The Regulation of Microfinance in Zambia

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ABBREVIATIONS

AMIZ	Association of Microfinance Institutions of Zambia
BFSA	Banking and Financial Services Act as amended in 2000 and 2005
BoZ	Bank of Zambia
CEO	Chief executive officer
CFO	Chief financial officer
CSO	Central Statistics Office
DT	Deposit taking
EU	European Union
MBT	Microbankers Trust
MFI	Microfinance institution
MFRs	Microfinance Regulations
MoFNP	Ministry of Finance and National Planning
NDT	Non deposit taking
NGO	Nongovernmental organization
SI	Statutory Instrument

INTRODUCTION

Until two decades ago, Zambia was one of the most prosperous countries in sub-Saharan Africa (SSA), but is now one of the least developed countries in the world. Approximately 64%[1] of a population of 12.9[2] million is living in poverty. The average population density ranges from 4.6 persons per square kilometre to 63.5 persons in the capital, Lusaka, with a national average of 13.1 persons per square kilometre[3]. The informal sector in Zambia, as in many other developing countries, remains the most dynamic in terms of employment generation. Policies to support this sector, are being put in place and the Government of Zambia perceives the role of microfinance to be crucial in this regard.

Moreover, economic reforms, which included the liberalisation of the financial sector, undertaken in the early 1990's; as well as the failure of state owned financial institutions; led to a financial sector that focused on meeting the needs of the corporate sector and working class elite. This led to the increase in the number of microfinance institutions (MFIs) operating in the financial sector. These MFIs were established to fill the gap that had been created with respect to the provision of financial services to low income households and the poor. This development led to calls by politicians, regulators and MFIs – through the Association for Microfinance Institutions of Zambia (AMIZ) - for the microfinance sector to be regulated and supervised as part of the financial sector.

THE MICROFINANCE SECTOR BEFORE THE REGULATIONS

To foster the interests of the microfinance sector, two organisations, the MicroBankers Trust (MBT) and the Association of Microfinance Institutions of Zambia (AMIZ), were set up. MBT was set up in 1996 by the Government and the European Union (EU) as part of the Microcredit Delivery for the Empowerment of the Poor Program to provide wholesale funds and training to MFIs. The primary objective of MBT was to empower vulnerable individuals through wholesale funding to MFIs, strengthen institutional capacity through staff training, assist in the development of viable, effective microcredit delivery systems, and improve MFI performance through evaluation, research, performance monitoring, and sound lending policies[4]. In 2000, MBT stopped providing wholesale funding and now provides microcredit directly to clients.

AMIZ was established by microfinance practitioners and was officially registered in March 1998. It took a lead role in campaigning for new legislation, standard setting and staff training for new MFIs. Its mission is to "facilitate, support and strengthen the services provided by member MFIs and represent them in the best way possible by utilizing microfinance best practices"[5]. AMIZ currently has a membership of 24 MFIs.

A survey conducted in 2004 revealed that the microfinance sector in Zambia was served by a variety of microfinance providers with a variety of legal forms registered under different acts[6]. These legal forms included societies (49%), companies (21%), cooperatives (21%) and statutory bodies (5%). Institutional forms included MFI NGOs

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[1] http://www.zamstats.gov.zm/lcm.php
[2] http://www.zamstats.gov.zm/media/projected_mid_year_population.pdf
[3] CSO, 2003
[4] Mbanacele, 2000; Musona and Coetzee, 2001b.
[5] AMIZ, 2003: 3
[6] Chiumya, 2006.

(26%), cooperatives (21%), commercial banks (15%), NGOs (13%)[7] and business associations (13%). The sector was dominated by member based organisations (48%) followed by NGOs (18%).

Societies and cooperatives are typically member based organisations. They are formed by a group of people (i.e. the "members") with a common interest[8] getting together and providing each other with microfinancial services. In this case, the members are the "owners" and funding is from the members in the form of savings. NGOs are typically set up as trusts which are registered with the Registrar of Societies. The main source of funding for these types of MFIs was donors and developmental organisations (41%).

The service being provided was predominantly microcredit, mainly for agriculture and trade/commercial loans for a duration of 6 months to one year. Loan sizes ranged from K50,000 (USD 11) to (USD 2,265)[9]. Both group lending and individual lending methodologies were used. Different types of collateral, ranging from personal to group guarantees, land, forced savings, household goods, cars and livestock.

With the exception of banks involved in the provision of microfinance, MFIs generally did not provide financial services other than microcredit. Those that provided savings facilities did so in the form of forced or compulsory savings which served as collateral against the clients' loans. This may have been due to the fact that the regulatory environment did not permit the mobilisation of deposits without a banking licence.

According to the survey results, there was not much difference in the reported distribution of clients between the genders. There was more of a difference in relation to urban distribution, with most clients being located in urban areas, i.e. along the "line of rail" (from the Copperbelt Province in the north to Livingstone in the Southern Province), stemming from the fact that most MFIs were located along the line of rail. The population density is highest along the line of rail; the quality of physical infrastructure, e.g. roads, telecommunications, and electricity is better than in outlying areas; and lastly cash transactions dominate whereas barter is still common in rural areas. In urban areas, most MFIs were located in compounds (urban slums) and by implication, therefore, targeted the population at the lower end of the income spectrum. Client selection was based primarily on interest in the program (46%), followed by poverty levels (13%).

Despite the increase in the number of MFIs, outreach was poor. The number of active clients reported by the survey respondents totalled approximately 15,356[10]. Although calls were made to regulate the sector, the industry was small and showing signs of contraction.

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[7] The distinction between MFI NGOs and NGOs is that MFI NGOs were set up solely to provide microfinancial, services whereas NGOs have a broader mandate which, in addition to the provision of micorifnancial services, also includes the provision of services such as health, education and business development services (BDS).

[8] The common interest may be professional, business or simply geographic.

[9] At the Bank of Zambia exchange rate of K4,414.90 as at 20 January 2010.

[10] However, this figure was probably grossly understated as it did not include figures from the banks which serve low income households. The same applies to the figures for the number of loans outstanding.

OBJECTIVES FOR REGULATING AND SUPERVISING THE SECTOR

A number of reasons were given for regulating the sector. Those given by Bank of Zambia (BoZ) officials included the need to maintain financial system stability and safeguard depositors' funds. Linked to this objective, was the need to protect customers and investors and ensure donor funds were being used efficiently and effectively for the purpose for which the funds were intended. It was felt that regulations would improve the integrity and credibility of MFIs operating in the sector and set minimum standards, checks and balances, thus improving the performance of MFIs and enhancing confidence in the microfinance sector. Regulation was also needed to promote the industry and encourage growth so that access to financial services by the majority of Zambians that did not have access would be increased, especially in rural areas. Lastly, BoZ officials felt that regulations would reduce the ambiguity that existed in the regulatory environment, especially with regard to the classification and treatment of "compulsory" or "forced" savings, and "insurance fees".

Reasons given by other stakeholders included the belief that regulation would facilitate the mainstreaming of microfinance, the collection of data and the monitoring of developments in the sector. Regulation would minimize exploitation of the public, and for this reason, stakeholders felt that interest rates, should, to some extent, be regulated. It was felt that the only way to achieve the objectives would be to introduce microfinance specific regulations. The process of developing the regulations started in 1999, culminating in the passing of the Banking and Financial Services (Microfinance) Regulations (MFRs) which became law on 30 January 2006.

THE LEGAL AND SUPERVISORY FRAMEWORK

REGULATION AND SUPERVISION OF THE FINANCIAL SECTOR

The responsibility of regulating and supervising the financial sector[11] lies with the central bank, the Bank of Zambia. The functions of the Bank of Zambia are contained in section 4 of the Bank of Zambia Act, 1996, which states that "the Bank shall formulate and implement monetary and supervisory policy that will ensure the maintenance of price and financial systems stability so as to promote macroeconomic development". To achieve this objective, the Bank of Zambia is authorised by the same Act to, amongst other things, license, supervise and regulate the activities of banks and financial institutions[12] and carry out the inspections of any bank or financial institution as the Bank deems necessary[13].

The financial sector is governed principally by the Banking and Financial Services Act of 1994 as amended in 2000 and 2005 (BFSA). The Act authorises the Minister of Finance and National Planning (MoFNP), on the recommendation of the Bank of Zambia, to issue regulations[14] to facilitate implementation of the Act. It also authorises the Bank of

[11] For the purpose of this paper, the "financial sector" comprises all the financial institutions that fall under the regulatory and supervisory ambit of the Bank of Zambia. Therefore, insurance companies, persons regulated by the Securities Act of 1993 such as brokerage firms and security houses and other financial service providers regulated by other regulatory authorities such as money lenders and hire purchase companies are not included.
[12] Section 4(2)(a).
[13] Section 42.
[14] Section 124, BFSA. Regulations are issued as "statutory instruments" (SIs).

Zambia to issue directives[15] and guidelines[16]. Thus the MFRs were issued under the BFSA.

DEVELOPMENT OF THE MICROFINANCE REGULATIONS

In developing the regulatory framework for microfinance, the Bank of Zambia undertook the 'Development of the Microfinance Regulation' Project. The Project had 3 main objectives. These were to develop regulations, prudential reports and the systems necessary for the effective supervision of MFIs; develop Bank of Zambia's capacity to effectively supervise MFIs; and to educate MFIs to facilitate their understanding and compliance with regulatory and supervisory requirements. The project was broken down into 2 phases. Phase I, undertaken in 1999, involved a survey of the microfinance sector covering key issues of governance, lending, financing, equity, accounting, staffing and legal status. The objective of this phase was to obtain an understanding of the market and its players to develop an appropriate regulatory and supervisory framework.

The survey results revealed a number of weaknesses in the sector. Firstly, although MFIs were committed to serving the poor, this was not done in an efficient, transparent and sustainable manner. Secondly, external reporting to clients and investors was either erratic or non-existent. Thirdly, there had been instances in which the public had been defrauded by unscrupulous persons posing as MFI officers. Fourthly, there was insufficient monitoring of MFIs by investors to ensure institutional soundness and self-sufficiency. Lastly, there was inadequate disclosure to clients regarding services, requirements and costs[17].

In the Bank of Zambia's view, the lack of a legal and supervisory framework for MFIs meant that the sector's stability was not guaranteed and regulation of this sector would achieve the goals of maintaining financial market stability, encouraging responsible growth and deepening financial services available to Zambians. Phase II of the project commenced in September 2001. Phase II focused on (1) developing and implementing regulations and (2) establishing and commencing operation of a supervisory framework for MFIs based on the results of Phase I. Both phases involved extensive stakeholder consultation. The process culminated in the development of the Banking and Financial Services (Microfinance) Regulations (MFRs) which became law on 30 January 2006.

SALIENT FEATURES/PROVISIONS OF THE MFI REGULATIONS

The MFRs define *microfinance institution*, *microfinance service, microcredit* and *savings* as follows[18]:

Microfinance institution – "*a person who, as part of their business, advances microcredit facilities*";

Microfinance service – "*the provision of services primarily to small or micro enterprises or low income customers and includes the following:*

(a) The provision of credit facilities usually characterised by frequent repayments; and

(b) *The acceptance of remittances and any other services that the Bank of Zambia may designate*";

[15] Directives are issued as "circulars".
[16] Sections 124A and 125 respectively of the BFSA 2000.
[17] Mudenda, 2002
[18] Regulation 2.

Microcredit – "*a credit facility that does not exceed five per centum of the primary capital of a licensed microfinance institution, as prescribed by the Bank of Zambia*";

Savings – "*a sum of money provided by the borrower as a partial guarantee or as precondition of a loan, and the immediate placement of such money in a bank or deposit taking financial institution...for the period of the loan*".

MFIs are categorised into three tiers[19]. These are: (1) Tier I - deposit taking (DT) MFIs; (2) Tier II - non-deposit taking (NDT) MFIs with paid up capital greater than K25 million[20]; and (3) Tier III - NDT MFIs with paid up capital less than K25 million[21]. Tier I and Tier II are currently regulated and supervised by the Bank of Zambia. Tier III MFIs are not supervised nor are they required to obtain a licence. It is expected that the oversight of Tier III MFIs will be done by the supervisory authority under which the MFI is registered as an interim measure[22]. The MFRs prohibit any institution not licensed by the Bank of Zambia from conducting "microfinance business"[23]. Financial institutions that are licensed to conduct "financial services", including banks, do not have to apply for a licence under the MFRs.

DT MFIs are required to have a minimum regulatory capital of K250 million[24]. The lower capital requirement is expected to have a positive impact on the microfinance sector in that more organizations should be able to satisfy the this capital requirement, enabling a higher number of MFIs to enter the microfinance sector than would otherwise be the case.

DT MFIs must be registered as companies and voting control is limited to a maximum of 25% per shareholder, unless Bank of Zambia approval is obtained to control more[25]. NDT MFIs are permitted to have a number of different legal forms which includes a company, a nongovernmental organisation (NGO) registered with the Registrar of Societies, or a cooperative. However, if a NDT MFI is registered as a company, then voting control is limited to a maximum of 50% per shareholder, unless Bank of Zambia approval is obtained to control more[26]. Trusts are not permitted to own shares or control MFIs[27].

MFIs that are companies must have a minimum of five board members[28] and separate individuals as the chief executive officer (CEO) and chief financial officer (CFO)[29]. The main reasons for these provisions are to ensure transparency with regard to the ownership structure of MFIs and improve their governance by limiting the amount of control vested in a single individual. In the development of the regulations, it was felt that these were particularly important as MFIs served one of the most vulnerable segments of the population and these provisions would minimize the likelihood of exploitation and abuse of MFIs clients.

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[19] Regulation 14.
[20] Approximately USD5,700 at the Bank of Zambia exchange rate, 18 January 2010
[21] Regulation 26.
[22] For instance the Registrar of Societies, the Registrar of Cooperatives, etc.
[23] Regulation 6.
[24] Approximately USD56,600. The BFSA (Capital Adequacy) Notice, 2006. This is lower than that required for other deposit taking financial institutions (Appendix 1).
[25] Regulation 35.
[26] Regulation 35.
[27] Section 24A, BFSA.
[28] Regulation 20.
[29] Regulation 21.

Under the MFRs, the services and products that can be provided by DT MFIs are restricted to the provision of credit facilities, linkage banking, in-country transfers and compulsory savings for borrowers[30]. NDT MFIs can only provide credit facilities[31]. In addition to restricting the type of deposits that MFIs can accept to compulsory savings, the MFRs make it clear that cash received as collateral, whether it is referred to as "forced savings", "compulsory savings" or "loan insurance fee", is classified as a deposit[32]. Thus the MFRs clarify the treatment of "cash collateral".

Both DT MFIs and NDT MFIs have to submit prudential reports to the Bank of Zambia on a monthly and quarterly basis respectively[33]. As licensed institutions, MFIs are subject to onsite inspection by the Bank of Zambia on a periodic basis[34].

THE MICROFINANCE SECTOR AFTER THE REGULATIONS

There are currently 25 MFIs licensed by the Bank of Zambia, an increase of 21 from 4 at the time the regulations were passed[35]. One of the main reasons for this increase was the requirement for all MFIs in existence at the time the regulations were passed to apply for licences and that fact that it is illegal to conduct microfinance business without a licence. Of the 25 MFIs licensed, 8 (16%) existed prior to the regulations being passed. Although it was set up to contribute to the development of the microfinance sector through the provision of wholesale funding to MFIs, MBT was required to apply for a licence under the MFRs, which it did. AMIZ, on the other hand, as an association did not fall within the definition of an MFI and therefore did not have to apply for a licence.

There are two main types of microfinance providers, payroll based consumer lenders[36] and microenterprise lenders ("conventional" microfinance). Of the 25 licensed microfinance providers, 21 (84%) were payroll based consumer lenders and accounted for 92% of the microfinance sector's total assets. Only 4 MFIs (16%) were microenterprise lenders. Six MFIs (24%) are licensed as deposit taking financial institutions (Appendix 2).

All MFIs licensed by the Bank of Zambia are companies. Those that were not companies prior to the MFRs being passed changed their legal form (typically from NGOs registered as societies) to companies. This applies even to those that are NDT. Eighteen of the 25 MFIs have 5 directors. It is clearly evident that these developments; specifically that all the licensed MFIs, including those that are NDT, are companies; and that most of the MFIs have 5 directors; are a result of the MFRs.

The structure of the industry has changed significantly with the proliferation of payroll based consumer lenders. This was not anticipated at the time the MFRs were being drafted. This has raised the question as to whether the current regulatory framework is appropriate in light of this development. The Bank of Zambia is reviewing the current

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[30] Regulation 15.
[31] Regulation 16.
[32] Regulation 2.
[33] Regulation 38.
[34] Regulation 37.
[35] The four that had NBFIs licences were Bayport Financial Services Limited, Blue Cash Xpress Limited (formerly Nedfin), Blue Financial Services Zambia Limited and Microfin Africa Zambia Limited.
[36] Payroll based consumer lending is lending to individuals in formal employment. Repayments are typically deducted directly from the payroll. As such, the employer signs an agreement with the MFI to facilitate the deductions from the payroll. Repayment periods range from 3 months to one year.

regulatory framework with a view to determining what changes are needed, if any. This is part of a broader law review exercise being undertaken under the Financial Sector Development Programme (FSDP).

Even then, the microfinance sector still accounts for a very small proportion of the financial sector. Total assets account for less than 35% of total assets for the non bank financial institutions sector and less than 3% when the banking sector is included[37]. All the MFIs currently licensed by the Bank of Zambia are companies registered under the Companies Act.

ATTAINMENT OF THE OBJECTIVES

As noted above, it was felt that the objectives could only be met with the introduction of microfinance specific regulations. With regard to the first objective of maintaining financial system stability, the microfinance sector in Zambia is very small in comparison to the rest of the financial sector, which is still dominated by the banking sector. Therefore, MFIs are low in risk in relation to financial system stability and the failure of even the largest MFI would not have any impact on financial sector stability[38]. Moreover, most MFIs do not accept deposits and are not part of the payment systems.

Similarly, in relation to the protection of depositors' funds, this matter was not addressed specifically by the MFRs. Furthermore, most MFIs are NDT and those that are DT do not provide a savings facility per se, but accept deposits in the form of "insurance fees" or "forced" or "compulsory" savings which serve to act as security for loans obtained by the client. In most cases, the position is that the client is a net borrower and not a net saver. It is the MFI that still stands to lose if the MFI should close. However, to the extent that the MFRs require MFIs to maintain adequate capital levels to absorb losses, adhere to minimum performance standards and maintain internal systems of control to monitor and manage risk, thus minimising the probability of failure, depositors and investors are somewhat protected. With respect to ensuring that public resources and donor funds are used effectively and for the purpose for which they were intended, this issue is not addressed by the MFRs.

With respect to the MFRs improving the integrity and credibility of the microfinance sector, setting minimum standards, checks and balances, thus enhancing confidence in the sector; discussions with various stakeholders provide some indication that this has been achieved to some extent. It is much easier, with the MFRs in place, to advise the general public to deal only with institutions that are licensed by the Bank of Zambia. Having to comply with the law with respect to having minimum standards for MIS, internal controls and risk management systems, as well as the reporting requirements, has improved levels of disclosure and transparency in the sector. MFIs, if they weren't already, are now more conscious of their performance and sustainability.

MFIs are now required to submit prudential reports to the Bank of Zambia. DT MFIs are also required to publish, on a quarterly basis, their financial statements and make them available to the public upon request. More information, therefore, is readily available to the Bank of Zambia and general public. Furthermore, MFIs are required to disclose their charges and interest rates in relation to the services and products on offer.

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[37] Bank Supervision Department and Non Bank Financial Institutions Supervision Department Reports to the 1st Supervisory Policy Committee Meeting of 2010.

[38] The closure of PRIDE, a NDT MFI, in 2008 did not have any impact at all on the financial sector.

These are published a newspaper of general circulation on a bi-annual basis for the public to make comparisons between the different institutions. The MFRs also require that MFIs have clear procedures in place for dealing with customer complaints, after which consumers have recourse to the Central Bank. These provisions, it is believed, are helping to reduce levels of consumer exploitation.

Lastly, the ambiguity and confusion that existed regarding the position and treatment of "insurance fees", "compulsory" and "forced" savings has been clarified. MFIs that charge loan "insurance fees", or require "forced" or "compulsory" savings as security will be deemed to be accepting deposits and treated as DT MFIs for regulatory and supervisory purposes. All MFIs now have to apply for a licence or risk prosecution.

IMPACT ON THE DEVELOPMENT OF THE SECTOR

More broadly, the MFRs have clarified the regulatory requirements for MFIs irrespective of their (original) institutional type, especially for NGOs. Any organisation conducting "microfinance business" falls under the regulatory and supervisory ambit of the Bank of Zambia. The influx of MFIs, albeit payroll based consumer lenders, is believed to be a direct result of this clarification. Knowing what is expected and required to conduct a specific type of business, or provide a particular service, makes it less risky for an investor to engage in the activity in question.

Clearly the regulations have shaped the legal form taken by licensed MFIs. As stated above, all licensed MFIs are registered as companies. Those MFIs that were in operation prior to the MFRs being passed and have obtained a licence have changed their legal form[39]. Furthermore, the majority of MFIs have 5 directors. The question arises as to whether the shareholders of all the MFIs licensed would feel the need to have 5 directors as stipulated in law considering the size and nature of the MFIs' operations.

Compliance costs are believed to be high. In addition to the requirement to have a minimum of 5 directors, the need to have different individuals for CEO and a CFO regardless of the MFIs size and level of sophistication, means high staff costs. The costs in terms of time, effort and resources associated with meeting reporting requirements of publication and prudential reports; preparing for inspections, assisting inspectors during inspections, and the disruption caused to business; opening new branches; having to have an annual audit; and the annual supervision fee (which the Bank of Zambia has not started charging as yet), all serve to increase the costs of operating an MFI. This has had an adverse impact on the number of institutions applying for a licence. However, it is difficult to determine to what extent entry into the microfinance sector has been directly affected (negatively or otherwise) by the level of compliance costs.

The MFRs are rather restrictive in terms of the services that can be offered by an MFI as noted above. One MFI has had to apply for a DT MFI licence in order to provide services other than credit facilities. This possibly has had a negative effect on services that can be offered by an MFI, thus affecting outreach. MFIs are still concentrated along the "line of rail". Even with the entry of the new MFIs, most are located in the capital, Lusaka. Only 3 MFIs have branches away from the line of rail. The developments in the microfinance sector have not necessarily led to the increase in access to financial services by the unbanked. Most of the new MFIs target salaried employees,

[39] CETZAM Financial Services Limited (DT), FINCA Zambia Limited (DT), and Pulse Financial Services Limited (DT). Microbankers Trust (DT) has yet to regularise its ownership structure.

most of whom already have bank accounts through which their salaries are paid. On the other hand, though there has been an increase in the level of indebtedness as a direct result of the ease with which these individuals can access loans, often from different lenders. This is proving to be a concern and ways of instituting responsible lending are being explored by the Bank of Zambia. For those MFIs that focus on enterprise lending, their client base remains very small and has not grown significantly in the last 4 years.

CHALLENGES FACED IN ENFORCING THE MFRS

The Bank of Zambia has faced a number of challenges in enforcing the MFRS. The first relates to the requirement for all MFIs in operation at the time the MFRs were passed to apply for a licence within one month. Not all have done so[40]. In addition to this, MFIs had to comply with the capital adequacy requirements which were revised in December 2006 as noted in Appendix 1. The MFIs had until the 30th of June 2008 to comply. In addition to the capacity constraints faced by the Bank of Zambia, which include staffing, there has been a reluctance to close MFIs that have not obtained a licence to date, especially if the MFI is NDT. The Bank's approach has been to actively "persuade" institutions to comply.

The governance structure, especially the requirement for DT MFIs to be companies registered with the Registrar of Companies and the restriction of voting control to 25% proved problematic, especially for those MFIs already in existence. Although, the MFIs in question did succeed in the end, it was only through a lot of negotiation and perseverance between the Bank of Zambia and the founders of the MFIs in question. However, in relation to MBT, this matter has still not been resolved.

Taken in totality, the number of organisations engaged in "microfinance business" is significant. However, despite being significant in number, these organisations account for an insignificant proportion of the financial sector as a whole. As a result, the Bank of Zambia has not been able to effectively supervise all institutions operating in the sector and is seeking to delegate the supervision of Tier III MFIs to a separate entity. Having recognised that the authorities under which Tier III MFIs might be registered do not have capacity to supervise the MFIs effectively, the Bank of Zambia as part of the FSDP is exploring ways in which Tier III MFIs can be supervised. This process will also identify which organisation would be the most appropriate to undertake the supervisory function or whether there will be a need to establish one.

IN CONCLUSION

The MFRs have now been in existence since January 2006. During this period, the number of licensed institutions has increased from 4 to 25. It is evident that a lot of faith was placed in the MFRs to achieve the objectives of regulating the sector outlined above. The outcomes to date, however, have been mixed. On the one hand, there have been benefits, specifically with regard to the clarification of the legal position of MFIs and the treatment of "insurance fees", "compulsory" and "forced" savings as deposits; increased confidence in the sector through enhanced credibility derived from being a licensed institution and the vetting of entrants; increased transparency through the disclosure of information and charges; and increased capital levels. It is believed that these developments are what have led to the increase in the number of licensed

[40] It is difficult to say how many MFIs exactly that should have applied for a licence have not done so due to insufficient data despite the surveys that were undertaken at the time the MFRs were being developed.

institutions and reduction in the level of customer exploitation and fraudulent behaviour on the part of MFIs and individuals posing as MFIs.

On the other hand, the costs of compliance are relatively high, reflected in the fact that some MFIs have not applied for licences despite the requirement to do so. Compliance costs with regard to meeting reporting requirements, facilitating inspections, and governance are significant, especially for the smaller MFIs. Moreover, the MFRs are restrictive in the types of products and services that can be offered by MFIs. This has no doubt had a negative impact on outreach and increasing access to financial services by low income households and the poor.

There has been a significant increase in the number of MFIs providing payroll based consumer credit and with it, an increase in concerns regarding the rising levels of over-indebtedness and the need to encourage responsible lending. Furthermore, this development, together with the challenges faced in implementing and enforcing the MFRs, has resulted in the Bank of Zambia questioning the appropriateness of the current regulatory framework. There has been a recognition that some provisions are in fact, rather onerous, especially for NDT MFIs. Moreover, capacity constraints have forced the Bank to consider delegated supervision for Tier III MFIs, NDT MFIs with paid up capital less than K25 million.

The current law review exercise being undertaken under the FSDP, covers a review of the BFSA and MFRs, and seeks to incorporate the experience and lessons learned thus far. In the broader context, the Bank of Zambia is in the process of implementing risk based supervision (RBS). RBS is an "approach to supervision where the degree of supervisory attention is dependent on the risk profile of the institution and where the resources of the supervisors are focused on the institutions that pose the greatest risk to the supervisory objective"[41]. Thus the review of the current regulatory and supervisory framework, including the prudential norms and guidelines, is being undertaken in the context of RBS. This process will enable the Bank of Zambia to address, to some extent, the capacity constraints it is facing in carrying out its supervisory function effectively.

[41] Adapted from Ma. Corazon Guerrero (2004:1), "Operational Issues on the Implementation of Risk Based Supervision Framework".

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Appendix 1: Capital requirements for financial institutions

Institutional type	Capital requirement*
Bank	K12 billion (USD 2.8 million)
Development finance institution	K7.5 billion (USD 1.7 million)
Deposit taking leasing company	K1.5 billion (USD 340,000)
Non deposit taking leasing company	K500 million (USD 113,000)

Source: The BFSA (Capital Adequacy) Notice, 2006

* At the Bank of Zambia exchange rate of K4,414.90/USD as at 20 January 2010.

Appendix 2: MFIs licensed by the Bank of Zambia

Name	Registration date.	Licensing date	MFI type	Enterprise lending	Existed prior to MFRs
1. Bayport Financial Services Ltd	18-Feb-02	18-Feb-03	NDT	No	Yes
2. Blue Cash Xpress Ltd	10-Nov-04	23-Nov-05	NDT	No	Yes
3. Blue Financial Services Zambia Ltd	28-Apr-04	17-Nov-05	NDT	No	Yes
4. Bomach Finance Ltd	n/a	16-May-08	NDT	No	No
5. Capital Solutions Ltd	19-Dec-03	20-Mar-08	NDT	No	No
6. CETZAM Financial Services Ltd	06-May-02	14-Oct-08	DT	Yes	Yes
7. Credit Finance Ltd	16-Aug-06	2-Apr-09	NDT	No	No
8. Elpe Finance Ltd	15-Feb-05	03-Oct-06	NDT	No	No
9. FINCA Zambia Ltd	08-Jan-01	08-Apr-08	DT	Yes	Yes
10. Genesis Finance Ltd	21-Dec-07	22-Jul-09	DT	No	No
11. Izwe Loans Zambia Ltd	12-Jul-05	02-Dec-08	NDT	No	No
12. Kungoma Financial Services Ltd	20-Nov-06	2-Apr-09	NDT	No	No
13. Letshego Financial Services Ltd	09-May-06	24-Sep-07	NDT	No	No
14. Meanwood Finance Corporation Ltd	14-Oct-05	15-Sep-09	NDT	No	No
15. Microbankers Trust	05-Jan-01	24-Jul-09	DT	Yes	Yes
16. Microcredit Foundation Ltd	17-Jan-08	11-Sep-09	NDT	No	No
17. Microfin Africa Zambia Ltd	17-Dec-02	17-Nov-03	DT	No	Yes
18. Mtawila Financial Services Ltd	04-May-06	04-Dec-09	NDT	No	No
19. Pelton Finance Ltd	28-Jul-05	14-Nov-08	NDT	No	No
20. Prime Circle Microfinance Ltd	12-Jun-07	30-Apr-09	NDT	No	No
21. Pulse Financial Services Ltd	24-Apr-01	04-Jun-09	DT	Yes	Yes
22. Royal Microfinance of Zambia Ltd	22-Aug-05	11-Apr-07	NDT	No	No
23. Unity Finance Ltd	06-Oct-06	02-Apr-08	NDT	No	No
24. Wide and Deep Services Ltd	01-Apr-08	16-Dec-09	NDT	No	No
25. Yakabutala Musa Company Ltd	12-Jun-96	15-Jul-09	NDT	No	No

n/a - not available