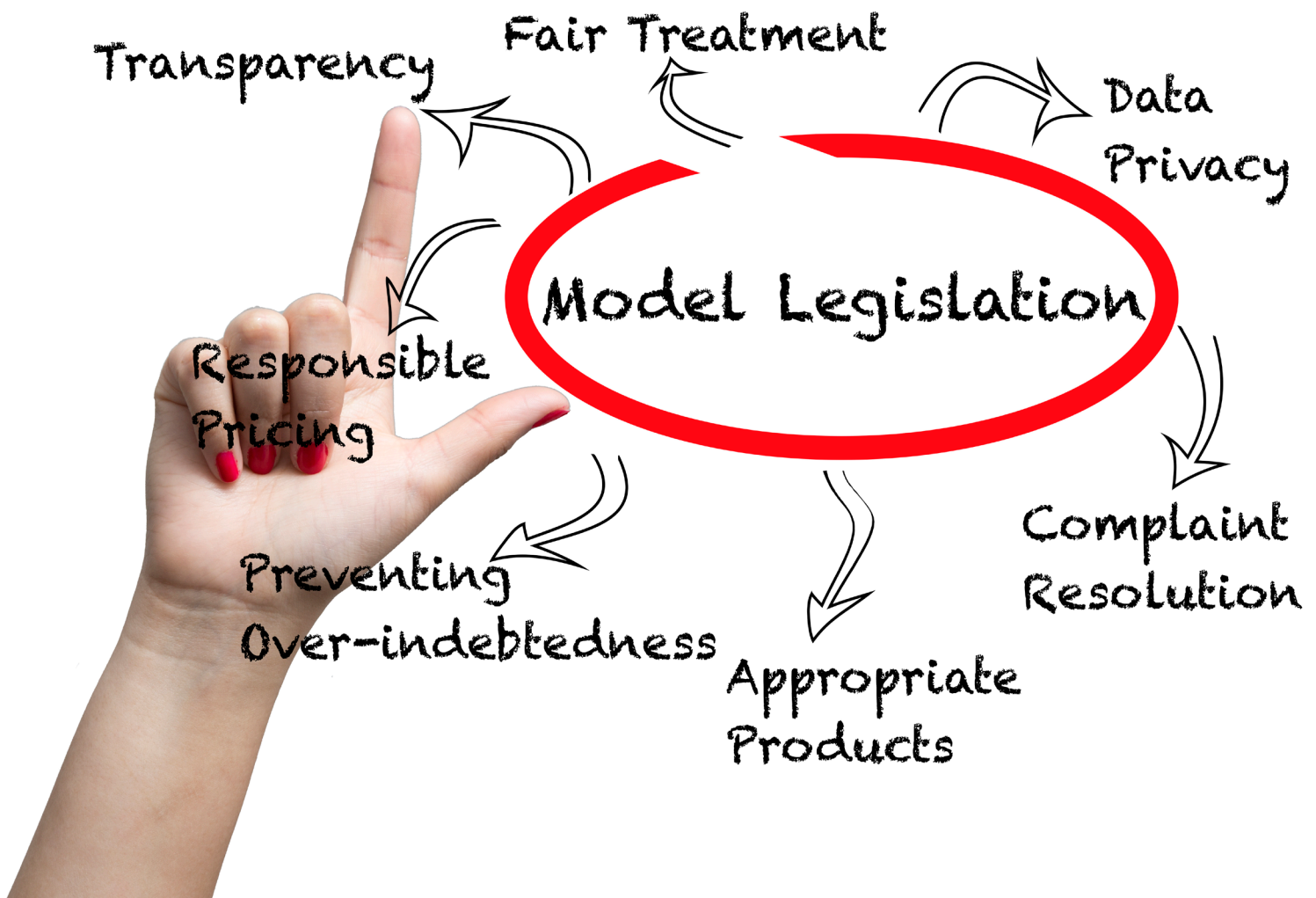


# Client Protection Principles: Model Law and Commentary for Financial Consumer Protection

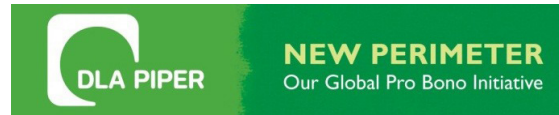


Microfinance  
CEO Working Group

# Client Protection Principles: Model Law and Commentary for Financial Consumer Protection

April 2015

Prepared by



Project Manager on behalf of the Council of Microfinance Counsels

## ACCION

With contributions by the Smart Campaign

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## **Introduction**

### **Overview**

This Model Law and Commentary (collectively, the “Model Law”) creates a legal framework for financial consumer protection based on the Smart Campaign’s Client Protection Principles.<sup>1</sup> It draws upon a broad survey of experts, relevant scholarship, and existing laws and regulations from countries across the globe. The document presented here reflects this background research, distilled into model legislative language with accompanying commentary.

The Model Law is intended for three main uses. First, it may be useful to policy makers as a tool in developing actual, enacted legislation. Taken as a whole, the Model Law forms a complete legal regime for client protection in line with the Client Protection Principles. However, the Model Law is also designed to facilitate adoption in parts, where individual sections or provisions may be adopted to fill in legal or regulatory gaps. And, of course, any adopting jurisdiction will have to adjust the Model Law’s provisions to fit local precedents and circumstances.

Second, the Model Law can be used to assess a given jurisdiction’s client protection regulatory regime. By setting the Model Law side-by-side with a jurisdiction’s current legislation and regulation, policy makers and commentators can easily assess how that jurisdiction’s legal framework compares with a model approach based on the Client Protection Principles.

Third, the Model Law may serve as a resource for the development of codes of conduct and guidelines, either for a single financial service provider or for any group or industry association. While the document is in the format of legislation, the systems and approaches described in the Model Law may provide guidance on effective ways to promote client protection through the internal operation of financial service providers.

### **The Smart Campaign’s Client Protection Principles**

This legal framework is the legislative counterpart of the Client Protection Principles, which have been developed within the microfinance sector and promoted by the Smart Campaign. The Smart Campaign is a global effort guided by the experience and expertise of microfinance leaders from around the world who are committed to following positive client protection practices. The Client Protection Principles represent a global consensus across the sector regarding the standards of conduct and treatment clients should receive from financial service providers. To learn more about the Smart Campaign and the Client Protection Principles please visit <http://www.smartcampaign.org>.

Here, the Client Protection Principles are matched with legal provisions which promote the realization of those principles in practice. Both the Client Protection Principles and the Model Law reflect years of consideration and study by a wide cross section of stakeholders in

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<sup>1</sup> The Client Protection Principles consist of: (i) appropriate product design and delivery; (ii) prevention of over-indebtedness; (iii) transparency; (iv) responsible pricing; (v) fair and respectful treatment of clients; (vi) privacy of client data; and (vii) mechanisms for complaint resolution.

and close to the microfinance sector, including financial service providers, industry organizations, regulators and consumer advocates, on leading industry standards and best practices. While the principles originated with microfinance, they are broadly applicable to retail financial consumers, particularly those with lower income and those new to the use of financial services.

The Smart Campaign operates a certification program that identifies and publicly recognizes financial service providers that meet the standards derived from the Client Protection Principles. Smart Campaign certification can assist in demonstrating that a financial service provider is meeting or exceeding industry-defined global best practices that are aligned with the legislative spirit of the Model Law.

### **Structure of the Model Law**

Each section of the Model Law is divided into three parts: Purpose, Content and Commentary. The Purpose gives a general explanation of the aim of the specific provision. The actual recommended legislative language is contained in the Content, while the Commentary seeks to explain, clarify and provide context on the language in the Purpose and Content.

### **Approaches Taken in the Model Law**

**1. Broad Provider Applicability.** All financial service providers, including banks, credit unions, microfinance institutions, money lenders, and digital financial service providers, are covered under the Model Law, regardless of their corporate form and primary business line, whether or not they are prudentially licensed, publicly owned, run for private gain or for charitable purposes. Effective client protection requires that all financial service providers providing similar consumer financial products or services be subject to very similar, but proportional rules. This is particularly important for lower income clients who are often served by smaller and less regulated financial service providers. Anything less than broad coverage of financial service providers will leave gaps in the regulatory framework, which experience shows are too often exploited to the disadvantage of the most vulnerable clients.

**2. Creation of a Dedicated Client Protection Regulator.** This Model Law assumes that the preferred institutional framework has a specific regulator charged with ensuring client protection in the financial sector and empowered with all the tools necessary to do so. As such, it begins with the establishment of a supervisory authority to conduct broad market monitoring, to supervise financial service providers and to initiate a variety of enforcement actions when necessary. The supervisory authority is also empowered to 1) facilitate the creation of a credit reporting system, if none currently exists; 2) create a client recourse mechanism for addressing client complaints; 3) gather and publish the fees and rates of consumer financial products to facilitate clients' ability to compare pricing; and 4) produce and publish reports on the financial services industry's client protection performance.

**3. Principles-Based and Rules-Based Regulation.** In some areas, the Model Law utilizes principles-based regulation, where regulators use a degree of discretion to assess a financial service provider's compliance with subjective standards. This approach is appropriate for areas where a wide range of conduct is acceptable, and in the Model Law principles-based regulation

is used in the area of transparency and disclosure, and in the prohibition on unfair, deceptive or abusive acts or practices. However, where more specific, objective requirements are appropriate, rules-based regulation is used. This approach can be seen in the Model Law's sections on registration, standardized calculation methods, key information disclosure requirements, non-discrimination in client selection, termination and prepayment fees, the provision of information to credit reporting systems and the prohibition on requiring clients to waive their rights as a condition of receiving a financial product.

**4. Client Rights.** The Model Law enshrines certain specific rights for clients. For example, clients are granted the right to have their complaints addressed and resolved, the right to a reasonable rescission period, the right to have their personal data protected and the right to have inaccurate information corrected.

**5. Consumer Financial Protection Subjects not Covered.** Several topics important to consumer financial protection that are beyond the scope of the Model Law, such as deposit insurance and bankruptcy, may need to be addressed in any country adopting or implementing a client protection regime. Additionally, financial capability and literacy is an important aspect of consumer protection and countries may be wise to establish a government division, department or agency focused on improving financial literacy.

### **The Authors**

This Model Law was sponsored by the Microfinance CEO Working Group. DLA Piper/New Perimeter was the lead author. Accion served as Project Manager on behalf of the MCWG Subcommittee of the Council of Microfinance Counsels. Significant contributions were made by the Smart Campaign.

The Microfinance CEO Working Group is a collaborative effort by the CEOs of ten leading global microfinance organizations whose impact is felt in 80 countries on five continents, and whose products and services are designed to offer support and opportunity to millions of low-income people around the world.

DLA Piper is a global law firm with 4,200 lawyers located in more than 30 countries throughout the Americas, Asia Pacific, Europe and the Middle East, positioning it to help companies with their legal needs anywhere in the world. In certain jurisdictions, this information may be considered attorney advertising.

New Perimeter is a nonprofit organization established by DLA Piper to provide pro bono legal assistance in under-served regions around the world to support access to justice, social and economic development and sound legal institutions. Founded in 2005 as a result of DLA Piper's commitment to support legal advancement worldwide, New Perimeter's vision is to harness the skills and talents of more than 4,200 DLA Piper lawyers to further a more just world for all.

Accion is a global nonprofit dedicated to building a financially inclusive world with access to economic opportunity for all, by giving people the financial tools they need to improve their lives. A world pioneer in microfinance, over the last 50 years it has helped build 63 microfinance institutions in 32 countries on four continents. Those institutions are currently reaching millions of clients.

### **Comments on the Model Law**

The Model Law is a living document that will be amended from time to time to reflect both experience and emerging practices. The authors welcome any and all comments and suggestions for future revisions.

Please send your feedback to [ModelLaw@MicrofinanceCEOWorkingGroup.org](mailto:ModelLaw@MicrofinanceCEOWorkingGroup.org).



## Preliminary Comments on Adoption and Implementation

- a) **Tailoring the Model Law.** The model legislation format is an idealized presentation, providing a view of what a client protection regime could be if created in a jurisdiction with no pre-existing laws or regulatory bodies covering consumer financial products or services. However, there are few, if any, countries where this is the case. In actual implementation, the language of the Model Law must be tailored to reflect the unique political, legal and economic circumstances of the adopting country. Client behavior and legal context all differ dramatically from country to country, and as such, detailed laws or regulations from one country cannot be effectively adopted wholesale and enforced in another jurisdiction.

To facilitate tailoring, the model legal language is accompanied by commentary. Much of the commentary seeks to explain or elaborate on why particular policy choices are made in the legislative provisions. Elsewhere, commentary describes alternatives to the proposed provisions. However, even where an explicit discussion of alternatives is absent, those utilizing the Model Law may conclude that pre-existing structures and laws, and the particular political environment, may make other policy choices the best fit for a specific country.

For example, where an existing financial client protection regulator exists, implementing the Client Protection Principles may be possible via rules and regulations, which is generally quicker and easier to accomplish than adoption through the legislative process. In such a scenario, the Model Law still provides a useful template for regulations, and much of the legislative language can be adapted for rulemaking.

Regulators with a nascent financial client protection regime may wish to take an incremental approach, first establishing or refining the simplest and most effective requirements, such as standardized disclosure regimes, before promulgating more complex regulations. Regulators need to build their own capacity and, through effective regulation, build the credibility and political will necessary to implement further protections across the financial sector.

Finally, where the Model Law is adopted and implemented, policy makers must address how to treat products and services that may have been developed, marketed or sold before the new law was in effect. The best approaches to alleviating these issues will largely depend on how similar the new client protection regime is to the old one.

- b) **Scope of Products Covered.** The Model Law is designed to apply to all consumer financial products and services, with the goal of providing clients a consistent level of protection regardless of the particular product, service or financial service provider. In many countries, because of existing structures and political realities, a client protection scheme across all financial service providers may be difficult to develop. However, even where implementing such broad coverage is impractical, the provisions of the Model Law may still prove useful. Most provisions can be easily adapted for legislation covering a narrower set of products, services or financial service providers.
- c) **Context and Engagement in Developing a Client Protection System.** Creation or revision of a client protection system is more likely to be successful when certain conditions exist,

including political and public support, engagement of all stakeholders and a careful study of the current laws and regulations. Analysis of the existing framework in dialogue with financial service providers, consumer groups, clients, industry associations and other stakeholders can increase support for changes by highlighting existing shortcomings and opportunities for new approaches. A deep examination must also be made of existing market conditions, to take stock of the size and complexity of current financial service providers, the actual and potential capacity of regulators and the sophistication of clients. This information can focus attention on areas where clients are actually most vulnerable. Further, regulators must be ever cognizant of the compliance cost imposed by regulations and consider how these costs may affect clients' access to financial services.

**d) The Supervisory Authority.**

- 1) **Form.** The supervisory authority created by the Model Law may be a stand-alone, independent, government agency. However, creation of an independent agency may not be practical in many countries. In actual implementation, financial client protection is often handled by a dedicated department or staff unit within the central bank, a prudential regulator, a general consumer protection regulator, or may be spread amongst several agencies, each charged with overseeing different types of products or financial service providers. The language in the Model Law seeks to encompass or be adaptable to all of the above formats for a supervisory authority. However, the authors advise against leaving the authority in the hands of a general consumer protection regulator likely to have other skills and priorities. The preferred scenario, on which the Model Law is based, is to have staff dedicated to financial client protection, with clear lines of demarcation between their authorities and powers and that of prudential regulators. While there are successful examples of client protection and prudential regulation being carried out by the same authorities or supervisors, the focus and concerns demanded by the different mandates are not always fully aligned. Where such separation is not possible, the substantive requirements of the Model Law may be implemented by prudential supervisors, through staff dedicated to financial client protection.
- 2) **Internal Governance and Structure.** The Model Law includes no choice of executive structure, although implemented legislation should clearly define how the leadership will be structured and appointed and may also describe the internal organization of the supervisory authority. It is desirable for the supervisory authority to be as independent as possible from political interference but also checked from arbitrary or capricious abuses of governmental authority. Such concerns may be addressed through the design of the governance and internal structure of the supervisory authority and through establishing administrative checks and balances, such as providing for rules or enforcement actions to be reviewable by another governmental body. Complaints against the supervisory authority could be directed to an appeal process within another regulatory body or to an ombudsman's office charged with investigating such complaints.

- 3) **Powers.** The Model Law provides a variety of powers and capabilities for the supervisory authority. In general, these powers represent tools to be used at the option of the regulators. For example, the Model Law provides that the supervisory authority may suspend the registration of financial service providers upon finding a violation, but the supervisory authority need not do so if other regulatory tools are more appropriate, and would be advised to use such a power only in extreme cases. Giving the supervisory authority an array of tools to be used at their discretion allows local experts to select the best method to address problems under the local circumstances. These tools should be used in a risk-based and proportionate manner, focusing supervisory attention on the greatest harms in the marketplace. Other powers may be required in actual implementation to allow the supervisory authority to operate as an independent government agency. These powers may include the ability to enter contracts, employ staff, lease buildings and set budgets.
- 4) **Open Questions.** Many questions about the operations of the supervisory authority are left open in the Model Law, in recognition of the various ways the supervisory authority may be structured. However, if a new government agency is being created to implement the Model Law, additional provisions may be needed regarding the financing, internal governance and structure of the supervisory authority, and its relationship to other regulators. With respect to funding, possible solutions include fees on financial providers or general allocations from the government budget. Other provisions may be required regarding who sets and approves the budget and any limits on expenditure.
- e) **Provisions Requiring Rulemaking.** To become operational and be fitted to local circumstances, some of the provisions of the Model Law require further elaboration, either through rulemaking or amendments to the proposed language. For example, those implementing the Model Law may need to provide greater detail for registration requirements, promulgate model disclosure forms, provide for a detailed standardized interest rate method and determine the appropriate length for rescission periods. Additionally, if there is a desire to limit the application of the Model Law to businesses over a certain threshold size, that threshold must be promulgated or incorporated into the Model Law.

## 1. Preliminary Provisions

### 1.1 Definitions of Terms

#### **Purpose:**

To define certain terms used frequently in this Act or that are basic to its understanding.

#### **Content:**

1. In interpreting this Act, the following definitions shall apply:
  - a. “Applicable Laws” shall mean all applicable laws, ordinances, regulations, rules, administrative orders, decrees and policies of any government, governmental agency or department of the country, block of countries or political subdivision in which the Financial Service Provider is located, or elsewhere, applicable to the Financial Service Provider.
  - b. “The Board” shall mean the highest level governing body of a Financial Service Provider.
  - c. “Client” shall mean an individual, or micro, small or medium-sized business that is a current or prospective customer of a Financial Service Provider.
  - d. “Complaint Handling Unit” shall mean the internal Client complaint mechanism established within a Financial Service Provider, as required by this Act.
  - e. “Consumer Financial Product(s) and/or Service(s)” shall mean any or all financial product(s) or service(s) generally marketed, sold or provided to Clients.
  - f. “Consumer Financial Protection Laws” shall mean this Act, [*enumerate all pre-existing consumer financial protection laws*], and any regulations, rules, guidance, administrative orders, decrees and policies issued under the aforementioned laws.
  - g. “Credit Reporting Systems” shall mean the providers of credit reporting or registration services in the jurisdiction in which a Financial Service Provider is located or any providers, organizations or systems designated by the Supervisory Authority.
  - h. “Declining Balance Calculation Method” shall mean that the interest charged on any loan payment is to be calculated based on the current outstanding principal and accounting for all payments made in previous periods.
  - i. “Financial Service Provider” shall mean any provider of Consumer Financial Products or Services for the retail market regardless of the organization’s corporate form and primary business lines, whether or not it is prudentially licensed, and whether it is run for private gain or for charitable purposes, including without limitation, public and private banks, credit unions, microfinance

institutions, money lenders, digital financial service providers, e-money issuers, money transfer companies, and when applicable, retail stores, post offices and pawn shops.

- j. “Key Facts Statement” shall mean a discrete, highly conspicuous section of a disclosure document highlighting important information pursuant to this Act and any regulations promulgated by the Supervisory Authority.
  - k. “Non-Public Client Data” shall mean information about Clients that the Financial Service Provider collects in connection with providing Consumer Financial Products or Services. Non-Public Client Data includes written data, as well as photographic and biometric information. Non-Public Client Data does not include information that is available from public sources.
  - l. “Pricing Procedures” shall mean the written internal procedures for setting Consumer Financial Product and Service prices by the Financial Service Provider.
  - m. “Privacy Laws” shall mean all applicable regulations and statutes that govern the collection, storage and release of a Client’s financial or personal information.
  - n. “Privacy Policy” shall mean a Financial Service Provider’s written internal policies and procedures for protecting the privacy of Non-Public Client Data.
  - o. “Standardized Interest Rate” shall mean the interest rate calculated in consideration of the total cost of a Consumer Financial Product or Service, expressed in a single rate only, and in accordance with any applicable calculation schedule promulgated by the Supervisory Authority.
  - p. “Supervisory Authority” shall mean the governmental authority created under this Act to regulate the offering, sale and provision of Consumer Financial Products or Services and the conduct of Financial Service Providers towards Clients.
2. The Supervisory Authority may interpret or define any term not defined in this section through rulemaking.

## 1.2 Scope of Application

### **Purpose:**

To define the scope of application for this Act.

### **Content:**

1. This Act applies to all Financial Service Providers. Financial Service Providers are accountable for any violations of this Act in connection with their Consumer Financial Products or Services so long as these violations occur as a result of the acts or omissions of their managers, employees, agents or third party service providers.

2. This Act applies to all Consumer Financial Products and Services offered or provided on or after [*the day of enactment of this law*], irrespective of whether the Financial Service Provider resides or has its principal office within or outside [*X Country*].
3. This Act shall not apply to a Consumer Financial Product or Service that is offered or provided if:
  - a. the recipient of such Consumer Financial Product or Service is—
    - i. a company or corporate body whose asset or turnover value equals or exceeds [*the threshold determined by the Supervisory Authority*], or
    - ii. a legislative or judicial body;
  - or
  - b. the Financial Service Provider is [*the central bank or other government body engaged in implementing monetary policy or issuing currency*].
4. This Act does not apply to any unincorporated group saving schemes or one-time, non-commercial transactions between individuals in a non-commercial setting.

**Commentary:**

- a) Excluded Types of Financial Activity. While the Model Law applies broadly to all providers of Consumer Financial Products and Services, this section is designed to exclude informal types of lending from coverage under the Model Law, as well as commercial activity amongst large, sophisticated businesses. Excluded informal activity means one-time, non-commercial transactions, such as one-time loans between two family members. However, peer-to-peer lending and other direct Client-to-Client financial activity should be covered where the transaction is facilitated by a Financial Service Provider.
- b) Agents and Third-Party Service Providers. Financial Service Providers are, in general, responsible for the conduct of all their employees, agents and third-party service providers that interact with Clients for the benefit or at the direction of the Financial Service Provider. However, such employees, agents and third-party service providers may also, when appropriate, be made individually accountable for violations they have committed or facilitated.

## **2. The Supervisory Authority**

### **2.1 Establishment of the Supervisory Authority**

**Purpose:**

To create a discrete authority to implement and enforce Consumer Financial Protection Laws and prevent harm to Clients.

**Content:**

1. There is hereby established [*as an independent agency*][or][*as a department within X*] a Supervisory Authority which shall regulate the offering, sale and provision of Consumer Financial Products and Services and the conduct of Financial Service Providers towards Clients.
2. The objective of the Supervisory Authority is to prevent harm to Clients.

**Commentary:**

- a) Importance of a Strong Regulator. Well-written Consumer Financial Protection Laws are of no use without a capable regulator overseeing and enforcing them. Not only must there be a regulator in place, capable of examining and supervising Financial Service Providers for compliance with Client protection rules, but that regulator must be able to promulgate new rules and guidance. The conduct of Financial Service Providers and Clients, as well as the legal context, differs dramatically from jurisdiction to jurisdiction; there must be continuous field-level monitoring to study the market place and to tailor compliance requirements to the jurisdiction's specific legal and business environment, accompanied by continuous monitoring of international benchmarks and best practices.
- b) Dedicated Staff. The Supervisory Authority, to maintain its focus on Clients, should be either a stand-alone agency or a department inside another agency with a dedicated staff focused solely on Client protection. In recent years, especially since the 2008 global financial crisis, countries around the world have moved towards having a dedicated Client protection staff, sometimes in an independent agency and sometimes as a department within another regulator. For example, the United States and the United Kingdom have newly established agencies focused exclusively on consumer financial protection. Malaysia, on the other hand, has established a dedicated consumer and market conduct department within its central bank.
- c) Client Protection as a Discrete Function. Prudential regulation differs dramatically from Client protection regulation in that prudential regulation focuses on the economic health of institutions and the financial system. Client protection regulation, on the other hand, focuses on the individual financial products, the way they are marketed, sold and serviced and their impact on Clients. Therefore, the Client protection staff should focus on protecting Clients and regulating the market conduct of Financial Service Providers towards Clients, and should have the authority to supervise Financial Service Providers whether or not those Financial Service Providers are prudentially supervised. Some Financial Service Providers (such as non-depository microfinance institutions) that should be supervised for Client protection purposes will pose minimal prudential risk and thus should not be subject to prudential supervision at all.
- d) Other Provisions Required for Implementation. Enacted legislation establishing a new regulator, or a new department within an existing government agency, will

require additional provisions. Provisions addressing funding and internal governance should be drafted in accordance with the relevant legal and political context.

- e) Pre-existing Regulator. A number of jurisdictions have already created specific financial consumer protection regulators. Where an appropriate regulator is already in place, the language of this section should be changed from establishing a new agency to, instead, explicitly empowering the existing regulator with the authorities and powers contained in the remainder of this Act.

## 2.2 Authority and Jurisdiction

### **Purpose:**

To grant the Supervisory Authority exclusive rulemaking authority for Consumer Financial Protection Laws and supervisory jurisdiction over all providers of Consumer Financial Products or Services.

### **Content:**

1. The Supervisory Authority shall have exclusive rulemaking authority for all Consumer Financial Protection Laws, including but not limited to, protections related to all Consumer Financial Products and Services.
2. The Supervisory Authority may prescribe rules covering and engage in supervision of all Financial Service Providers.

### **Commentary:**

- a) Independence of the Supervisory Authority and Exclusive Rulemaking. To avoid regulatory turf battles and questions of authority, the Supervisory Authority should be given exclusive rulemaking power for all Consumer Financial Protection Laws. Final legislation should specifically enumerate any pre-existing Consumer Financial Protection Laws in the definitions section.
- b) Consistent Standards. As much as possible, all providers of similar Consumer Financial Products or Services should be held to similar and proportional Client protection standards. Creating specialized regimes and applying more stringent requirements on certain types of Financial Service Providers encourages regulatory arbitrage. Financial Service Providers may seek whichever license or formation type will allow them to avoid the most costly compliance. In many countries, for example, unregulated pawn shops are major providers of consumer credit. Applying the same set of Client protections across Consumer Financial Products and Services ensures that all Financial Service Providers are subjected to the same rules. This levels the playing field among all Financial Service Providers offering similar Consumer Financial Products or Services, be they banks, microfinance institutions, credit unions or other providers, even those currently not regulated. For this same reason, it is also advisable that a single regulatory body be responsible for supervising all Financial Service Providers for Client protection purposes. Multiple agencies, even if



implementing the same rules, are less likely to provide consistent treatment across Financial Service Providers than a single regulator would.

- c) Amendment of General Consumer Protection Law. If a pre-existing general consumer protection law that addresses non-financial as well as Consumer Financial Products or Services with jurisdiction over all significant Financial Service Providers is in place, that general legislation should be amended to no longer cover Consumer Financial Products and Services for several reasons. First, general consumer protection bodies often have little regulatory capacity to appropriately supervise financial products and instead tend to prioritize health, safety and fraud concerns. Second, overlapping jurisdiction between the Supervisory Authority and a general consumer protection body should be avoided. Such overlap leads to greater uncertainty and compliance costs for Financial Service Providers and may lead to the unnecessary expenditure of agency resources on regulatory turf battles.

### 2.3 General Powers

#### **Purpose:**

To grant the Supervisory Authority the basic powers needed to regulate Financial Service Providers.

#### **Content:**

1. Registration:
  - a. The Supervisory Authority may:
    - i. In compliance with [*Section 2.3(4) Coordination*], require the registration of Financial Service Providers; and
    - ii. Upon a finding that a Financial Service Provider is in violation of Consumer Financial Protection Laws, suspend or revoke the Financial Service Provider's registration.
2. Supervision:
  - a. The Supervisory Authority may require reports from, and conduct examinations of, all Financial Service Providers for the purposes of:
    - i. Assessing compliance with Consumer Financial Protection Laws;
    - ii. Obtaining information about the activities, practices, policies and procedures of the Financial Service Provider; and
    - iii. Detecting and assessing risks to Clients and to markets for Consumer Financial Products and Services.

3. Market Monitoring:
  - a. The Supervisory Authority may:
    - i. Require reports, as needed, from the third party agents and service providers of Financial Service Providers and industry associations;
    - ii. Access relevant data about Consumer Financial Products and Services and markets from other government agencies; and
    - iii. Produce and publish reports on the financial services industry's Client protection performance.
4. Coordination:
  - a. The Supervisory Authority shall:
    - i. To the extent reasonably possible, coordinate examinations with prudential regulators, other government agencies, independent certification bodies and industry associations, as appropriate; and
    - ii. To the extent reasonably possible, coordinate the content, timing, form and collection of required reports and applications with prudential regulators, other government agencies, independent certification bodies and self-regulatory bodies, as appropriate.

**Commentary:**

- a) Requiring Registration. All Financial Service Providers should be required to register. While deposit-taking Financial Service Providers are generally required to obtain bank licenses, many countries have no license or registration requirement for non-deposit taking, lending-only Financial Service Providers. This omission is generally a reflection of the low risk such Financial Service Providers pose from a prudential perspective. However, to ensure a level playing field from a Client protection perspective, all Financial Service Providers should be subject to regulation. A registration requirement ensures that the Supervisory Authority is aware of the Financial Service Provider and that it meets minimum requirements. Financial Service Providers not subject to prudential supervision should register directly with the Supervisory Authority as their sole regulator. Financial Service Providers subject to prudential supervision are likely already licensed by the agency overseeing their safety and soundness. The Supervisory Authority should coordinate with prudential regulators to minimize duplicative filing requirements and allow bank licenses and similar regulatory approvals to satisfy the registration requirement of this section.

Regulations giving greater definition to the registration requirement should be promulgated by the Supervisory Authority. Such regulations should provide a detailed registration process and specify size or activity level thresholds under which registration is not required. Failure to meet registration requirements should lead to

denial of a registration application, and failure to maintain any such requirements should lead to suspension or revocation of the registration.

- b) Reporting Requirements. The Supervisory Authority may require regular reports from all covered Financial Service Providers. These reports provide regulators with information about the state of the market and can help flag potential trouble areas. However, because the administrative costs of reporting may be high, smaller Financial Service Providers should be held to less frequent and simpler reporting requirements than larger and more complex Financial Service Providers. At a minimum, Financial Service Providers should be required to report pricing data, information on Client complaints and incidents of default.
- c) Coordination and Consultation. Coordination and consultation with other regulators can help ease the regulatory burden on Financial Service Providers and therefore help keep compliance costs down. Regulators should, to the fullest extent possible, synchronize, share and harmonize all required reports and examinations to avoid duplicative processes. Where industry associations are present, such organizations should be seen as important sources of reporting standards, market intelligence and analysis. Especially in regards to market monitoring, industry associations may already provide comprehensive information. Where this is the case, the Supervisory Authority should avoid creating duplicative processes and instead coordinate and consult with these industry associations.

## 2.4 Enforcement Powers

### **Purpose:**

To grant the Supervisory Authority a range of enforcement powers.

### **Content:**

1. The Supervisory Authority may take any or all of the following steps upon a substantiated finding that a Financial Service Provider is in violation of a Consumer Financial Protection Law:
  - a. Require the Financial Service Provider to sign a memorandum of understanding and agreement;
  - b. Publish the names of offenders;
  - c. Assess monetary penalties reflecting the harm done to Clients;
  - d. Require the Financial Service Provider to refund excess charges;
  - e. Require the Financial Service Provider to correct any erroneous data, information or statements;

- f. Prohibit the Financial Service Provider from offering a particular Consumer Financial Product or Service or class of Consumer Financial Products or Services;
- g. Restrict the ability of the Financial Service Provider to continue to collect fees or charges in connection with a particular Consumer Financial Product or Service or class of Consumer Financial Products or Services;
- h. Remove Financial Service Provider officials responsible for violations and ban them from working for any Financial Services Provider;
- i. Place a non-prudentially supervised Financial Service Provider into conservatorship or recommend that a prudentially supervised Financial Service Provider be placed into conservatorship; or
- j. Refer the matter to criminal authorities for prosecution.

**Commentary:**

- a) Finding Violations. The Supervisory Authority should be careful that enforcement actions are aimed at efficiently and effectively correcting market practices while ensuring that Clients maintain access to financial services. A finding of wrongdoing must be made in accordance with the existing laws and customs in the adopting country. In general, a substantiated finding will be the result of an administrative process that is clearly defined and articulated, and involves more than one person evaluating the relevant evidence. To promote fairness and build the credibility of the Supervisory Authority, regulators should embrace transparency by clearly articulating their policies, procedures and expectations to all Financial Service Providers and by specifying what amounts to a violation in more specific regulations or through administrative adjudications with precedential value.
- b) Alternate Enforcement Mechanisms. The Model Law does not include provisions providing the right of individuals or groups to use the judicial system to enforce any rules or provisions in courts. In adopting the Model Law, legislators should consider whether or not such a right should be provided in conjunction with any or all provisions. That decision should be informed by the capacity of regulators, the effectiveness of the judicial system and the other particular circumstances of the country.

**2.5 Rulemaking**

**Purpose:**

To empower the Supervisory Authority to promulgate regulations.

**Content:**

1. The Supervisory Authority may prescribe rules and issue standards, guidance or orders to carry out the purposes and objectives of the Consumer Financial Protection Laws, and to prevent evasions thereof.
2. Without limiting the generality of the section above, standards and rules promulgated under that section may address:
  - a. Appropriate product design and delivery;
  - b. Prevention of over-indebtedness;
  - c. Transparency;
  - d. Responsible pricing;
  - e. Fair and respectful treatment of Clients;
  - f. Privacy of Client data; and
  - g. Mechanisms for complaint resolution.
3. In promulgating rules and setting standards the Supervisory Authority must consider:
  - a. The potential benefits and costs to Clients, including the positive benefits of financial services; and
  - b. The financial impact on Financial Service Providers related to compliance costs and any reduction in financial access.

**Commentary:**

- a) Rule-Based and Principle-Based Regulation. Consumer financial protection regulation, broadly speaking, encompasses two approaches: 1) rule-based regulations where legislators or the regulator issue specific directives or prohibitions; and 2) principle-based regulation where regulators use a degree of discretion to assess a Financial Service Provider's compliance with subjective standards. Each approach has strengths and weaknesses. While rule-based regulation provides clarity to Financial Service Providers, it allows less room for regulators to tailor their expectations to the level of risk actually posed in a specific circumstance. Similarly, while principle-based supervision gives regulators an opportunity to assess the actual risk that practices and products pose, the uncertainty inherent in more subjective regulation may increase the compliance costs for Financial Service Providers and regulators in ways that are disproportionate to the chances for harm to Clients. The Supervisory Authority should seek to use each approach appropriately, mindful of their respective strengths and weaknesses. The best solutions in a particular country will depend on preexisting regulatory approaches and the capacity of the regulator.

Where the capacity of the Supervisory Authority is relatively limited and close market monitoring and institutional supervision is difficult, laws and regulations should be more heavily rule-based. The Model Law, in the sections that follow, utilizes both rules-based and principles-based approaches, in some areas mandating clear laws, and in other areas empowering the Supervisory Authority to assess the market conduct of Financial Service Providers and define best practices over time through adjudicative processes.

- b) Broad Authority. The Supervisory Authority should have broad authority to set standards related to any point in the product life cycle (from design and conception of the product, to advertising and sale practices) and through the duration of the contract. The financial services industry is in a constant state of evolution. New products and approaches are always emerging. The classic consumer protection approach focused exclusively on disclosure at the time of purchase, and “buyer beware” has proven unable to protect Clients in the ever changing marketplace. To correct harmful practices as they emerge, the Supervisory Authority needs to be able to address issues that may arise throughout a Financial Service Provider’s relationship with a Client.
- c) Risk-based and Proportionate Regulation. There is great variety in the risk posed to Clients by different Consumer Financial Products and Services and Financial Service Providers. The Supervisory Authority should adopt a philosophy of risk-based and proportionate regulation, with the regulatory burden imposed on Financial Service Providers, in terms of disclosure and reporting requirements, as well as supervision and examination processes, reflecting the probability and potential magnitude of harm to Clients.
- d) Product Design. While the Supervisory Authority is granted powers to promulgate rules related to appropriate product design and delivery, actual product design should be left in the hands of Financial Service Providers. Regulations should be focused, instead, on ensuring proper internal controls are in place within Financial Service Providers to facilitate appropriate design and delivery.

### **3. General Requirements for Financial Service Providers**

#### **3.1 Prohibited Acts**

**Purpose:**

To prohibit Financial Service Providers from operating without a valid registration or in violation of Consumer Financial Protection Laws.

**Content:**

- 1. It shall be unlawful for any Financial Service Provider:
  - a. To offer or provide Consumer Financial Products or Services without a valid registration under [*Section 2.3(1) Registration*];

- b. To offer or provide any Consumer Financial Product or Service in violation of a Consumer Financial Protection Law or commit any act or omission in violation of a Consumer Financial Protection Law;
- c. To engage in any unfair, deceptive or abusive act or practice;
- d. To provide a credit product to any person below the age at which a person may enter into contracts unless his/her legal guardian is also a party to the credit agreement; or
- e. To fail or refuse to take any action required by any Consumer Financial Protection Law or any rule or order issued by the Supervisory Authority.

**Commentary:**

- a) Unfair, Deceptive or Abusive Acts and Practices. Note that while [*Section 2.5 Rulemaking*] grants the Supervisory Authority the power to issue rules aimed at preventing harmful behavior, this section contains a broad prohibition on unfair, deceptive or abusive acts or practices. This gives the Supervisory Authority broad authority to step in and stop the most malicious practices when they are detected, without relying on specific guidelines covering the behavior. However, this authority comes at the price of added uncertainty for Financial Service Providers. The Supervisory Authority should, over time, develop more concrete and specific guidance in regulations or directives as to what acts and practices are unfair, deceptive or abusive. This guidance should be made in consultation with industry and stakeholder groups, and in consideration of best practices and local context.
- b) Examples of Prohibited Behaviors. The following general behaviors are illustrative of the types of conduct prohibited as unfair, deceptive or abusive: the use of abusive language; the use of physical force; limiting physical freedom; shouting at a Client; entering a Client's home uninvited; publicly humiliating a Client; violating a Client's right to privacy; discriminating based on ethnicity, gender, sexual orientation, religious belief, political opinions or disability; participating in corruption, kickbacks or theft; and participating in sexual or moral harassment. In promulgating regulations under the prohibition on unfair, deceptive or abusive acts or practices, or in initiating enforcement actions under such regulations, the Supervisory Authority should target the most egregious practices.

**3.2 Board and Senior Management Oversight**

**Purpose:**

To require that all Financial Service Providers have an internal compliance management system in place that effectively ensures conformity with Consumer Financial Protection Laws.

**Content:**

1. The Board or a committee of the Board of each Financial Service Provider must ensure that appropriate systems and processes are in place to maintain compliance with Consumer Financial Protection Laws.

**Commentary:**

- a) The Financial Service Provider is Primarily Responsible for Compliance. Financial Service Providers themselves bear the primary responsibility for ensuring compliance with Consumer Financial Protection Laws and Client protection rules. The Board should be vigilant in ensuring that policies and procedures are in place to follow all relevant Consumer Financial Protection Laws and Client protection rules. Most issues should be self-identified by the Financial Service Provider and corrective action should be implemented independently. Ensuring compliance by their managers, employees, agents and third party service providers should be an integral part of the day-to-day operations of the Financial Service Provider.
- b) Internal Compliance Systems. Requiring Financial Service Providers to formulate an internal compliance management system not only increases the chances the Financial Service Providers will be in conformity with Consumer Financial Protection Laws, but also provides an important tool for regulators. Financial Service Providers should be given flexibility to design compliance systems that fit their size and product class, but in general, an effective program will include top-management oversight, employee training, mechanisms to respond to Client complaints and regular compliance audits.
- c) Supervisory Strategy. The Supervisory Authority should examine the internal controls put in place by Financial Service Providers and focus regulatory attention in areas where these controls are the weakest.

## **4. Appropriate Product Design and Delivery**

### **4.1 Product Risk Management**

**Purpose:**

To require Financial Service Providers to continuously evaluate their Consumer Financial Products and Services and their practices related to the provision of such Consumer Financial Products and Services to minimize the risk of harm they pose to Clients.

**Content:**

1. Financial Service Providers must have adequate written policies and procedures to prudently manage the risks of harm to Clients associated with the Consumer Financial Products and Services offered by the Financial Service Provider. At a minimum, such policies shall:



- a. Identify and control product risk across the value chain including during product and service development, authorization, pricing, marketing, sale, distribution, portfolio management, accounting and ongoing service and maintenance;
- b. Set out a product design and pricing philosophy, including which product and service lines the Financial Service Provider can offer, will offer, or is restricted by law or regulation from offering. This philosophy should reflect corporate strategy, competitive positioning, risk/reward philosophy and the financial capacity of the Client to absorb losses;
- c. Provide for staff training on the appropriate delivery of Consumer Financial Products and Services. This training should include the evaluation of the suitability of products and services for Clients in terms of the individual Client's ability to meet the obligations of a Consumer Financial Product or Service with a low probability of serious hardship and a reasonable prospect that the product or service will provide value to the Client;
- d. Include mechanisms for confirming that the terms and conditions of Consumer Financial Products or Services are adequately understood by Clients;
- e. Define the target Client for each type of Consumer Financial Product or Service offered; and
- f. Define the process for the authorization and introduction of new Consumer Financial Products and Services, including clear identification of decision makers and the process for evaluating the products' or services' affordability and suitability for prospective Clients.

**Commentary:**

- a) Continuous Internal Monitoring. Financial Service Providers themselves are best positioned to identify the risks presented by their Consumer Financial Products and Services and to implement corrective action. This section requires that Financial Service Providers have internal systems in place that consider the risks their Consumer Financial Products and Services pose before they hit the markets and that they continue to monitor for risks during every stage of the product or service life cycle. Such a system must, at a minimum, ensure that employees are adequately trained and monitoring processes are in place to ensure that Consumer Financial Products and Services are appropriately targeted to the risk appetites and tolerances of both their markets and their Clients.

**4.2 Affordability and Suitability Assessments**

**Purpose:**

To require Financial Service Providers to have suitability and affordability procedures for all Consumer Financial Products and Services.

**Content:**

1. Financial Service Providers must:
  - a. Have written procedures for determining whether a particular Consumer Financial Product or Service is suitable and affordable for a Client; and
  - b. Determine whether the amount and terms of an offered Consumer Financial Product or Service allow the Client to meet the obligations of the Consumer Financial Product or Service with a low probability of serious hardship and a reasonable prospect that the Consumer Financial Product or Service will provide value to the Client.
2. Any contract for a Consumer Financial Product or Service offered or provided in violation of this section shall be invalid and unenforceable against the Client.

**Commentary:**

- a) Affordability Assessments. Instead of prescribing specific numerical debt caps or debt ratios, the above provision requires Financial Service Providers to conduct an affordability assessment. If that assessment finds that the Client cannot reasonably meet obligations without substantial hardship the Consumer Financial Product or Service should not be provided to the Client. This approach gives Financial Service Providers and regulators more flexibility than a mandated debt ratio or cap, while keeping the option open for the Supervisory Authority to craft more specific requirements as they gain experience and market data becomes available.
- b) Example. South Africa's National Credit Act requires lenders to perform an affordability assessment and determine that the Client has the ability to repay in a "reasonable time". Lenders who fail to do so are unable to enforce the financial contract against the borrower.

**4.3 No Waiver of Rights**

**Purpose:**

To prohibit Financial Service Providers from requiring Clients to waive rights as a condition to receiving a Consumer Financial Product or Service.

**Content:**

1. No provision of a contract for a Consumer Financial Product or Service shall be lawful or enforceable if it waives or otherwise deprives a Client of a legal right to sue the Financial Service Provider, receive information, have their complaints addressed and resolved, have their Non-Public Client Data protected or cancel the use of the Consumer Financial Product or Service without an unreasonable penalty.

**Commentary:**

- a) Arbitration Clauses. This section prohibits arbitration clauses where a Client waives the right to sue in court and agrees to only pursue action against the Financial Service Provider in arbitration. However, arbitration itself is often beneficial for both the Client and Financial Service Provider. In many contexts, arbitration programs may be better for Clients than more elaborate formal dispute resolution mechanisms. The Supervisory Authority may wish to adopt modified guidelines providing for the waiver of certain rights in writing with the informed consent of the Client. However, regulators using this type of modified guideline should consider prohibiting the use of a waiver of rights as a bargaining mechanism, such as a situation where a Financial Service Provider offers a lower interest rate to a Client willing to waive certain rights.

**4.4 Rescission Period**

**Purpose:**

To mandate a period during which a Client can rescind a contract for a Consumer Financial Product or Service and have any fees and advances returned.

**Content:**

1. Financial Service Providers must provide Clients the right to terminate any contract for Consumer Financial Products or Services within a reasonable time after the date on which the contract was executed, or within the time period, if any, promulgated by the Supervisory Authority for that Consumer Financial Product or Service.
2. When a contract for a consumer financial product or service is terminated under the terms of this section, the Financial Service Provider:
  - a. Must refund any money the Client has paid under the contract within a reasonable time after the delivery of the notice to terminate;
  - b. Must cancel any automatic payment plans and give notice of termination to any Credit Reporting Systems to which the credit agreement has been reported; and
  - c. May only require payment from the Client of a reasonable fee to compensate it for the costs incurred.
3. Financial Service Providers must provide notice of the Client's right of rescission in all contracts and disclosures regarding Consumer Financial Products and Services.

**Commentary:**

- a) Reasonable Time. Under this section, Clients are provided a cooling-off period that allows them to consider the costs and risks of a Consumer Financial Product or Service free from the pressure of a sales team. The length of the cooling-off period should be determined by the individual Financial Service Provider based on a

reasonable expectation of the time required for a Client to fully evaluate all the terms and risks of the Consumer Financial Product or Service and contact others who may be affected by its terms and conditions (such as family members or business partners). Similarly, the method and processes for rescission should be determined by the individual Financial Service Provider based on the Consumer Financial Product or Service and the local context. The Supervisory Authority should evaluate these rescission programs for reasonableness and fairness, particularly the ease with which the Client may invoke the rescission without burdensome requirements. The reasonableness of a rescission period is likely to differ from product to product, and may encompass more than just a set time period. For example, a reasonable rescission period for loans may be limited to the time before the funds are disbursed. It may be useful for the Supervisory Authority to, based on the local circumstances, set rescission periods for certain products or a minimum length of a rescission period.

- b) Reasonable Fee. Upon termination under this section, the Client should receive a refund. The Financial Service Provider may withhold from this refund a fee that is no greater than actual costs incurred by the Financial Service Provider in providing the product or service to the Client prior to termination.

## **5. Preventing Over-Indebtedness**

### **5.1 Creditworthiness Assessments**

#### **Purpose:**

To require Financial Service Providers to assess creditworthiness before extending credit.

#### **Content:**

1. Before contracting with a Client for a Consumer Financial Product or Service extending credit valued at or exceeding [*the threshold determined by the Supervisory Authority*], the Financial Service Provider must:
  - a. Conduct a comprehensive assessment of the Client's overall indebtedness by obtaining information on outstanding debt obligations;
  - b. Obtain a reliable statement of the Client's expected income over the course of the Consumer Financial Product or Service;
  - c. Determine whether the amount and terms of the offered Consumer Financial Product or Service allow the Client to meet the obligations of the Consumer Financial Product or Service with a low probability of serious hardship and a reasonable prospect that the product will provide value to the Client; and
  - d. Document the basis for approval of the transaction including the results of the analysis required under this section.

2. Any contract for a Consumer Financial Product or Service offered or provided in violation of this section shall be invalid and unenforceable against the Client.

**Commentary:**

- a) Greater Requirements for Credit Products. While Financial Service Providers should have written suitability and affordability procedures for all Consumer Financial Products or Services, the inherent risk of over-indebtedness associated with credit products necessitates more stringent requirements. Here, the extension of a credit product requires the Financial Service Provider to first perform a thorough evaluation, including a credit assessment through a Credit Reporting System, if possible, and document the basis for approving the transaction.

## 5.2 Mandated Credit Reporting

**Purpose:**

To mandate that Financial Service Providers supply account information to a Credit Reporting System, if one exists, in order to increase the effectiveness of creditworthiness assessments.

**Content:**

1. Upon entering into or amending a contract for a Consumer Financial Product or Service extending credit valued at or exceeding [*the threshold determined by the Supervisory Authority*], the Financial Service Provider must make a report, in the prescribed format and within the prescribed time, to a Credit Reporting System servicing its geographical location and product categories, if one exists.
2. A Financial Service Provider must report the particulars of the termination, satisfaction, default or entering into arrears of any contract for a Consumer Financial Product or Service extending credit valued at or exceeding [*the threshold determined by the Supervisory Authority*] to a Credit Reporting System in a timely fashion.
3. Financial Service Providers who detect, discover or are notified of any inaccurate information they have provided to a Credit Reporting System must provide corrected information to the Credit Reporting System as soon as possible.
4. The Supervisory Authority may facilitate the establishment of a Credit Reporting System, if none is currently available, to service all Financial Service Providers covered by this Act.

**Commentary:**

- a) Credit Reporting Systems. In order to effectively perform a creditworthiness assessment, Financial Service Providers need to verify the total outstanding debt obligations of the Client. The Supervisory Authority should ensure that effective and efficient Credit Reporting Systems are in place. In addition to helping prevent over-

indebtedness, a functioning Credit Reporting System advances financial inclusion by allowing borrowers to create and benefit from reputation collateral. However, it must be noted that Financial Service Providers with small loan volumes or relatively small loan sizes may find the costs of obtaining a credit report disproportionate to the size of the loan. The Supervisory Authority should be aware of this problem and seek to develop a Credit Reporting System that will meet the needs of all Financial Service Providers. Policy makers may want to consider assisting in the process of both establishing Credit Reporting Systems and enabling smaller lenders to incorporate the use of such systems into their business. This is not a regulatory function, but the importance of Credit Reporting Systems to Client protection suggests that governments may wish to encourage their development and use. Additional legislation for the establishment and operation of such systems may be needed but is outside of the scope of this Model Law. For more guidance on Credit Reporting Systems please see the World Bank's General Principles for Credit Reporting (2011).

- b) In the Absence of a Credit Reporting System. Notwithstanding the provisions herein safeguarding Non-Public Client Data, when there is no formal Credit Reporting System servicing the Financial Service Provider's geographical location or Consumer Financial Product or Service categories, Financial Service Providers should be required to disclose to other Financial Service Providers, upon a request accompanied by a legitimate and verifiable need for the information, the total outstanding balance and payment obligations of a Client and any relevant negative payment information. Efforts should be taken to protect the confidentiality of this information. Clients should be informed of the nature of any such disclosure of account data, including the identity of all recipients of the data.
- c) Need for Integration. Where there are multiple Credit Reporting Systems in operation, the information collected should be shared with all Credit Reporting Systems, to the extent practical. This will maximize the comprehensiveness of the data and the effectiveness of creditworthiness assessments. Such information sharing will also remove the need for Financial Service Providers themselves to supply information to, or receive information from, multiple Credit Reporting Systems and will allow providers of Credit Reporting services to compete on the amount of value added instead of how much data they have acquired.
- d) Amendment of Bank Secrecy and Data Protection Laws. In many countries, bank secrecy and data protection laws restrict the sharing of Client information, including Non-Public Client Data. Where such rules are in place, they should be amended to allow for disclosure to Credit Reporting Systems or to other Financial Service Providers if no Credit Reporting System exists.

## 6. Transparency

### 6.1 Disclosure Principles

#### **Purpose:**

To prescribe basic principles for communicating the terms and conditions of Consumer Financial Products or Services and to empower the Supervisory Authority to issue product-specific disclosure requirements.

#### **Content:**

1. Financial Service Providers must ensure that, in their communications with Clients, they adopt the following disclosure principles:
  - a. Clear and Concise Disclosures in Simple Language. Information about Consumer Financial Products and Services must be expressed in simple language and presented in a clear and reasonably understandable format.
  - b. Timeliness. A Client must be provided with the most up-to-date information at the moments that information will be most useful for the Client. This requirement applies to information provided in advertisements, during the pre-contractual stage, at the point of entering into a contract and during the term of the contract.
  - c. Accurate and Relevant Information. The information provided must be true, accurate and relevant.
  - d. Key Facts Statement. The information most helpful to Clients should be highlighted in a “Key Facts Statement,” a discrete, compact but highly conspicuous section of any disclosure form.
  - e. Consistent and Comparable. Disclosures should be made in a consistent manner to facilitate comparison between similar Consumer Financial Products and Services.
2. The Supervisory Authority may issue product-specific disclosure requirements to implement the above principles by mandating specific disclosure practices for any specific category of Consumer Financial Products or Services.

#### **Commentary:**

- a) Specific Disclosure Requirements. While the principles enumerated here reflect the best practices applicable to all Consumer Financial Products and Services, the specific information Clients need, and when they need it, may differ among such product and service categories. In the absence of more specific requirements, Financial Service Providers should determine which information is most important and relevant. And, to promote consistency and comparability, the Supervisory Authority should monitor the marketplace, research Client behavior and decision-

making and seek to identify the specific disclosure requirements that should be made applicable within specific product categories.

- b) Key Facts Statement to Highlight Important Information. Disclosure of information is only effective to the extent it is comprehensible and relevant to the Client's decision-making process. Too much information (overload) reduces the usefulness of disclosure. Thus, the disclosure principles specifically require that the most important information be highlighted. Annex 3 contains examples of Key Facts Statements.
- c) The Client's Language. In jurisdictions where more than one language is spoken, the principle of providing disclosures in simple language must be viewed as a requirement to provide disclosures in the language of the target Client. Further, where target Clients are less likely to be literate, this principle requires that the disclosures be made orally and with materials specifically designed to communicate the information to an illiterate Client.
- d) Contents of Contracts. The disclosure principles have important implications for the contents of contracts for Consumer Financial Products and Services. As part of the requirement to be accurate, clear and concise, these contracts should not contain illegal or unenforceable clauses or provisions. Similarly, these contracts may not be overly long, convoluted or burdensome. If the contract contains terms that conflict with any disclosure, such as a Key Facts Statement, frequently asked questions document, or other disclosure document regarding the Consumer Financial Product or Service, the disclosure document shall control the contract.
- e) Timeliness and Regular Account Statements. For some Consumer Financial Products and Services with multiple payment periods, the principle of timeliness will require regular account statements to be delivered to the Client over the lifecycle of the product. Generally, this will include monthly or quarterly account statements of any outstanding balance and fees charged during the applicable period. To ensure Clients receive these periodic account statements, they should be offered multiple delivery methods to receive the statements, including via paper format or electronically. Where account statements are readily accessible to a Client electronically, regular paper statements may be unnecessary. Clients should be provided with at least one free account statement per period, but Financial Service Providers may charge reasonable fees for duplicate account statements.
- f) Disclosure of Agent Relationships. The requirement for disclosure of accurate and relevant information should be read, in general, to compel agents and third party service providers to disclose to Clients the nature of their relationship with a Financial Service Provider any time they are marketing, selling or servicing Consumer Financial Products or Services, or when they are providing services, including debt collection, in connection with a Consumer Financial Product or Service.



## 6.2 Product Disclosure Form

### **Purpose:**

To require Financial Service Providers to furnish Clients with a product disclosure form based on the principles in [*Section 6.1 Disclosure Principles*].

### **Content:**

1. Before contracting for a Consumer Financial Product or Service with a Client, the Financial Service Provider must provide the Client with a product disclosure form in compliance with [*Section 6.1 Disclosure Principles*] and give the Client a reasonable amount of time to review the form before entering the contract. The product disclosure form must include:
  - a. All fees and charges that may be imposed, with all interest rates expressed as a Standardized Interest Rate;
  - b. The total, aggregated cost of the Consumer Financial Product or Service and, if the Consumer Financial Product or Service requires the Client to pay in installments, a repayment schedule for the life of the Consumer Financial Product or Service;
  - c. Key features of the Consumer Financial Product or Service including the benefits, rights and obligations the Client is entitled or subject to, or may become entitled or subject to;
  - d. Significant risks, if any, associated with the Consumer Financial Product or Service;
  - e. A summary of the Financial Service Provider's Privacy Policy;
  - f. Any costs associated with a prepayment or charges associated with late payment; and
  - g. Contact information for the Financial Service Provider's Complaint Handling Unit and the Supervisory Authority.
2. Before any changes to the terms or conditions of a Consumer Financial Product or Service, including, in the case of a credit product, changes in the interest rate, the Financial Service Provider must provide a product disclosure form documenting all modifications and their effects on the aggregated cost of the product. Changes detrimental to a Client may not come into effect unless the Client has previously consented to such changes or has an opportunity to terminate the contract for the Consumer Financial Product or Service before the detrimental change comes into effect.

3. The Financial Service Provider must provide a product disclosure form upon request by the Client at any time during the life of a Consumer Financial Product or Service.
4. Model Disclosure Forms:
  - a. The Supervisory Authority may issue model disclosure forms for specific categories of Consumer Financial Products or Services. Such forms may be used at the option of the Financial Service Provider.
  - b. Any Financial Service Provider using an accurate model disclosure form issued under this section shall be deemed to be in compliance with the applicable disclosure requirements.
5. Any contract for Consumer Financial Products or Services offered or provided in violation of this section shall be invalid and unenforceable against the Client.

**Commentary:**

- a) Product Disclosure Forms. All Financial Service Providers must provide Clients a product disclosure form in connection with any Consumer Financial Product or Service. This section outlines the minimum disclosure requirements for any financial product or service. In [*Section 6.2(4) Model Disclosure Forms*] the Supervisory Authority is authorized to produce product-specific model disclosure forms, based on the specific requirements for those specific Consumer Financial Products or Services.
- b) Total Cost of Credit and Repayment Schedules. Total cost of credit is the entire amount the borrower must repay over the life of a loan. While Clients cannot use a disclosure of total cost of credit to compare products as easily as with a Standardized Interest Rate (such as APR or EIR), multiple studies suggest that it is often easier for Clients to understand. Similarly, Clients need to have the exact information on the size and timing of repayments that is contained in a repayment schedule. Client comprehension, therefore, is furthered by mandating total cost of credit and repayment schedule disclosure in addition to a Standardized Interest Rate. However, regulators must be cognizant of the need to balance disclosure requirements that may enhance the ability of Clients to absorb information with the cost of such requirements on Financial Service Providers.
- c) Summary of Privacy Policy. [*Section 9.1 Privacy and Protection of Non-Public Client Data*] requires Financial Service Providers to develop and implement Privacy Policies. Under the provisions of this section, Providers are required to include a brief summary of that policy. Such a summary should inform the Client of any third-parties having access to Non-Public Client Data and refer the Client to where they may read the Privacy Policy in its entirety.
- d) Developing Model Disclosure Forms. While model disclosure forms have been a part of consumer protection regulation for some time, recent years have seen increased market and Client testing to refine model forms and test for Client comprehension. The Supervisory Authority should consider conducting or supporting consumer

studies in their markets to determine what visual layouts are most effective and what information is most important for Client decision making and then design model disclosure forms accordingly. Annex 4 contains a sample product disclosure form.

- e) Easier Comparisons. Where Clients are presented with identical formats for the key information for a particular class of Consumer Financial Products or Services, their ability to compare those Consumer Financial Products or Services is greatly increased. Having model forms facilitates side-by-side comparison of products and makes Clients more familiar with the terms and language used to describe the costs of Consumer Financial Products and Services.
- f) Reduced Compliance Cost. Model disclosures that provide a safe harbor give Financial Service Providers greater certainty and lower compliance costs while giving Clients a document that makes comparing offers from competing Financial Service Providers easier and more efficient.

### 6.3 Publication of Fees, Rates, Terms and Conditions

#### **Purpose:**

To authorize the Supervisory Authority's collection and publication of the interest rates and fees charged by Financial Service Providers.

#### **Content:**

1. The Supervisory Authority may require Financial Service Providers to report or publicly post their current fees, rates and other terms and conditions on a regular or continuous basis.
2. The Supervisory Authority may publish the fees, rates and other terms and conditions of Consumer Financial Products and Services in any manner designed to facilitate the ability of Clients to compare them.

#### **Commentary:**

- a) Pricing Transparency to Promote Market Competition. Providing Clients the information they need to compare Consumer Financial Products and Services is the best way to ensure consumer protection and an efficient marketplace. When Clients have the ability to shop around for the best terms and conditions, Financial Service Providers are forced to compete by offering lower prices, better products and services, and better Client treatment. While disclosure requirements mandating that certain information be given to a Client in the course of a specific transaction promote this goal, many Clients, particularly those with lower incomes, may not have the time, energy or other resources to effectively collect and compare the important aspects of various Consumer Financial Products and Services. Making fees and rates from all Financial Service Providers available to the general public can help facilitate comparison shopping and thus promote increased market competition. Further, collecting and publishing this information can assist the media, the academy and

consumer watchdogs in drawing attention to Financial Service Providers charging unusually high fees.

- b) Market Monitoring. Collecting the fees and rates charged by Financial Service Providers also provides the Supervisory Authority with a valuable market monitoring tool. Large disparities in the prices Financial Service Providers charge for similar Consumer Financial Products or Services may indicate a breakdown of competitive forces, which is a sign that Clients' ability to comparison shop has been diminished and that some sort of corrective action may be needed.

#### 6.4 Fees

**Purpose:**

To discourage Financial Service Providers from disguising the true costs of their Consumer Financial Products and Services.

**Content:**

1. Financial Service Providers shall not charge a Client fees that have not been previously disclosed to that Client.
2. Any service or penalty fee, including prepayment, early termination, set-up, documentation, or initial fees imposed by a Financial Service Provider must be reasonable.

**Commentary:**

- a) Hidden Fees. Some Financial Service Providers may attempt to disguise the true costs of their Consumer Financial Products or Services by charging fees to Clients that are not included in the pricing disclosures. Financial Service Providers should not be allowed to assess unexpected or hidden fees.
- b) Reasonableness of Fees. Whether or not a particular fee is reasonable will depend on context and circumstances, but in general a fee is reasonable if it is based on a reasonable estimate of the costs incurred by the Financial Service Provider as a direct result of the activity for which the fee is imposed.

#### 6.5 Standardized Calculation Methods

**Purpose:**

To establish a standardized way of describing the terms and conditions of Consumer Financial Products and Services.

**Content:**

1. In all communications describing the cost of or yield on a Consumer Financial Product or Service, that cost or yield must be prominently expressed as an all-encompassing Standardized Interest Rate that:
  - a. Incorporates the present value of all commitments, future or existing, agreed by the Financial Service Provider and the Client;
  - b. Incorporates the total cost of the Consumer Financial Product or Service inclusive of fees and/or compulsory insurance products or mandatory savings; and
  - c. Is expressed as a single rate only.
2. In calculating installment payments for Client credit transactions, Financial Service Providers must use the Declining Balance Calculation Method.
3. Payments made by a Client must:
  - a. Be allocated to clearing any amount in arrears before any fees and charges; and
  - b. Be allocated to the balances assessed the highest interest rate first.
4. The Supervisory Authority may amend or replace the formulas for the Declining Balance Calculation Method or Standardized Interest Rate.

**Commentary:**

- a) Standardized Disclosure Calculations. Clients should know and understand the terms and conditions of a Consumer Financial Product or Service in order to make an informed decision whether or not to purchase. However, without standardized calculations mandated for certain basic terms, Financial Service Providers may calculate such terms in a wide variety of ways, making it impossible for Clients to understand the features of Consumer Financial Products and Services or compare the true and total costs of one product to another.<sup>2</sup> Providing standardized calculation methods, especially for the calculation of interest, and defining how the interest can be expressed, are two of the most common tools used by regulators to improve Client comprehension.<sup>3</sup>

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<sup>2</sup> In many parts of the world Islamic finance is prevalent and Sharia-compliant consumer financial products are increasingly available. While much of the content of the Client Protection Principles is compatible with Islamic finance, Islamic finance's eschewing of traditional interest charges and embracing of other forms of revenue generation are not imagined by the Client Protection Principles in their current form. Because this Model Law is based on the Client Protection Principles, it contains provisions inapplicable in an Islamic finance context and no analysis has been conducted regarding how effective and appropriate the provisions of the Model Law would be as a legal framework for Islamic finance products.

<sup>3</sup> For more information on interest rate disclosures, please visit <http://smartcampaign.org/tools-a-resources/81-understanding-interest-rates>

- b) Declining Balance Calculation Method. In some countries, Financial Service Providers have adopted flat interest calculation methods, charging interest on the original loan amount at the time each installment payment is made, instead of on the current outstanding balance. This calculation method disguises the costs of the loan and leads to quoted, nominal rates that do not reflect the true price a Client is paying to borrow money. The flat interest calculation method essentially charges the Client for renting money they no longer have use of. This is contrary to the ordinary meaning of interest: the price one pays to have the use of someone else's money. Experience shows that mandating the use of the Declining Balance Calculation Method to calculate interest has an immediate impact on Clients' ability to compare products. In Peru, for example, the introduction of such a mandatory disclosure regime led to a sudden drop in prices due to Clients' increased ability to comparison shop.
- c) Standardized Interest Rate. Consumer Financial Products and Services come in a vast array of forms. In particular, Consumer Financial Products and Services are offered with a variety of compounding periods (daily, monthly, quarterly, annually and so forth). To be able to compare the true costs or yields of Consumer Financial Products or Services with different nominal interest rates, Financial Service Providers must be required to restate the interest rate using a standardized calculation. In most cases, the most appropriate method is to express the price or yield of the Consumer Financial Product or Service as an annualized rate. To make this rate as accurate a representation of the cost as feasible, all mandatory fees should be factored into the calculation. If such fees are not included in a disclosure calculation, Financial Service Providers have greater incentive to disguise the costs of the Consumer Financial Product or Service by including additional fees, making comparison more difficult.
- d) EIR and APR. Around the globe, there are two dominant methods used for standardized interest rate calculations: effective interest rate (EIR) and annual percentage rate (APR). While both methods take into account all the mandatory fees charged the Client, EIR accounts for the effects of compounding interest while APR does not. The Model Law makes no recommendation between the two methods -the Supervisory Authority should implement the calculation method that is best suited to the local context while maintaining alignment with international standards.
- e) Standardized Interest Rate Schedule. Different types of Consumer Financial Products and Services will require slightly different calculation formulas for calculating Standardized Interest Rates. The Supervisory Authority should promulgate a schedule of appropriate Standardized Interest Rate formulas while adopting a uniform approach, either EIR or APR, across all Consumer Financial Products and Services.

## 7. Responsible Pricing

### 7.1 Pricing Procedures

#### **Purpose:**

To require Financial Service Providers to set prices while taking account of Client needs and the competitive landscape.

#### **Content:**

1. Each Financial Service Provider must have written internal procedures for setting the prices for Consumer Financial Products and Services (“Pricing Procedures”).
2. Pricing Procedures must examine competitors’ prices, the cost to provide the Consumer Financial Product or Service and affordability to Clients, and must require documentation of the reasons for setting the price of each Consumer Financial Product or Service.

#### **Commentary:**

- a) Pricing Floors and Caps. In general, lawmakers should not enact usury laws, and the Supervisory Authority should not set price or interest rate floors or caps. Due to political pressure, such caps are often set too low for Financial Service Providers to be able to offer Consumer Financial Products or Services to the hardest-to-reach Clients. Further, interest rate caps often encourage Financial Service Providers to disguise the true price of their Consumer Financial Products or Services through the assessment of fees and other charges. Where adequate disclosures and other Client protections are in place and the market for Consumer Financial Products and Services is competitive, the collective force of informed Consumer choice should ensure prices are not inflated to dangerous levels. Where unreasonably high prices are present, the best long term solutions are generally to improve disclosures and to facilitate competition among service providers.
- b) Pricing Procedures. Instead of setting specific pricing limits, this section requires Financial Service Providers to have, follow and document pricing procedures. Requiring pricing procedures and documentation gives regulators a window into the rationale for why and how prices have been set. Where a Financial Service Provider’s pricing procedures are inadequate or result in harm to Clients, the Supervisory Authority should use its regulatory powers and authorities to require the appropriate corrective action.

## **8. Fair and Respectful Treatment of Clients**

### **8.1 Client Treatment Policies and Procedures**

**Purpose:**

To require Financial Service Providers to treat Clients fairly and respectfully.

**Content:**

1. General. Financial Service Providers should treat Clients with high ethical standards and with honesty, fairness and respect.
2. Non-discrimination. Client selection and treatment shall not involve discrimination on the basis of personal characteristics or personal affiliations, including race, ethnicity, origin, gender, political and/or religious affiliation, disability or sexual orientation.
3. Detection. Financial Service Providers shall ensure adequate mechanisms are in place to detect and correct corruption as well as aggressive or abusive treatment by their staff and agents, particularly during the loan sales and debt collection processes.
4. Internal policies and procedures.
  - a. Each Financial Service Provider must have internal policies and procedures in place that educate employees, agents and third party service providers of the Financial Service Provider on how to behave toward Clients and ensure that employees and agents are treating Clients with high ethical standards. Such internal policies and procedures must also set forth penalties (which may include, but not be limited to, employment-related sanctions such as suspension or termination of employment) against any employees or agents for failure to comply with these requirements.
  - b. Any handbooks, policies, or similar guidelines established by the Financial Service Provider related to fair and respectful treatment of Clients must be written in a clear, understandable manner so that the employees, agents and third-party service providers of the Financial Service Provider can acknowledge understanding of the same.
  - c. Financial Service Providers shall not provide incentives to staff, management, agents or third-party service providers that encourage unethical Client treatment or over-indebtedness.
  - d. At least every three years, Financial Service Providers shall audit, review and, as necessary based on the findings of such audit and review, revise in consultation with industry associations and Clients:



- i. Its handbooks, policies or similar guidelines related to fair and respectful treatment of Clients to ensure that they are reflective of industry standards and in compliance with Consumer Financial Protection Laws; and
- ii. Its employee training and supervision programs, human resource and employee evaluation systems, internal Complaint Handling Unit, internal compliance systems, employee incentives and other internal policies and procedures to ensure that employees, agents and third-party service providers are adhering to Client treatment policies on a continuing basis.

**Commentary:**

- a) Client Treatment. Clients are entitled to being treated with dignity. A respectful attitude from the Financial Service Provider encourages Client trust and confidence, thereby promoting the responsible use of financial services and furthering financial inclusion.
- b) Targeting Clients to Correct for Discrimination. Prohibited discrimination must be distinguished from the practice of targeting members of a particular group to correct for societal discrimination. For example, the practice in the developing world of targeting women or persons with disabilities, who traditionally lack access to Consumer Financial Products and Services, as Clients, would not be prohibited under this section.
- c) Debt Collection. Clients are particularly vulnerable to inappropriate treatment during the debt collection process. Under this Model Law, Financial Service Providers are responsible for the actions of those who collect debt on their behalf, whether they are employees, agents or third-party service providers.

## **9. Privacy of Client Data**

### **9.1 Privacy and Protection of Non-Public Client Data**

**Purpose:**

To require that Non-Public Client Data be collected, stored, viewed and used by Financial Service Providers in a manner that effectively protects the Client's privacy.

**Content:**

1. General.
  - a. Each Financial Service Provider must respect the privacy of Clients and protect their Non-Public Client Data. Such data must only be used for the purposes specified and agreed to by the Client or as permitted by law.
2. Establishment of a Privacy Policy.

- a. Each Financial Service Provider that collects, receives, possesses, stores, deals with or handles Non-Public Client Data must have adequate policies and procedures that:
  - i. Enshrine the principle that Non-Public Client Data is owned by the Client;
  - ii. Clearly set out the Financial Service Provider's practices and policies with respect to Non-Public Client Data;
  - iii. Identify any sensitive data collected and processed;
  - iv. Explain the purposes for which the Non-Public Client Data is collected and used;
  - v. Provide for reasonable security practices and procedures to safeguard Non-Public Data; and
  - vi. Include clear procedures for when a Client may voluntarily allow for disclosure of their Non-Public Client Data.
- b. Any Privacy Policy established by the Financial Service Provider must be written in simple language Clients can understand. Financial Service Providers must highlight the most important privacy information in any Product Disclosure Form provided to Clients in conformity with [*Section 6.1 Disclosure Principles and Section 6.2 Product Disclosure Form*].

**Commentary:**

- a) Non-Public Client Data. At the core of the privacy principles is the acknowledgment that Non-Public Client Data belongs to the Client, and that misuse of such data has the potential to harm the Client. Other aspects of safeguarding Non-Public Client Data apply to IT security, as well as to maintaining paper data securely. Each Financial Service Provider should recognize that sharing Non-Public Client Data should be done with Client acknowledgement and be based on clear disclosure. Clients should not be asked to share Non-Public Client Data unless genuinely necessary. However, such data may be anonymized, that is scrubbed of any personal identifying information, and shared or published by Financial Service Providers or the Supervisory Authority. For more information on protecting the privacy of Client data see the OECD Privacy Framework (2013).
- b) Privacy Officer. It is recommended that each Financial Service Provider have a designated privacy officer who understands Privacy Laws, and is able to develop appropriate policies for the Financial Service Provider. Such responsibilities can be shared by multiple persons depending on the size and scope of the organization. The privacy officer should also train relevant staff and assist Clients, upon request, in understanding their rights to privacy.

- c) Challenges in Privacy. Two particular challenges in the area of privacy must be noted. First is the challenge of achieving the informed consent of Clients while ensuring they understand their rights in regards to Non-Public Client Data, when in actual practice few, if any, Clients consider or weigh privacy considerations before contracting for a Consumer Financial Product or Service. Second, even where privacy and data protection rules are in place, many regulators lack the capacity or expertise to effectively enforce them.

## 9.2 Collection of Non-Public Client Data

### **Purpose:**

To require that the manner in which Non-Public Client Data is processed and stored by Financial Service Providers be set forth and disclosed to the Client in advance.

### **Content:**

1. Clients must be made aware of the fact that their Non-Public Client Data is being collected, the purpose for which the data is collected, the intended recipients of the data and the contact details of the Financial Service Provider collecting the data.
2. Clients have the right to review their Non-Public Client Data to ensure that inaccurate or deficient data is corrected or amended, as feasible.
3. Non-Public Client Data shall be:
  - a. Collected only for specified and legitimate purposes;
  - b. Processed lawfully; and
  - c. Accurate, relevant, and, where appropriate, kept up to date.
4. Inaccurate or incomplete Non-Public Client Data must be corrected, supplemented, destroyed or restricted, as appropriate.

### **Commentary:**

- a) Confidentiality. Clients' rights to the confidentiality of their Non-Public Client Data protect their privacy and individual liberties. The privacy of Non-Public Client Data is particularly important to Clients because it assists in the prevention of losses due to theft and fraud. In addition, by protecting Non-Public Client Data, Clients are better safeguarded against appropriation or pressure from friends and family (which otherwise may not be the case if Non-Public Client Data were publicly available).

### 9.3 Storage of Non-Public Client Data

**Purpose:**

To require each Financial Service Provider to implement various security measures to protect Non-Public Client Data.

**Content:**

1. Financial Service Providers must:
  - a. Implement reasonable and appropriate organizational, physical and technical measures for the protection of Non-Public Client Data against unlawful access or destruction, misuse or accidental loss or destruction;
  - b. Determine the appropriate level of security that must be maintained in order to preserve the confidential nature of the Non-Public Client Data, taking into account the risks of processing, size of the organization, current privacy best practices and cost of implementation;
  - c. Require that all of their Non-Public Client Data controllers and third parties processing personal information abide by a confidentiality clause similar in nature to these privacy provisions; and
  - d. Report to the Supervisory Authority and to affected Clients security breaches resulting in the unauthorized disclosure of Non-Public Client Data.
2. Financial Service Providers must have clear procedures for ensuring the security of written and electronic Non-Public Client Data. Procedures regarding written data must address: access, copying, storage, internal and external transmission by the Financial Service Provider, archiving, disposal and overall security. Electronic data policies must address: data entry, data alteration, access to data, the Financial Service Provider's secure internal and external transfer of data (including internationally), archiving, disposal, security of back-up systems and overall data security. Staff should be informed and trained regarding these policies.

**Commentary:**

- a) Time Limits. Non-Public Client Data must be stored and used only for as long as it is necessary to achieve the purpose for which it was processed and all related purposes, or, if longer, as long as Applicable Laws require.

### 9.4 Disclosure of Non-Public Client Data

**Purpose:**

To outline the permissible disclosures of Non-Public Client Data.

**Content:**

1. Financial Service Providers may disclose Non-Public Client Data to a third party in any of the following instances:
  - a. When the Client has been informed about such disclosure and permission has been obtained in writing;
  - b. When the third party in question has been authorized by the Client to obtain the Non-Public Client Data from the Financial Service Provider;
  - c. When required or permitted under [*Section 5.2 Mandated Credit Reporting*]; and
  - d. When the Financial Service Provider is legally required to disclose the Non-Public Client Data pursuant to Applicable Law.

**Commentary:**

- a) Exception for Credit Reporting. The existing legal structures in many countries would require Clients to authorize the sharing of data for credit reporting purposes. However, given the importance of credit reporting information for safe lending and prevention of over-indebtedness, the Model Law does not require this, but instead requires that Clients be duly informed of this exception as part of the Financial Service Provider's disclosures.

## **10. Complaint Resolution**

### **10.1 Internal Complaint Handling Unit**

**Purpose:**

To require Financial Service Providers to have internal complaint handling mechanisms.

**Content:**

1. Complaint Handling Unit.
  - a. Each Financial Service Provider must establish a single Complaint Handling Unit to receive Client complaints, either in person or in writing, via telephone, e-mail, webpage or other similar method.
  - b. The staff of the Complaint Handling Unit must be equipped and empowered to act decisively to resolve complaints.
2. Accessibility and Disclosures.
  - a. The Complaint Handling Unit and all complaint procedures must be designed and operated to be easily accessible to all Clients.

- b. Financial Service Providers must actively inform Clients about how to make a complaint. This information must, at minimum, be displayed prominently by the Financial Service Provider and by its agents or third party service providers, if any, at their physical locations and on their electronic sites.
  - c. All contracts and disclosures given to Clients by Financial Service Providers regarding Consumer Financial Products and Services must include contact information for the Complaint Handling Unit and the Supervisory Authority.
3. Responsiveness.
- a. Financial Service Providers must establish a reasonable timeline for resolving each complaint and ensure all complaints are addressed in an equitable, objective and timely manner.
  - b. Upon completion of any investigation into a complaint, the Financial Service Provider must immediately communicate its resolution to the Client and should clearly explain the basis of the decision.
  - c. The Financial Service Provider must inform the Client of the procedure to appeal or to further pursue the complaint in the event of an adverse decision, including referrals to conciliation or mediation and to any complaint process established by the Supervisory Authority or an industry association.
4. Records and Reporting.
- a. The Financial Service Provider must retain the records pertaining to each Client complaint, including records of how the complaint was resolved, for the period established by the Supervisory Authority. The Supervisory Authority may require periodic data reporting and may engage in monitoring the complaint handling process.

**Commentary:**

- a) Flexibility. A Financial Service Provider should tailor its complaint handling mechanism to the specific Clients it serves and the specific Consumer Financial Products and Services it offers, commensurate with the Financial Service Provider's own size and complexity. Larger Financial Service Providers should be expected to have a robust process with dedicated employees. Smaller Financial Service Providers, however, should be given more discretion to develop efficient and cost-effective complaint handling mechanisms.
- b) Minimum Standards. The internal complaint handling process may differ depending on each Financial Service Provider's circumstances. However, the process must, at minimum, be (1) overseen and actively monitored by senior management, (2) focused on resolving Client concerns and correcting problems, (3) fair and proportionate, (4) sensitive to Client's needs, (5) affordable, (6) clear and straightforward, (7) easily understood and (8) readily accessible.

- c) Single Point of Contact and Dedicated Staff. There should be a single point of contact to receive Client complaints, which can be made either in person or in writing, and the Complaint Handling Unit should be staffed by individuals specifically equipped and empowered to act decisively to resolve complaints. The staff must have decision-making authority and be flexible enough to handle complaints effectively and decisively.
- d) Timeliness and Responsiveness. A response to each complaint should be made in an equitable, objective and timely manner, in compliance with established timelines for handling complaints. Clients should promptly receive acknowledgments of any complaints they may have filed, the contact information of the officer or staff member handling the complaint and the timeline for the complaint's resolution. The Financial Service Provider's senior officers should conduct regular audits of the effectiveness of the Complaint Handling Unit and its timeliness in resolving complaints. The Supervisory Authority may provide further guidance on the appropriate response time through rulemaking.
- e) Process of Appeal. Clients should have access to a process of appeal if a complaint is not resolved in their favor. Such appeal process may be a further review within the Financial Service Provider, or an external process that could involve third-party arbitration or appeal to a resolution mechanism established by the Supervisory Authority under [*Section 10.2 Supervisory Authority Response to Client Complaints and Inquiries*]. Reasonable time limits on when an appeal can be filed should be permitted.
- f) Data Reporting. Each Financial Service Provider must report to the Supervisory Authority, at the end of each regular reporting period (e.g., monthly, quarterly, or annually), the number of complaints it has received, those pending resolution and those that have been resolved, with a short description of the nature of the complaints received during the reporting period, the average time period for resolving the complaints and how these complaints were or are planned to be resolved. To facilitate supervision and market monitoring the Supervisory Authority should establish a standardized format for such reports.
- g) Data Monitoring. The Supervisory Authority should investigate Financial Service Providers whose periodic reports reveal (1) an unusual number of, or a significant increase in, Client complaints, (2) a significant backlog in the resolution of complaints or (3) a material change in the severity or the nature of the complaints. An effective complaint handling mechanism by Financial Service Providers combined with effective data monitoring by the Supervisory Authority provides an early warning signal to regulators and supervisors on market deficiencies, conduct doing harm to Clients and emerging risks.

## 10.2 Supervisory Authority Response to Client Complaints and Inquiries

### **Purpose:**

To authorize the Supervisory Authority to establish or facilitate a Client complaint mechanism or ombudsman.

### **Content:**

1. Regulator Response to Clients.
  - a. The Supervisory Authority may establish procedures to receive complaints against, or inquiries concerning, a Financial Service Provider.
2. Timely Response to Supervisory Authority by Financial Service Provider.
  - a. When the Supervisory Authority gives notice of a Client complaint or inquiry to a Financial Service Provider, the Financial Service Provider shall provide a timely response to the Supervisory Authority, including:
    - i. Steps that have been taken by the Financial Service Provider to respond to the complaint or inquiry;
    - ii. Responses received by the Financial Service Provider from the Client; and
    - iii. Follow-up actions or planned follow-up actions by the Financial Service Provider to respond to the complaint or inquiry.

### **Commentary:**

- a) Supplementary Role. Financial Service Providers are in the best position to respond to Client complaints. As such, primary responsibility for handling complaints should fall on the Financial Service Providers and Clients should be instructed to first work with their Financial Service Provider. The Supervisory Authority's complaint resolution program should supplement the internal complaint handling mechanism required of each Financial Service Provider.
- b) Possible Structures. Possible external complaint resolution programs may take a variety of forms, each with their own costs and benefits. Courts and formal judicial hearings may provide fair administration, but are generally costly and time-consuming. Less formal alternative dispute resolutions may be cheaper and quicker. Non-binding mediation may perhaps be faster still, assuming both parties can find a mutually agreeable solution. These alternative dispute resolution mechanisms could be housed in an independent statutory body, located within the Supervisory Authority or within an ombudsman's office.



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Client Protection Principles: Model Law

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## **Annex 2 Mapping of Client Protection Principles to the Model Law**

To aid policymakers and others seeking to introduce or reform various aspects of their Client protection framework, this Annex provides a clear mapping between key Client Protection Principles and this Model Law.

### **Appropriate Product Design and Delivery Channels**

<u>Element</u>	<u>Model Law Provision</u>	<u>Notes</u>
1. <b>Suitable Product Design:</b> Relates to providers gathering sufficient information from Clients to ensure the product is likely to meet the customer's needs and capacity.	4.1 Product Risk Management; 4.2 Affordability and Suitability Assessments; 5.1 Creditworthiness Assessments	
2. <b>Suitable Product Delivery:</b> Relates to product design taking into account the processes by which products will be sold.	4.1(c) Product Risk Management; 4.4 Rescission Period	
3. <b>Simplicity:</b> Relates to making products and pricing easier for Clients to understand and compare.	6.1 Disclosure Principles; 6.2 Product Disclosure Form; 6.3 Publication of Fees, Rates, Terms and Conditions; 6.5 Standardized Calculation Methods	
4. <b>No Waiver of Client Rights:</b> Relates to ensuring that Clients are not asked to waive rights, such as the right to sue the provider, receive information, cancel use of the product, maintain privacy, etc.	4.3 No Waiver of Rights	
5. <b>Minimum Changes:</b> Relates to minimizing the possibility that product changes, such as unexpected changes in pricing, terms or fees, will become necessary during the course of the product's life.	4.1 Product Risk Management; 6.2(2) Product Disclosure Form; 6.4 Fees; 7.1 Pricing Procedures	Fees may not be charged to a Client unless previously disclosed.
6. <b>Affordability:</b> Relates to ensuring the costs of a financial	4.2 Affordability and Suitability Assessments; 5.1	



product fit reasonably within a Client's paying capacity.	Creditworthiness Assessments	
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**Preventing Over-indebtedness**

<u>Element</u>	<u>Model Law Provision</u>	<u>Notes</u>
1. Client Underwriting Process: Relates to analysis of a Client's repayment capacity and methodologies for assessing creditworthiness.	4.2 Affordability and Suitability Assessments; 5.1 Creditworthiness Assessments	
2. Loan Terms and Conditions: Relates to the appropriate use of collateral, ensuring loan repayment schedules correspond with the Client's cash flow, or procedures for evaluating a guarantor's creditworthiness and relationship to the Client.	4.2 Affordability and Suitability Assessments; 5.1 Creditworthiness Assessments	
3. Sales Techniques: Relates to discouraging aggressive sales tactics.	3.1(1)(c) Prohibited Acts; 8.1 Client Treatment	Prohibits unfair, deceptive or abusive acts and practices.
4. Staff Incentives: Relates to ensuring staff incentives, such as compensation, do not encourage over-indebtedness.	8.1(4)(c) Client Treatment Policies and Procedures	Financial Service Providers may not have incentives that encourage over-indebtedness.
5. Monitoring Systems: Relates to mechanisms for on-going monitoring of the repayment capacity of Clients, individually and in the market as a whole.	5.2 Mandated Credit Reporting	
6. Market Initiatives: Relates to market-level initiatives to prevent over-indebtedness, such as the development of credit reference systems, credit bureaus, or financial education programs.	2.3(4) Coordination; 5.2(3) Mandated Credit Reporting	Authorizes the Supervisory Authority to facilitate the creation of a Credit Reporting System, if no adequate credit reference system exists.

**Transparency**

<u>Element</u>	<u>Model Law Provision</u>	<u>Notes</u>
1. Cost Information about Products: Relates to the explanation of interest rates, exchange rates, penalties, premiums and fees in a way that is accurate and understandable.	6.2 Product Disclosure Form; 6.3 Publication of Fees, Rates, Terms and Conditions; 6.4 Fees; 6.5 Standardized Calculation Methods	
2. Non-cost Information about Products: Relates to disclosing attributes of products such as switching barriers, effects of delinquency or default, etc. Also relates to information about Client rights, process for making complaints, and privacy of information.	6.2 Product Disclosure Form; 9.1(2)(b) Protection of Non-Public Client Data; 10.1(2) Internal Complaint Handling Unit	
3. Clear Use of Language: Relates to effectiveness of communication between the FSP and a Client; e.g. the use of simple language, absence of fine print, and use of multiple ways of delivering information.	6.1(1)(a) Disclosure Principles; 6.1(1)(d) Key Facts Statement; 6.2 Product Disclosure Form; 9.1(2)(b) Protection of Non-Public Client Data	Mandates clear and concise disclosures in simple language.
4. Appropriate Timing of Disclosures: Relates to the provision of timely account information before, after, and at the time of establishing a relationship with a Client.	6.1(1)(b) Disclosure Principles	Requires Clients to be provided with the most up-do-date information at the time it is most needed.
5. Mechanisms for Confirming Client Understanding: Relates to double-checking that Clients understand the products offered and disclosures made by FSPs.	4.1 Product Risk Management	Requires internal procedures for confirming that Clients understand the terms and conditions of products and services.

**Responsible Pricing**

<u>Element</u>	<u>Model Law Provision</u>	<u>Notes</u>
1. Pricing Procedures: Relates to providers having a formal (internal) pricing procedure for each product to ensure competitive and efficient prices.	7.1 Pricing Procedures	
2. Fees: Relates to restricting fees or ensuring that fees are to provide a reasonable coverage of the provider’s costs and to encourage responsible repayment by the Client (e.g., late payment fees that encourage on-time principal and premium payments).	7.1 Pricing Procedures; 6.4 Fees	

**Fair and Respectful Treatment of Clients**

<u>Element</u>	<u>Model Law Provision</u>	<u>Notes</u>
1. Commitment to Code of Ethics: Relates to committing providers to a code of ethics, stating the institution’s mission and articulating its organizational values, such as fair treatment of Clients.	3.2 Board and Senior Management Oversight; 8.1(4) Client Treatment Policies and Procedures	
2. Non-Discrimination: Relates to ensuring all Clients are treated equally, regardless of their race, gender, religion, ethnicity, political affiliation, disability or gender.	3.1(c) Prohibited Acts; 8.1(2) Client Treatment Policies and Procedures	The prohibition on unfair, deceptive or abusive acts or practices includes discrimination; 8.1(2) contains an explicit prohibition on discrimination.
3. Appropriate Incentive Structure and Sales Practices: Relates to ensuring that staff compensation is aligned with responsible behavior.	8.1(4)(c) Client Treatment Policies and Procedures	Financial Service Providers may not have incentives that encourage unethical behavior.

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<p>4. Responsible Use of Agents: Relates to provider relationships with agents and making providers responsible for the behavior of agents.</p>	<p>1.2(1) Scope of Application; 3.2 Board and Senior Management Oversight; 8.1(4) Client Treatment Policies and Procedures</p>	<p>Financial Service Providers are responsible for the behavior of agents.</p>
<p>5. Preventing Staff Corruption: Relates to preventing staff from obtaining money or other favors from Clients in return for providing products, creating a corporate culture where employees feel safe to be whistle blowers, and systems for detecting and correcting corruption.</p>	<p>3.1(1)(c) Prohibited Acts</p>	<p>The prohibition on unfair, deceptive or abusive acts or practices includes staff corruption.</p>
<p>6. Informing Clients of Their Rights: Relates to the provision of information to Clients about their rights, including what is and is not acceptable behavior by the provider's staff, and how to make complaints.</p>	<p>6.1 Product Disclosure Principles; 6.2 Product Disclosure Form; 10.1 Internal Complaint Handling Unit</p>	
<p>7. Client Feedback: Relates to tools for assessing a provider's success in fostering responsible treatment, including Client surveys, third party interviews, mystery shopping, and effective systems for addressing Client complaints.</p>	<p>8.1(4)(d)(ii) Client Treatment Policies and Procedures; 10.1 Internal Complaint Handling Unit; 10.2 Supervisory Authority Response to Client Complaints and Inquiries</p>	

**Privacy of Client Data**

<u>Element</u>	<u>Model Law Provision</u>	<u>Notes</u>
1. Complete Policy and Procedures: Relates to requiring providers to have internal policies and procedures to keep Client data private unless otherwise mandated by law.	9.1 Privacy and Protection of Non-Public Client Data; 9.3 Storage of Non-Public Client Data	
2. Information Security: Relates to ensuring the security of written and electronic information.	9.3 Storage of Non-Public Client Data	
3. Information Provided to Clients About Their Rights and Responsibilities: Relates to furnishing Clients with information about the provider's privacy policy and procedures, as well as each Client's rights and responsibilities.	6.1 Product Disclosure Principles; 6.2 Product Disclosure Form; 9.1 Privacy and Protection of Non-Public Client Data; 9.2 Collection of Non-Public Data	
4. Waivers of Privacy Rights: Relates to restrictions on waivers of privacy rights or procedures for instances when a Client chooses to waive his or her privacy rights.	4.3 No Waiver of Rights	
5. Data That Could be Used for Discriminatory Purposes: Relates to restrictions on collecting data that could be used for discriminatory purposes, such as information about ethnicity, religion, or political affiliations.	9.2(3) Collection of Non-Public Data	Data can only be collected for lawful purposes.

**Effective Complaint Resolution**

<u>Element</u>	<u>Model Law Provision</u>	<u>Notes</u>
1. Policy and Procedures: Relates to requirements for providers to have internal policy and procedures for complaint resolution.	10.1 Internal Complaint Handling Unit	
2. Ensuring Effectiveness: Relates to ensuring that complaint resolution systems are effective, including escalating serious complaints to senior management for attention and resolution, staff training, providing Clients easily accessible and safe ways to make complaints, resolving complaints in a timely manner and learning from complaints.	10.2 Supervisory Authority Response to Client Complaints and Inquiries	
3. Advising Clients of Their Rights: Relates to providing Clients with clear and simple information about their right to complain, how to register a complaints, the steps that take place after a complaint is filed, the time frame within which Clients should expect their complaint to be addressed, and the steps to follow if they are dissatisfied with how their complaint is handled.	6.1 Product Disclosure Principles; 6.2 Product Disclosure Form	

**Annex 3 Key Facts Statement**

For illustrative purposes, a sample Key Facts Statement (for a loan) is reproduced below.

• Total amount borrowed (Loan size and currency)		• Your monthly installment	
• Effective Interest Rate (EIR) or Annual Percentage Rate (APR)		• Total number of installments	
• Disbursement date		• Installment frequency	
• Maturity date		• Grace period (if applies)	
• Purpose of loan		• Type of guarantee or collateral	
• Penalty for late payment		• Total cost of loan (interest + fees)	
• Penalty for pre-payment		• Total amount repaid at the end of the loan (principal + interest + fees)	

Client signature \_\_\_\_\_ Date \_\_\_\_\_

Loan Officer signature \_\_\_\_\_ Date \_\_\_\_\_

Branch Director signature \_\_\_\_\_ Date \_\_\_\_\_

**Please contact our Customer service Line if you have any questions or complaints about our products, services or staff: 555-555-5555. Open Monday to Saturday 7:00-20.00. All calls are free.**

Source: Smart Campaign:

<http://www.smartcampaign.org/tools-a-resources/1047sample-key-facts-statement>

[https://centerforfinancialinclusionblog.files.wordpress.com/2013/08/essential-docs-for-new-clients\\_version-2-01.pdf](https://centerforfinancialinclusionblog.files.wordpress.com/2013/08/essential-docs-for-new-clients_version-2-01.pdf)

**Annex 4 Product Disclosure Form**

For illustrative purposes, a sample Product Disclosure Form is reproduced below (for a loan).

<p><b>PRODUCT DISCLOSURE FORM</b></p> <p><b>(Read this Product Disclosure Form before you decide to take out the &lt;Name of Product&gt;. Be sure to also read the terms in the Contract. Seek clarification from your institution if you do not understand any part of this document or the general terms)</b></p>	<p>&lt;Name Financial Service Provider&gt;</p> <p>&lt;Name Product&gt;</p> <p>&lt;Date&gt;</p>
<p><b>1. What is the product about?</b></p> <ul style="list-style-type: none"> <li>• Purpose of loan</li> </ul>	
<p><b>2. What do I get from this product?</b></p> <ul style="list-style-type: none"> <li>• Total amount borrowed (Loan size and currency)</li> <li>• Disbursement date</li> </ul>	
<p><b>3. What are my obligations?</b></p> <ul style="list-style-type: none"> <li>• Your monthly installment</li> <li>• Total number of installments</li> <li>• Installment frequency</li> <li>• Tenure (Maturity date and Maturity in months)</li> <li>• Grace period (if applies)</li> </ul>	
<p><b>4. What charges to I have to pay?</b></p> <ul style="list-style-type: none"> <li>• Interest rate (% - declining)</li> <li>• Commission fee</li> <li>• Other fees</li> <li>• Mandatory savings</li> <li>• Effective Interest Rate (EIR) or Annual Percentage Rate (APR)</li> </ul>	
<p><b>5. What is the total cost for this product?</b></p> <ul style="list-style-type: none"> <li>• Total cost of loan (interest + fees)</li> <li>• Total amount repaid at the end of the loan (principal + interest + fees)</li> </ul>	
<p><b>6. What if I fail to fulfill my obligations?</b></p> <ul style="list-style-type: none"> <li>• Penalty for late payment</li> <li>• Other consequences</li> </ul>	
<p><b>7. What if I fulfill my obligations ahead of time?</b></p> <ul style="list-style-type: none"> <li>• Penalty for pre-payment</li> <li>• Other consequences</li> </ul>	
<p><b>8. Do I need a guarantor or collateral?</b></p> <ul style="list-style-type: none"> <li>• Type of guarantee or collateral</li> </ul>	
<p><b>9. What do I need to do if there are changes to my contact details?</b></p> <p>It is important that you inform us of any changes in your contact details to ensure that all correspondences reach you in a timely manner.</p>	



**10. Where can I get assistance and redress?**

***If you have difficulties in making repayments, you should contact us earliest possible to discuss repayment alternatives.***

We are here to serve you. Please contact us with any questions or complaints you may have. Your contact with us is confidential.

Please contact us using any of the following options:

- Email the MacroDreams Customer Service Department: customers@md.info.
- Leave a comment card in the “Suggestion Box” at your local branch.
- Call the MacroDreams Customer Service Line: 555-555-5555.
- Send a text to the MacroDreams Customer Service Line: 555-555-5555.

We strive to respond to your email, phone or text messages within 48-hours, and your comment cards within 7 business days.

Our Customer Service Line is open Monday to Saturday from 7:00 to 20:00. All calls and text messages are free.

Clients may also make complaints to the National Bureau of Consumer Protection: 555 Fifth St., Fivetown.

Source: Smart Campaign:

<http://www.smartcampaign.org/tools-a-resources/1048sample-product-disclosure-form>

[https://centerforfinancialinclusionblog.files.wordpress.com/2013/08/essential-docs-for-new-clients\\_version-2-01.pdf](https://centerforfinancialinclusionblog.files.wordpress.com/2013/08/essential-docs-for-new-clients_version-2-01.pdf)



# Microfinance CEO Working Group

The Microfinance CEO Working Group is a collaborative effort of the leaders of ten leading international organizations that promote microfinance around the world.



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