

REGULATORY FRAMEWORK FOR MICROFINANCE OPERATIONS IN BOLIVIA

These last few years, the Bolivian State has been working to consolidate an appropriate juridical and regulatory framework for the needs of institutions specialized in offering microfinance services.

In Bolivia, Private Financial Funds (FFPs) and BANCOSOL are the organizations that offer regulated microfinance services. There are also Non Governmental Organizations (NGOs) in the country that provide these services, but their activities are not regulated by the Law on Banking and Financial Institutions nor by the Superintendence of Banks and Financial Institutions (SBEF).

The most important regulations that rule micro financing operations in Bolivia are:

- **Supreme Decree 24000**, of May 1995, that authorizes the creation of FFPs, as corporations specialized in resource intermediation for micro managers of the productive, commercial and service sectors, allowing NGOs specialized in this type of operations to achieve their objectives through the organization of risk capital corporations, authorized to capture deposits subject to the control of the SBEF.

The creation of FFPs facilitated the formalization of NGOs technologies and operations in Bolivia, demanding from them a minimum capital (of 630 thousand Special Drawing Rights), which is lower than that requested from banks, this comes together with a strict prudential framework that establishes limits for supplying credit and concentration smaller than those established for banks.

The Supreme Decree establishes that the FFPs should be organized as corporations, since this is a suitable form for financial intermediation, both for artificial stability that represents mercantile institutions to civil society, and for allowing timely increases or equity replenishment, whenever required to do so by SBEF in accordance with the regulatory framework included in the Law on Banking and Financial Institutions.

Since the Decree was approved, the concept of FFP has been the legal form which became the starting point from which private initiative has been able to guide its efforts toward filling an unsatisfied credit demand from traditionally excluded sectors of the financial services.

- **Law on Banking and Financial Institutions** that, in its last amendment of December 20, 2001, incorporates FFPs in chapter III of Title IV on non banking financial intermediation institutions.

In that chapter, the Law points out that: "Private Financial Funds are corporations whose main purpose is to channel resources to small and micro borrowers whose activities are located in urban and rural areas."

It also indicates assets and liabilities operations that those institutions can develop and the services they can provide, and it reiterates that the minimum capital to operate as an FFP is of 630.000 Special Drawing Rights.

With this modification, operations the Private Financial Funds can perform are those that the banks provide, except for:

- Providing deposit services in general deposit warehouses.
- Carrying out factoring operations.
- Receiving bills of exchange or other collection items, as well as make collections, payments, and transfers.*
- Performing wire transfers and issue payment orders payable within the country or abroad.*
- Investing in the capital of securitization companies.
- Investing in the capital of Insurance Companies.
- Administering investment funds to invest for third party accounts.

** Only regarding operations of foreign trade, they are allowed to send and receive money remittances by legal and natural persons, within the country and abroad.*

The Law on Banking also points out that the Superintendence of Banks and Financial Institutions should authorize each of the following operations:

- Reception of funds for checking accounts.
- Issue of credit cards.
- Investment of capital belonging to financial services institutions.

The aforementioned standard in turn points out that non banking financial intermediation institutions (among them FFP's) will not be authorized to carry out the following operations:

- Receive, partially or completely, shares of the institution itself as collateral for credit.
- Grant credit to directors and members of the credit committees during the period of their mandate. Credit that is outstanding at the time of their election shall remain binding to the originally agreed conditions and cannot be subject to rescheduling.
- Grant or maintain credit with executive staff, employees or borrowing groups related to them, within the scope of Article 50° of this law. For purposes of the present law, executive staff and employees shall be those persons who exercise

decision-making or operational functions, whether they are legal representatives or otherwise, or who render services to the organization under any name, that can compromise the organization, without limitation or subject to specific limitations. Credit granted to such persons shall be paid entirely before they assume their functions.

- Grant credit to a borrower or borrowing group for an amount that exceeds one percent (1%) of its net worth should they offer personal guarantees.
- Grant or maintain credit with a borrower or borrowing group that amount to over three percent (3%) of their net worth. An exception is awarded for housing credits intended for a borrower or borrowing group, which shall however not exceed five percent (5%) of the net worth of the financial intermediary. This last limit shall reach ten percent (10%), subject to express prior authorization of the Superintendence of Banks and Financial Institutions.
- Grant credit to an institution of the financial system that exceeds twenty percent (20%) of its net worth, except for cases that are expressly authorized by the Superintendence in places that lack sufficient financial institutions.
- Transfer consumption real estate and credit portfolios, subject to regulations of the Superintendence, approved by the Prudential Financial Standards Committee (CONFIP).

Another specific standard issued by the SBEF for the microfinance sector

In the last few years, the SBEF has issued and adapted to the new market conditions and the characteristics of the microfinance sector, some standards that we mention next:

Standards for loan portfolio

The SBEF has considered the special characteristics of lending to micro enterprise, and in terms of that it has developed specific standards for credit risk in this sector, with the demand to constitute provisions for uncollectible loans for:

- i) **How long overdue and times it was rescheduled** in reference to micro credit, according to the following scale:

DAYS DELAYED - NUMBER OF RESCHEDULINGS	QUALIFICATION	% OF PROVISIONS
1 to 5 days delayed	1 Normal	1
6 to 30 days delayed	2 potential problems	5
31 to 60 days delayed or 2 reschedulings	3 doubtful	20

61 to 90 days delayed	4 Doubtful	50
More than 90 days delayed	5 Lost	100

The system for qualification and provisions described in the previous graph have a close relationship with the type of activities that Microfinance institutions finance, this is to say that economic cycles of micro managers are very short, and their earnings are obtained in the short term and almost immediately generate profit reinvestment in the following cycle. This, together with the great volume of operations, makes days on delay a valid measure to evaluate implicit credit risks.

ii) Additional Risk of Delays in Payment

Aside from the régime on specific provisions, standards establish generic provisions in terms of policy evaluations, concessionary practices and procedures and credit management and of control of credit risks that must consider the existence of an adequate credit technology, policies for dealing with rescheduling, and the existence of computer systems and procedures to follow up the reprogrammed loan portfolio.

If it is decided that policies and practices described do not adjust to the minimum guidelines established in the standards, the institution involved must constitute a generic forecast of 3% of the total of its micro credit loan portfolio.

In addition, an outline of constitution of generic provision has been provided in terms of the institution's clients who may have overdue accounts or other problems with other institutions. That situation represents a potential credit risk for the institution under consideration, and it is a third plan in addition to the previously estimated amount.

Opening agencies, branches, and mobile services

Given the geographical extension of the country and for the purpose of extending geographical coverage with financial services, standards for opening agencies and branches for micro finance services have been simplified. Specific standards for providing mobiles services are included, which become a tool that allows micro finance institutions to expand their services.

Correspondent contracts

This standard allows regulated financial intermediation institutions to sign correspondent contracts among themselves and with non regulated institutions to provide financial services of payments and transfers, except reception of deposits or placement of credit.

Credit information bureaus

The SBEF has issued specific regulations for opening Credit Information Bureaus (BICs), that will allow regulated micro finance entities under SBEF supervision to access credit information provided by non regulated microfinance institutions, who in turn will be able to obtain information on credit in the regulated financial system. That would allow microfinance institutions to have more accurate information about over indebtedness that affected this industry in recent years and that has been one of the main lessons of the Bolivian experience.

At present, there already is an information bureau that will render its services in these months.

Transparency

In this topic, it is important to mention the Rules and regulations on interest rates that specify characteristics and minimum content that credit contracts should have, regardless of the type of institution or of credit.

With this standard, the attempt has been made to reduce asymmetry of existent information between financial institutions and small clients, thus generating more transparency in credit activities.

Claims and Consultation Service (SARC)

This rule offers the clients of financial services the possibility to make any claim or consultation directly to financial institutions responsible for answering their clients within established terms, after which those claims or consultations are turned over to SBEF to be adequately processed. This mechanism for the defense of consumers of financial services seeks to eliminate the existent distortions in the relationship of financial institutions and clients and it looks to avoid abuses in bad practices matters.

Governance

This aspect that has lately become increasingly relevant, mainly in the environment of micro finance institutions, is also reflected in the standards of the SBEF, its purpose being to cooperate with good corporate management, understanding as such the group of rules that sets order in relationships and behavior among Management, the Board of Directors, shareholders and third parties, producing the strategic objectives of the company, the means, resources and processes to reach those objectives, as well as systems for follow up verification of responsibilities and controls in each level of the structure of financial institutions.

Internal control

With reference to this topic, the rule points out that systems of internal control should be implemented inside each financial institution that includes the components of control environment, risk evaluation, control activities and segregation of functions, information and communication and monitoring and

correction of deficiencies activities. A central point of the aforementioned system is that it implies the participation of all directors, managers and personnel of financial intermediation institutions, with functions to be determined for each one of them and according to its responsibilities.

Rules on the duties and responsibilities of the Trustee have also been issued, as well as on control and internal auditing.