility results clearly to the client.</li> <li>If negative, explain why a decision was made and how the client can take action to achieve a positive result in the future.</li> <li>Provide a phone number where the client can get additional information and recourse.</li> </ul>
<b>CP TOOL</b>	Guide for development of promotional flyer with relevant information; sample flyer	Guide for initial sales pitch; sample pitch	Guide for describing products available to client	Guide on how to request information from a client; sample form	Guide for communicating eligibility criteria

## 2. EVALUATION



CP#	CP6	CP7	CP8
ACTIVITY/FORMS	<b>DATA COLLECTION: NON-FINANCIAL EVALUATION</b>	<b>DATA COLLECTION: FINANCIAL EVALUATION</b>	<b>DATA PRIVACY / DATA MANAGEMENT</b>
CP PRINCIPLES	Over-indebtedness, Transparency, Appropriate Collections, Staff behavior, Data privacy	Over-indebtedness, Ethical staff behavior	Ethical Staff Behavior, Data privacy
POLICY CONSIDERATIONS	<ul style="list-style-type: none"> <li>Commit to respect client privacy and confidentiality of information.</li> <li>Collect relevant data to ensure sufficient “willingness to repay” and to analyze “capacity to repay.”</li> <li>Commit to collect and incorporate 3rd-party debt information on each client.</li> <li>Develop clear policy guidelines on loan guarantee and collateral mechanisms, including guarantor profiles and what can and cannot be registered as collateral.</li> </ul>		
OPERATIONAL CONSIDERATIONS	<p><b>General</b></p> <ul style="list-style-type: none"> <li>Explain to client what information is needed and why.</li> <li>Explain how the information will be used.</li> <li>If relevant, explain what a credit score is and how it will be used.</li> <li>Clearly ask about other outstanding loans client may have. Use available means (e.g., credit reference bureau, shared client lists, etc.) to confirm outstanding debts.</li> <li>Ensure privacy of photos; if client photos are taken, explain how the pictures will be used and who will have access to them.</li> </ul> <p><b>Collateral</b></p> <ul style="list-style-type: none"> <li>Explain why assets are being recorded (collateral as well as evaluation) and what can happen to them in the case of default.</li> <li>If applicable, describe under what circumstances client assets can be removed and describe the confiscation process.</li> </ul> <p><b>Co-Signors, Guarantors, Spouses</b></p> <ul style="list-style-type: none"> <li>Explain why co-signers and guarantors are used and why spouses are involved.</li> <li>Explain the rights and duties of co-signers, guarantors, and spouses.</li> <li>The explanation should precede signing.</li> <li>Treat with all parties with respect.</li> </ul> <p><b>References</b></p> <ul style="list-style-type: none"> <li>Explain why assets are being verified.</li> <li>Focus on fact checking.</li> <li>Refrain from judgmental questioning.</li> </ul>	<ul style="list-style-type: none"> <li>Before initiating financial evaluation: <ul style="list-style-type: none"> <li>explain to the client the consequences of over-indebtedness and why it is important to provide accurate information—Stress honesty and integrity, and</li> <li>explain what information is necessary to collect and how it will be used.</li> </ul> </li> </ul> <p>Discuss institutional values for avoiding over-indebtedness, such as appropriate products and debt capacity analysis.</p>	<ul style="list-style-type: none"> <li>Limit access to private data within the institution with strong internal controls.</li> <li>Strong data security means: <ul style="list-style-type: none"> <li>internal controls, good IT management;</li> <li>clearly-defined user access hierarchy; and</li> <li>frequent change of passwords.</li> </ul> </li> <li>Special considerations for sharing data with third parties include: <ul style="list-style-type: none"> <li>considerations for data security when outsourcing, and</li> <li>MOUs with contracted third parties should agree to CP guidelines/ethics.</li> </ul> </li> </ul>
CP TOOL	Guide for collecting non financial evaluation information	Guide for collecting financial evaluation information	Guideline for developing data management protocol

### 3. APPROVAL



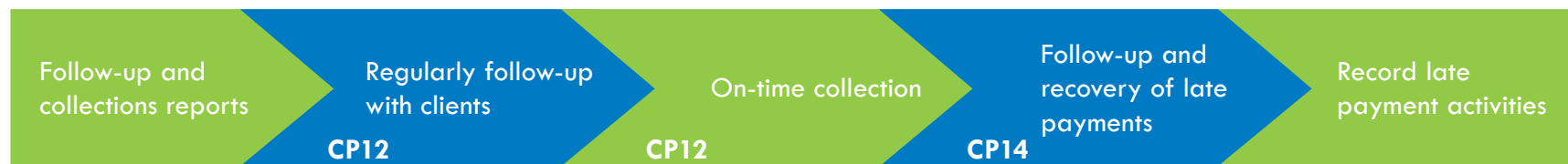
CP#	CP9
ACTIVITY	FINANCIAL ANALYSIS
CP PRINCIPLES	Over-indebtedness
POLICY CONSIDERATIONS	<ul style="list-style-type: none"> <li>• Never lend more than the client requests or more than they have capacity to repay.</li> <li>• All lending decisions should incorporate some element of capacity to pay analysis; as loan size increases, this analysis should be increasingly more thorough.</li> <li>• Ensure credit decisions are made by appropriately trained professional staff.</li> </ul>
OPERATIONAL CONSIDERATIONS	<ul style="list-style-type: none"> <li>• At a minimum, capacity-to-pay analysis should include calculation of the client's working capital and business and household surplus, as well as their assets and liabilities.</li> <li>• Over-indebtedness: It is the responsibility of the MFI to collect data on other loans the client may have. This can be done through an interview, a credit bureau, or an information exchange between MFIs.</li> <li>• MFIs need to invest in acquiring data available so that the best credit decision can be made. Any other loans outstanding should be incorporated into client's indebtedness analysis.</li> <li>• Client indebtedness should be continually monitored by the organization.</li> <li>• Guidelines may need to be regional, by business sector, or both.</li> </ul>
CP TOOL	Guideline for financial evaluation

## 4. DISBURSEMENT



CP#	CP10	CP11
ACTIVITY	DISBURSEMENT SPEECH	DOCUMENTATION
CP PRINCIPLES REFLECTED	Over-indebtedness, Transparency, Data privacy	Over-indebtedness, Transparency, Appropriate Collections, Ethical Staff Behavior, Redress
POLICY CONSIDERATIONS	<ul style="list-style-type: none"> <li>Ensure sufficiently senior/ trained person is responsible for assembling all relevant documentation and the disbursement speech. Ensure this person is not the same person who later collects loan payments.</li> <li>MFI should only accept as guarantors persons who have the financial capacity to pay back the loan.</li> </ul>	
OPERATIONAL CONSIDERATIONS	<p><b>General:</b></p> <ul style="list-style-type: none"> <li>Provide verbal explanation of each document to client, especially the payment schedule.</li> <li>Read the summary page (see CP11) to the client.</li> <li>For illiterate clients, verbally read or explain all the documents.</li> <li>Consider a poster on the wall near where the disbursement occurs to remind staff and clients of client rights and responsibilities.</li> </ul> <p><b>Key elements of disbursement speech:</b></p> <ul style="list-style-type: none"> <li>Explain all costs (e.g., stamp duty, margin money, insurance, any other fees, linked products, etc.). Clients should also be alerted to never pay any additional commissions or fees to staff, beyond what is explained in the disbursement speech.</li> <li>Advise client to always ask for a receipt of their account balance and to ask for exact change.</li> <li>Explain impact of fees on amount disbursed, which may be less than loan amount approved if fees are deducted up front.</li> </ul> <p><b>For guarantors, spouse, co-signors:</b></p> <ul style="list-style-type: none"> <li>Inform the spouse about the disbursement, unless there is good reason to believe that the spouse might misuse/appropriate the funds.</li> <li>Inform the guarantor/co-signer of his/her co-responsibility to pay back the loan in case the client defaults.</li> <li>Ensure that the guarantor is not a “professional guarantor” who guarantees multiple clients and may ask for a fee or percentage of the loan.</li> <li>Explain that the loan recipient should control the use of the loan money.</li> </ul>	<ul style="list-style-type: none"> <li>Include a summary page that: <ul style="list-style-type: none"> <li>Provides the client with one summary page with key information. This summary page can be tailored to the client or can be generic. (Generic pages increase efficiency and reduce error rate; tailored ones can be more understandable to the client. Consider making it a part of the welcome kit.)</li> <li>Includes rights and duties of both the MFI and the client.</li> <li>Includes complaints information (e.g., how to access MFI and third-party consumer agencies).</li> <li>Explains collections practices, consequences, and procedures in the case of non-repayment</li> <li>Provides verbal explanations for all clients, especially for illiterate clients.</li> </ul> </li> <li>Explain complete contract in non-legal, clearly understandable terms.</li> <li>Ensure the client always receives a copy of the loan repayment table.</li> </ul>
CP TOOL	Guideline for disbursement speech; sample speech	Guideline for documentation requirements; sample plain language contract and sample one page summary

## 5. COLLECTIONS & RECOVERY



CP#	CP12	CP13	CP14
ACTIVITY	ON TIME COLLECTIONS	OUTSOURCING - USE OF THIRD PARTY COLLECTIONS AGENTS	RECOVERY AFTER LATE PAYMENT
CP PRINCIPLES	Transparency, Appropriate Collections, Ethical Staff Behavior	Appropriate Collections, Ethical Staff Behavior	Over-indebtedness, Transparency, Appropriate Collections, Ethical Staff Behavior, Data Privacy
POLICY CONSIDERATIONS	<ul style="list-style-type: none"> <li>Commit to ethical standards for collections.</li> <li>Collection agents (in-house or 3rd party) should share organizational culture and/or be trained on the institution's values.</li> <li>Collection agents (in-house or 3rd party) should be held accountable for the same standards of behavior outlined in the institution's code of ethics.</li> <li>Established standards for ensuring the privacy of client data should be used by both MFI and the third party.</li> </ul>		
OPERATIONAL CONSIDERATIONS	<ul style="list-style-type: none"> <li>Ensure ethical staff behavior during collections as described in the code of ethics.</li> <li>Use preventive recovery methods, such as reminders.</li> <li>Always provide a receipt and give correct change.</li> <li>For field collections, provide special training for collections staff.</li> <li>For field collections, ensure visits happen on a specified day.</li> </ul>	<ul style="list-style-type: none"> <li>The CP 12 guidelines apply.</li> <li>Develop contracts with 3rd-party agents that hold agents accountable to the MFI's ethical standards.</li> <li>Implement a quality control process to ensure that the standards are being met.</li> </ul>	<ul style="list-style-type: none"> <li>Draft recovery-visit scripts to emphasize respect and model appropriate behavior.</li> <li>Ensure restructuring does not increase the debt levels of already-indebted clients.</li> <li>Ensure any confiscation of assets follows legal recovery channels.</li> </ul> <p><b>Penalty fees</b></p> <ul style="list-style-type: none"> <li>Fees, penalty interest, etc., should not exceed an established portion of the original loan amount. Each institution should establish its own standard.</li> <li>Do not charge interest after the loan is written off.</li> </ul>
CP TOOL	Guidelines for collection practices; sample code	Guidelines for 3rd-party collection practices	Guidelines for recovery practices; sample scripts