3rd REGIONAL CREDIT INFORMATION SHARING CONFERENCE - KENYA

A. OVERVIEW : CREDIT INFORMATION SHARING

1. Credit information sharing plays a critical role in the functioning of the retail financial services sector at a number of different levels. It:

a. Contributes to increased access to finance by providing critical information necessary for rapid and better informed assessment of credit applications from individuals and SMEs;

b. Is an important tool in preventing over-indebtedness, by making information available on consumer debt levels, enabling early detection of potential over-indebtedness;

c. Provides valuable information for banks and other credit providers to manage credit risk, both in the approval of applications and in the management of the SME and consumer credit portfolios;

d. Supports prudential supervision through better risk management, by reducing the levels of default and risk of bank failure; and

e. Promotes regional commercial activity as it improves commercial and financial institutions' ability to manage their risk on a regional basis.

2. Experts agree broadly on the principles of effective credit reporting systems. In 2011, a task force assembled by the World Bank Group published the "General Principles for Credit Reporting," which articulated a consensus set of standards for effective credit reporting systems. These principles provide good practice guidance to new or developing credit reporting systems and underpin this roadmap.

B. STATUS OF THE CREDIT REFERENCE SYSTEM IN ZIMBABWE

3. A Credit Registry Department has been established as a unit in Bank Supervision Division. The unit will coordinate the collection of credit information from all banking institutions and microfinance institutions and maintain the databank for the credit registry.

4. The Reserve Bank has undertaken regional study tours to gain an understanding of the operations and legal frameworks of CRBs in those jurisdictions.

5. As part of the implementation process, the Reserve Bank has held several meetings with the key stakeholders such as Banking Institutions, private credit bureaus and the Credit Providers Association. To this end, a Stakeholders' Seminar was held in July 2015 to create awareness and present the model being adopted by the Reserve Bank.

6. In addition, three (3) thematic committees, namely Credit Steering Committee, IT Steering Committee and Legal Steering Committee have since been established at BAZ level.

7. The Banking Amendment Bill with provisions empowering the Reserve Bank to establish the credit reference bureau and the issuance of regulations for the licensing, accreditation and operation of private credit reference bureaus has since been passed by both the House of Assembly and the Senate. The Bill now awaits Presidential assent. Further, draft Regulations have been developed and are under review.

8. The Reserve Bank in liaison with stakeholders, are already working on the development of data submission template to enable data providers to submit data in a standardised format.

9. In addition, the Reserve Bank has conducted a survey of the information that is collected by banks and how it is electronically stored and feedback from the banks is under evaluation.

10. The Reserve Bank will continue to conduct consumer education and sensitization campaigns in order to promote an understanding of the benefits accruing from the establishment of credit registry.

11. The processes for the acquisition of the credit reference databank software have begun and are at advanced stages. The vendor who will supply the credit reference

software has been identified and implementation of the system is expected during the first half of 2016.

C. STATUS ON THE ESTABLISHMENT OF A COLLATERAL REGISTRY SYSTEM

12. In the 2015 National Budget, the Honourable Minister of Finance and Economic Development alluded to the emergence of a new economy based on the informal sector.

13. Meanwhile, the majority of SMEs and individuals operating in the informal sector, are not able to access credit from financial institutions due to lack of acceptable security such as houses or factories (immovable collateral) which are preferred by formal lending institutions.

14. Empirical studies have indicate that, in developing economies, 78% of the capital stock of businesses is typically in movable assets such as machinery, equipment or receivables, and only 22% in immovable property (Alvarez de la Campa, 2011). As such, these economic agents, such as SMEs and households, find themselves with **"dead capital"**, in form of moveable assets which they are unable to utilize as collateral.

15. More than 35 countries across the world have established collateral registry systems, as a way of promoting the use of movable collateral by lenders in order to increase access to credit. Of these countries ten (10) are African countries namely: Burundi, Ghana, Kenya, Lesotho, Liberia, Malawi, Nigeria, Sierra Leone, South Africa and Zambia

16. Against this background, the Government and the Reserve Bank in collaboration with the World Bank are working on measures to enhance the range of acceptable and qualifying collateral security in line with international best practices through the establishment of a **collateral registry** for movable property

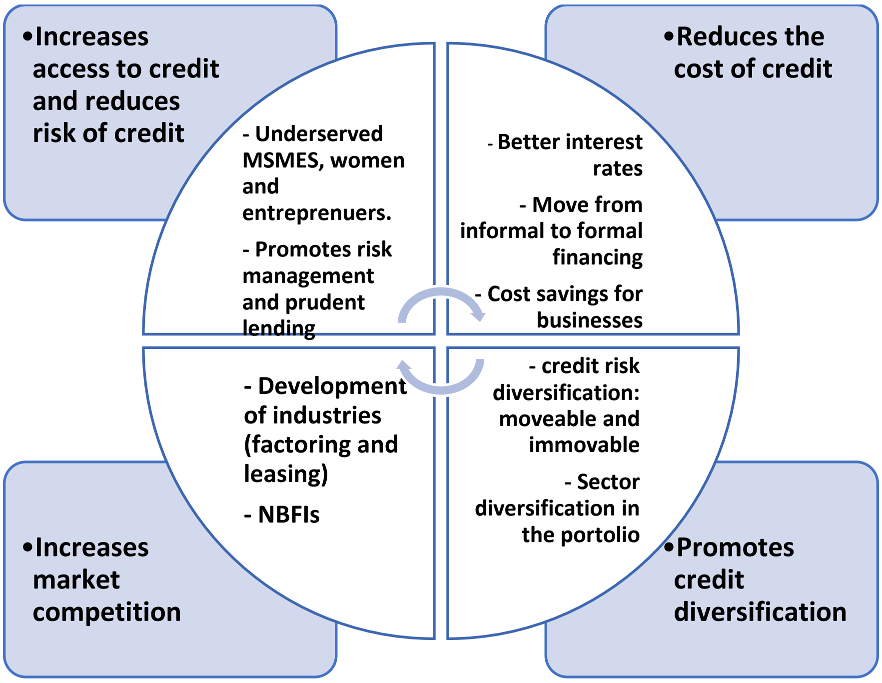
such as machinery, automobiles, inventory, and account receivables, among others.

17. In this regard, the Reserve Bank has created a unit within its structures that **will file notices of security interests in qualifying movable properties** and determine **priority in a borrower's collateral**, so that lenders find it to accept movable property as collateral.

18. A reliable collateral registry or pledge system that allow the use of moveable collateral has a number of benefits to the economy.

Benefits on Collateral Registry System

19. The envisaged benefits of establishing Collateral Registry are depicted in the diagram below:



20. A number of key steps have since been taken towards establishing the collateral registry at the Reserve Bank.

a) Stakeholder sensitisation has commenced. The Reserve Bank in collaboration with the World Bank held stakeholder meetings from 30 November to 4 December 2015.

b) A draft Personal Securities Interest Bill has prepared to provide the supporting legal framework. The promulgation of collateral registry laws will allow for the acquisition of collateral registry software and successful roll out.

D. USE OF CREDIT BUREAU DATA ANALYTICS TO INFORM MONETARY POLICY

21. The goals of monetary policy are to promote maximum employment, stable prices and moderate long-term interest rates. By implementing effective monetary policy, the Central bank can maintain stable prices, thereby supporting conditions for long-term economic growth and maximum employment.

22. A Credit Bureau is a critical part of the financial infrastructure. It provides rapid access to accurate and reliable standardised information on potential borrowers, enabling lenders to evaluate credit risk more accurately and to reduce lending processing time and costs. This in turn promotes profitability and increased credit activity.

23. The use of credit bureau data analytics can inform the Monetary policy in the following:
    a. determine the size and rate of growth of the money supply, which in turn affects interest rates;
    b. modifying the interest rates;
    c. increasing the money supply in order to lower unemployment, boost private-sector borrowing and consumer spending, and stimulate economic growth; and
    d. credit easing which involves the purchase of private-sector assets to boost liquidity.

E. USE OF CREDIT INFORMATION FOR FINANCIAL SECTOR STABILITY: COMPARING CREDIT REGISTRIES & PRIVATE CREDIT BUREAU MODELS

24. Credit reporting has important benefits for financial stability. By providing information on clients' financial behaviour and outstanding debt, credit reporting systems help financial institutions lend to clients who can sustainably use credit. At a large scale, this is essential for preventing over-indebtedness crises, such as those that have recently affected the financial sectors of a number of countries.

25. A basic credit-reporting system is made up of a **public credit registry** and/or **private credit-reporting firms** that function within the necessary legal and regulatory framework for credit reporting and privacy. Many countries **have public credit registries, normally operated by a central bank or bank supervisor.**

26. Public credit registers are non-profit institutions in the ownership of the central bank and part of the supervisory and reporting structure. They are used for off-site bank supervision or compilation of statistics.

27. When comparing the utility of public and private credit registries, it is often believed that a public credit registry can better protect the privacy of consumer/firm data from private firms that sometimes cross legal boundaries. On the other hand, private credit registries have proved more effective in collecting a broader spectrum of information and providing more comprehensive services for customers.

28. The table below summarises the key differences between public and private registries.

Public vs. Private Credit Registries

Feature	**Public**	**Private**
Purpose	Bank supervision & credit checks for lenders	Credit checks for lenders
Source of information	Supervised institutions (banks)	Varied sources (banks, retailers, telecoms)
Positive Info?	Yes	In some cases
Minimum loan size	In some countries	No
Fee for service	No charge or minimal charge	Yes

Basis for operations	Government Regulation	Contract

29. The main motivation for creating Public Credit Registries are to:
    a. To promote exchange of credit information in the financial system
    b. To improve private credit reporting activities
    c. To overcome legal problems with sharing credit information; and
    d. To strengthen supervision of regulated financial institutions.

F. BENEFITS OF CROSS BORDER DATA SHARING

30. Information asymmetries can severely limit cross-border border expansion of banks. When a bank enters a new market, it has incomplete information about potential new clients. Such asymmetries are reduced by credit registers, which distribute financial data on bank clients.

31. The adoption of cross-border information sharing on borrowers as part of regional integration would help control the levels of non-performing loans (NPLs).

32. Through cross border data sharing CRBs are expected to weed out serial defaulters taking advantage of open borders in the region.

33. There is need for Memorandum of Understanding to be signed.

G. CREDIT INFORMATION SHARING LEGAL & REGULATORY FRAMEWORK – OPPORTUNITIES FOR IMPROVEMENT

34. Credit information registries should include objective information relevant for assessing creditworthiness and suitability for commercial transactions. The authorities should adopt a sound legal and regulatory framework for the credit reporting industry. This framework should recognize the critical role played by credit reporting in the development of modern financial systems and the broader economy, while at the same time providing consumers with effective protections against abuse of the information.

35. The key elements of the legal framework should include the following:

a. Legal framework should encourage information sharing among lenders;
b. Regulations should offer consumer protection i.e. restrictions on access to information (permissible purpose, consent), fair credit granting and consumer credit regulations;
c. Borrowers should have access to their own credit reports;
d. Procedures in place to challenge erroneous information in reasonable time frame; consumers should have ability to bring complaints outside judicial system;
e. Maintaining data for a reasonable time period – at least five years;
f. Creating an obsolescence provision which enables consumers to make a fresh-start;
g. Developing an effective strategy for alerting data subjects to problems associated with their report – adverse action notification is recommended;
h. Establishing who has access to the data and under what circumstances;
i. Providing consumers with effective and actionable protections under the law including means to access their own data and dispute resolution mechanisms which are appropriate for consumers with varying levels of education and access to technology;
j. Developing a regulatory structure capable of system supervision. The law should specify the instruments and mechanisms which regulators will have for supervision of the credit reporting industry including issues such as the ability to bring court cases on behalf of a class of plaintiffs, to require external audits, to require reports and access to the database, and to specify penalties and sanctions.
k. Another key aspect of credit reporting law concerns who has access to the data and under what circumstances.

36. Credit registries should not collect highly sensitive information such as political or religious affiliation, race or ethnicity, etc. (Other identifying information, such as gender, should be evaluated more carefully).

H. USE OF CREDIT INFORMATION FOR FINANCIAL INCLUSION AND INNOVATION

37. The absence of credit history has resulted in banking institutions shunning low income groups. Credit information sharing addresses the problem of information asymmetry between borrowers and lenders, which leads to adverse selection, credit rationing, and moral hazard problems. Credit information sharing can thus result in enhanced access to finance by low income households and MSMEs at affordable costs.

38. The low income groups including MSMEs fail to access credit facilities largely due to lack of requisite collateral such as immoveable property that mainstream lenders (financial institutions) require as security. Credit information sharing may also enable low income groups without collateral to leverage on reputational collateral to gain access to funding.

39. Credit information sharing helps identify the data models needed to track healthy lending development. Improving the breadth and quality of information on consumer credit in a market should help identify what providers are offering what kind of products, to what consumer segments, and the performance and health of their consumer credit portfolios.

40. Through Credit information sharing lenders can understand how consumer and behavioral insights might change existing consumer protection guidelines and norms by unlocking how consumers think about consumer credit, and what leads some consumers to manage their debt responsibly while others end up in over their heads.

41. Credit information sharing reduces the cost of doing business - Build information capital, reduce information search costs and problems associated with information asymmetry; and extending credit based on financial identity. This allows change in the collateral technology in use.

42. Financial innovation increases the efficiency of the financial system: Improves efficiency of the financial system and availability of funds for business activities - a positive effect on long-term economic growth.

43. As business models evolve, credit information sharing assist in **learning more about how innovations in branchless banking may expand access to credit** and promote an early assessment of how this might change existing risks or bring new ones.

44. Invest in information sharing systems that are sensitive to the needs and incentives of the data furnishers. For instance, financial services firms have a clear interest in sharing customer payment data with a credit bureau, and need access on the same from other lenders to make responsible lending decisions. Not so for non-financial service providers that aren't assessing risk for enlisting customers and have other means to punish those who pay late or don't pay, such as termination of service. These organizations don't often trust credit bureaus or any third-parties with their data, want remuneration, and fear customer backlash. These must be addressed for this data to be accessed in sufficient quantity for purposes of credit underwriting

45. The project aims to:

a) increase access to finance for households and SMEs,
b) improve risk management for credit providers,
c) curb increasing over-indebtedness
d) contribute to improved bank supervision and compliance with international best practice
e) ensure that information sharing takes place within a regulated environment which provides for appropriate protection of consumer rights.
f) promote cross-border credit information sharing by facilitating greater harmonization of legislation and regulations governing credit reporting in the SADC region.

I. ADR Training

46. The legal framework should encourage adoption of Alternative Dispute Resolution (ADR) strategies that seek to resolve disputes "in-house" through adoption of policies on Customer Complaints Resolution.

47. The complaints procedure should include continuous and comprehensive training of employees on complaints resolution.

48. Main elements of the policy should be circulated to all clients and should be prominently displayed by credit bureaus in an area of direct interface with clients such as the reception area. For any such policy to be effective consumer training and awareness is important. Further, clients should be encouraged to engage the credit bureau before resorting to litigation.

Main message

a. Credit reports greatly reduce the time and cost of providing credit
b. Public credit registries and private credit reporting firms are not substitutes – they can complement one another
c. Maximize the completeness of credit histories; make data available to open user group (non-bank creditors)
d. Establish regulatory framework for consumer protection and educate consumers as to their rights.

J. Data Security

49. *Data security is fundamental:* Data security is crucial and data processes should include a data security review to be sure all data is safe from loss and secured against unauthorized access.

50. *Data Security Principles:* By specifying how the credit bureau collects, uses, discloses, and protects personal data of its customers, data security policies can help the credit bureau to identify who needs access to confidential data, how this data should be secured, and procedures for effectively deleting or destroying data once it is no longer needed by the bureau.