



PROPOSALS FOR REGULATIONS

Tier 4 Microfinance
Institutions and Money
Lenders Act (2016)

Shared with
Department of Microfinance
MoFPED

March 2017



UDN congratulates the Ministry of Finance Planning and Economic Development upon achieving the passing of the Act and wishes to share proposals for incorporation in the guidelines that will regulate the operations of Microfinance and Money lending institutions.

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INTRODUCTION

Cooperatives were established in Uganda in the 1900s but formalized by the Cooperative Ordinance of 1946 and the Cooperatives Societies Act of 1962. Their performance was short-lived with the political interference and insecurity in the 1970s but the introduction of Savings and Credit Cooperatives (SACCOs) revived Cooperatives in Uganda. The Government then adopted a component on the Rural Financial Services Programme (RFSP) to develop a sustainable financial infrastructure for delivering services at the rural community level.

In 2007, RFSP was re-oriented towards the new Rural Financial Strategy to promote efficiency and profitability of SACCOs which was also part of the elements of the Prosperity for All (PFA) Programme introduced in 2008 to translate into eventual actual poverty reduction. However, due to the management challenges in SACCO groups and absence of a regulatory law, Uganda Debt Network (UDN) developed proposals which were incorporated into the Tier 4 Microfinance Institutions and Money Lenders Act 2016. The Ministry of Finance Planning and Economic Development is currently formulating the guidelines and regulations to operationalize the Act and UDN wishes to share and discuss her input with the ministry for adoption.

Overview of Uganda Debt Network (UDN)

UDN is a national policy advocacy organization that promotes and advocates for poor and marginalized people to participate in influencing poverty focused policies, demand for their rights and monitor service delivery to ensure prudent, accountable and transparent resource generation and utilization. Currently, UDN operates in 24 districts and over 80 sub-counties; and engages with various Government Ministries Departments and Agencies at national level, and through partnerships with Local Governments and nurturing CBOs at Sub national Levels. At the national level, the organization engages with various Government Ministries, Departments and Agencies on issues of service delivery, public sector accountability, budget processes and policy alternatives; some of which have been adopted by the various relevant stakeholders.

UDN ADVOCACY JOURNEY ON MANAGEMENT OF SACCOS

In 2012, UDN assessed the performance of Prosperity for All (PFA) programme; a poverty alleviation initiative launched by Government in 2007 and held engagement dialogue meetings with officials in the Microfinance Department in the MoFPED, Cabinet, Office of the Vice President, International Fund for Agricultural Development (IFAD) and Parliament to discuss proposals for more effective operation of SACCOS in Uganda. Due to constant advocacy with the relevant stakeholders, four UDN proposals were adopted into the Tier 4 Microfinance Institutions and Money Lenders Act (2016)¹.

UDN congratulates the Ministry of Finance Planning and Economic Development upon achieving the passing of the Act and wishes to share proposals for incorporation in the guidelines that will regulate the operations of Microfinance and Money lending institutions. Specific emphasis is put on improving delivery and accountability of the management of SACCOS. UDN envisages that regulating SACCOS will;

- a) Ensure that rights and interests of the different stakeholders are respected and protected in pursuit of the entity's objectives.
- b) Enhance Governance through improved transparency and accountability in the business conduct (or management)
- c) Deepen access to financial services and thus contribution to the social-economic empowerment of the citizens.

¹ a) Establishment of a legal regime Regulatory Authority and supervisory system of SACCOS (Clauses 6), b) to retain membership, all SACCO members should have access to loans available, Clause 37 (2) (a); c) Publication of SACCO information and related records in public places to improve and to strengthen transparency Clause 43; and d) Equal treatment with regard to policies on loan appraisal and disbursements, repayment procedures, savings accounts, interest rates calculations and other financial policies Clauses 51 (2).

Proposals for Guidelines and Regulations for the Tier 4 Microfinance Institutions and Money Lenders Act 2016

1. **The Microfinance Regulatory Authority:** Part II of the Act upholds the establishment of the Uganda Microfinance Regulatory Authority as an autonomous body. However; the extent to which the Authority should be centralized or decentralized needs to be clarified in the regulations. As the Central Bank is responsible for prudential supervision and regulation of licensed financial institutions, the Authority should set respective regulatory units with specialized responsibilities fragmented among them for effective management e.g
 - i) A co-operatives authority responsible for member-based SACCOs
 - ii) A unit to register Non-Governmental Organizations MFIs
 - iii) A Unit to register Microfinance Deposit Taking Institutions.
 - iv) Regional or District Microfinance Units need to be formed to ensure efficiency and relax on crowding at State level Microfinance regulatory Units as members follow up on SACCO related processes.

This will streamline records of specific institutions given the large number of MFIs the Authority is expected to regulate under the microfinance law but also ease the supervisory burden on Central Bank.

2. **SACCO Regulation and Supervision.** The Regulatory Authority should provide regulatory and supervisory services to SACCOs to ensure compliance with the Act, Regulations, related

bylaws, policies, procedures and all other applicable laws. This will require the Authority to access to all premises and scrutinize documents or records of SACCOs to ensure capital capability requirements. The Authority should carry out on-site inspection of SACCOs and give written feedback of its findings from spot checks with highlights of corrective or remedial actions to be undertaken in a specified period of time. All this is aimed at improving the performance of SACCOs since they will be careful not to breach or fail to – adhere to the requirements and regulations of the Act, while conducting business.

3. Credit Policy: Subject to Section 51 of the Act on Credit, subsection (1) requires a SACCO to have a Credit Policy which indicates terms and conditions of repayment, maximum amount to be borrowed and an acceptable security for the loan. The documented Credit Policy should be consistent with the relevant provisions of the Act, the Regulations and any other applicable laws.

- a) The policy should contain information on;
 - i) Borrowing guidelines/procedures and required documentation.
 - ii) Loan types, maximum loan size per available product, interest rates and frequency of payments.
 - iii) Requirements for approving and granting a loan request.
 - iv) Acceptable types of loan security and agreeable loan purposes.
 - v) Loan appraisal and guaranteeing requirements.

- b) The regulations should uphold that members make repayment of a loan prior to its maturity in whole or in part without being charged full-term interest. This will reduce the risk on the total loan by reducing default rates hence safeguarding members' savings.

4. Credit Issuance and Administration: The regulations should emphasize that responsible persons who lends money from a SACCO to a loan applicant in breach of the requirements commits an offence which is punishable. The regulations should as well determine the punishment. Some of the requirements for credit issuance for consideration include;

- a) **Standard Loan application forms:** Loan applications should be made on agreed standard forms by SACCO members. The forms should be issued by the Committee members. The forms should provide a fill-in section on the purpose for which the loan is being requested. The purpose should be lawful and must be declared in the loan application form.
- b) **Collateral or loan Security:** Information on the collateral or loan security should be provided by the loan applicant before the SACCO Credit Committee inspects and reviews the status of the collateral. Marketable and acceptable security needs to be attached to all loan requests with reference to the set limits in the regulations. The loan security should be in the possession or within the control of the SACCO with proper documentation and registration before a loan transfer transaction is made. Security documents should be kept in safe custody and registers for such security should be maintained to keep track of their movement. The SACCO leadership should conduct an annual assessment of the value of collateral to confirm that it remains realizable.
- c) **Capacity to repay the loan:** In order to determine a member's ability to repay the loan, the Credit Committee should make careful inquiry on the character/behavior (including history of mental stability if necessary) and the financial conditions of each loan applicant and guarantors. No member should be given a loan unless he/she provides sufficient evidence that he/she will repay the loan.
- d) **Guarantorship:** A guarantor should be adequately informed of his/her role and the nature of liability prior to signing an agreement to stand surety for the borrower. There is need to determine the limit in terms of loan amounts and number of loan applicants one can guarantee to deter over-guarantor ship.
- e) **Priority in granting loan requests:** In the event that SACCO funds are in short supply for members to borrow, priority in the granting of loans should be given to smaller loan requests based on the degree of emergency.

- f) **Loan terms and repayment conditions:** The regulations should guide on the maximum period within which a member can serve a loan, mode of repayment e.g; in installments with a grace period (if agreed by members) up to a certain agreed period.
 - g) **Debt Collection committee.** When a loan application is approved, it is expected that the applicant will repay the loan based on agreed terms and conditions. However, in case of suspected default tendencies, the SACCO should appoint a Credit Committee to devise means of recovering such a loan from the member after exhausting the normal debt collection procedures. Loans with deteriorating ratings should therefore be subjected to additional oversight and monitoring through more visits from the credit committee and credit officers. This should be done in a manner that doesn't undermine or threatens but encourages the defaulting member to repay the loan
 - h) **Board Credit Committee:** This Committee should be established to oversee credit risk taking business ventures and overall credit risk management function within a SACCO. It should ensure that the credit risk policy/strategy approved by the board is being implemented by the SACCO.
- 5. Inter SACCO Borrowings:** A SACCO may wish to borrow or lend to another SACCO to mobilize more funding for member loans or to finance temporary liquidity shortages. The regulations should therefore ensure that the Board of Directors of both SACCOs approves the process of borrowing or lending to other SACCOs. This should be supported with a signed agreement between both SACCOs and the loan amount should not exceed the prescribed limit for external borrowing. Limits on such inter SACCO borrowing should also be contained in the regulations.
- 6. Introducing a new SACCO product:** The regulations should guide on how a SACCO may introduce a new loan product for roll out eg;
- a) Approval from the Authority/Board of Directors should be sought.

- b) Evidence of demand for the product and market targeted.
 - c) Evidence of availability of qualified and experienced staff with capacity to manage the new product.
- 7. Relocation of business:** In the event that there is need for relocating a SACCO, a written approval by the Regulatory Authority should be sought by members of the Executive before relocation. The SACCO intending to relocate the business premises should give the Authority reasons why and the re-settlement plan. The Authority should establish that preparations of the new business premises are completed.
- 8. Closure of a business place:** A SACCO intending to close a business should make an application to the Regulatory Authority citing reasons for such closure (permanently or temporarily). A plan for settlement or transfer of assets and liabilities should be spelt out. Before closure, on verification, the Authority should make an approval.
- 9. Opening and operating a new SACCO branch:** A SACCO should seek permission from the Regulatory Authority through an application for opening and operating a new SACCO branch. The Authority should then inspect the premises and examine compliance with the standards in the guidelines. If satisfied with the operational readiness of the SACCO for commencing operations, an approval for a new branch should be granted by the Authority after any prescribed payments are made.
- 10. Non Compliance by a SACCO on capital adequacy:** The Regulatory Authority should pursue administrative sanctions on a SACCO where it fails to meet its capital adequacy requirements e.g. suspension from;
- i) Acquiring any additional land, buildings and any other assets;
 - ii) Lending, investment and from accepting new deposits.
 - iii) Declaring dividends, paying bonuses, salary incentives and other discretionary compensation to officers of the SACCO

- iv) Engaging in activities that the Regulatory Authority recognizes to be causing liquidity strain in the SACCO.

- 11. SACCO Liquidity Management:** To ensure effective liquidity management of SACCOs, the Board of Directors of the SACCOs should formulate a Liquidity Policy to be reviewed and adjusted periodically.
- 12. A Contingency plan:** The plan should be developed to handle liquidity crises in addition to measures for making up liquidity shortfalls in emergency situations where the usual approaches to funding operations are disrupted.
- 13. Investment Policy:** SACCOs should endeavor to formulate an Investment Policy that is consistent with the Act and regulations, and should be subjected to review and amendment periodically where necessary. The policy will act as a guide to SACCOs on any investment plans they may have as well as monitoring and effective reporting. On realization of surplus funds to its operating requirements and not immediately required to finance core operations, a SACCO may invest any of such funds.

CONCLUSION

SACCOs are important in fulfilling the goals of financial inclusion hence the need for a regulatory policy to govern their operations in the financial sector. Incorporating SACCOs into the formal financial system offers an alternative to using microcredit as an instrument for socially-motivated poverty alleviation projects. Saccos emphasize the financial sustainability necessary to serving the poor without depending on subsidies. For this UDN, will always share her views with the MoFPED during the formulation of the guidelines and regulations for operationalizing the Tier 4 Microfinance Institutions and Money Lenders Act, 2016.

VISION

A Uganda where public resources are prudently, sustainably and equitably managed.

MISSION

To generate advocacy expertise that influences people-based and accountable public resource management in Uganda.



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