



REGULATORY AND SUPERVISORY FRAMEWORK FOR MICROFINANCE BANKS [MFBs] IN NIGERIA.

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LIST OF ACRONYMS

AIP	- Approval In Principle
BOFIA	- Bank and Other Financial Institutions Act
CAC	- Corporate Affairs Commission
CAMA	- Companies and Allied Matters Act
CBS	- Community Banks
CBN	- Central Bank of Nigeria
CRR	- Cash Reserve Requirements
CV	- Curriculum Vitae
KYC	- Know Your Customer
LGA	- Local Government Area
MFB	- Micro Finance Bank
MFIs	- Micro Finance Institutions
MIS	- Management Information System
NGO	- Non Governmental Organization
OFID	- Other Financial Institutions Department
PAR	- Portfolio at Risk



REGULATORY AND SUPERVISORY FRAMEWORK FOR MICROFINANCE BANKS [MFBs] IN NIGERIA.

1. INTRODUCTION

The growing awareness of the potential of microfinance in poverty reduction, economic growth and development coupled with the emergence of several highly successful and fast growing Micro Finance Institutions [MFIs], has effectively put the issue of microfinance on the political agenda of most developing countries. Consequently, the supervisory authorities have taken active measures to address the issue of microfinance through the development of an appropriate regulatory and supervisory framework based on the particular features and risks associated with this activity.

The challenge supervisors' face, which is sometimes complicated by a multitude of legal initiatives in this area, is how to accommodate or reasonably encourage microfinance within a framework of generally accepted norms and prudential standards for the financial services industry. In general, a framework that does not adequately address the features and risks of microfinance would not effectively serve these institutions or the people who depend upon them. Therefore, bank supervisors should ensure that the supervisory framework in place is such that would result in innovative, rapid and balance growth of the industry as well as consistent with accepted banking practices. The issue of savings/deposits is central to the regulation and supervision of microfinance. Supervisory authorities are supposed to ensure that the poor clients do not lose their savings in failing institutions.

A new challenge for developing an appropriate regulatory and supervisory framework for microfinance lies in the great diversity of institutions that offer microfinance services. A comprehensive framework significantly based on micro lending as an activity should, therefore, be

developed and made applicable to all supervised institutions that offer this service, regardless of whether they are licensed as a bank or new institutional form created specifically for microfinance. The regulation should be defined to include standards for portfolio classification, loan documentation, loan loss provisioning and write-offs for microfinance operations.

It is instructive to note that the characteristics of microfinance clients are distinct, the credit methodology different and, in many cases the ownership structure of the institutions is not the same as that typically found in conventional financial institutions. These and other factors give rise to a unique risk profile that needs to be addressed through the regulatory framework and supervisory practices. In this regard, a risk based supervision shall be implemented which would focus mainly on (a) governance and ownership structure (b) lending methodology (c) borrower characteristics (d) appropriate management information system (e) internal control mechanisms and procedures.

A simple and rational regulatory and supervisory framework which would achieve a balanced growth, promote transparency, control risks faced by the institutions engaged in microfinance, eliminate barriers and unnecessary requirements has therefore, been developed and would be implemented for the sector.

2. POWER TO REGULATE

These supervisory and regulatory guidelines are issued by the Central Bank of Nigeria [hereinafter referred to as CBN or the Bank] in exercise of the powers conferred on it by the provisions of Section 28 subsection (1) (b) of the CBN Act 24 of 1991 [as amended] and in pursuance of the provisions of Sections 56-60A of the Banks and Other Financial Institutions Act [BOFIA] 25 of 1991 [as amended]. The guidelines are to regulate microfinance activities and the establishment and operations of Micro-Finance Banks [MFBs] that seek to take savings/deposits from members of the public and engage in microfinance intermediation services for their clients in Nigeria.

For the purpose of clarity, the following terms and definitions shall be used in the applicable sections of these guidelines.

f. Micro Finance Bank

A Micro Finance Bank [MFB], unless otherwise stated, shall be construed to mean any company licensed to carry on the business of providing micro-finance services such as savings, loans, domestic fund transfers and other financial services that economically active poor, micro-enterprises and small and medium enterprises need to conduct or expand their businesses as defined by these guidelines.

g. Micro Finance Client

A client of MFB that generally possess the following characteristics shall qualify as micro finance client:

- i. Have a monthly income of not more than twice the monthly per capital income of Nigeria or minimum wage, whichever is higher.
- ii. Have a total productive assets [inclusive of those arising from loans but excluding the cost of land] of not more than five hundred thousand Naira [N500, 000.00] only
- iii. Is not a regular employee of any organization
- iv. Age between 18 and 60 years.

h. Poor Person

A poor person shall be defined as one who has meagre means of sustenance or livelihood and whose total income during a year is less than the minimum taxable limit set out in the law relating to income tax.

i. Micro- Enterprise

A micro-enterprise is a business that requires micro credit/loans to operate. The operations and management are often built around the sole owner or micro entrepreneur. The micro entrepreneur usually works alone or provides employment for few people mainly the immediate family members and others over time. It does not often require formal registration to start, but tend to operate as sole proprietorship. The management and accounting requirements are very simple and flexible. Generally, micro entrepreneurs work informally, without business licences or formal records of their activities or earnings. The scope of economic activities of micro-enterprises typically includes primary production and crafts, value added processing and distributive trades.

j. Microfinance Loan

A microfinance loan is a facility granted to an individual or a group of borrowers whose principal source of income is derived from business activities involving the production or sale of goods and services. The maximum principal amount shall not exceed N500, 000 or and as may be reviewed from time to time by the CBN. Generally, a microfinance loan is granted to the operators of micro-enterprises, such as peasant farmers, artisans, fishermen, women, senior citizens and non-salaried workers in the formal and informal sectors. The said loans are usually unsecured, but typically granted on the basis of the applicant's character and the combined cash flow of the business and household. Ordinarily, the tenure of microfinance loans is 180 days [6 months]. However, in the case of crops with longer gestation period, a maximum tenure of twelve [12] months shall be permitted. Microfinance loans may require joint and several guarantees of one or more persons. The repayment may be on a daily, weekly, bi-monthly or monthly basis in accordance with amortization schedule in the loan contract.

3. Permissible Activities

A MFB shall be allowed to engage in the provision of the following services to its clients:

- a) Acceptance of various types of deposits including savings, time, target and demand from individuals, groups and associations; except public sector deposits [government],
- b) provision of credit to its customers, including formal and informal self-help groups, individuals and associations;
- c) promotion and monitoring of loan usage among its customers by providing ancillary capacity building in areas such as record keeping and small business management;
- d) issuance of redeemable debentures to interested parties to raise funds from members of the public with approval of the CBN;
- e) collection of money or proceeds of banking instruments on behalf of its customers through correspondent banks;

- f) provision of payment services such as salary, gratuity, pension for the various tiers of government;
- g) provision of loan disbursement services for the delivery of credit programme of government, agencies, groups and individual for poverty alleviation on non-recourse basis;
- h) provision of ancillary banking services to their customers such as domestic remittance of funds and safe custody;
- i) maintenance and operation of various types of account with other banks in Nigeria;
- j) investment of surplus funds of the MFB in suitable instruments including placing such funds with correspondent banks and in Treasury Bills;
- k) pay and receive interests as may be agreed upon between them and their clients in accordance with existing guidelines;
- l) operation of micro leasing facilities, micro finance related hire-purchase and arrangement of consortium lending and supervise credit schemes to ensure access of micro finance customers to inputs for their economic activities;
- m) receiving of refinancing or other funds from CBN and other sources, private or public, on terms mutually acceptable to both the provider of the funds and the recipient MFBs;
- n) provision of micro finance related guarantees for their customers to enable them have greater access to credit and other resources;
- o) buying, selling and supplying industrial and agricultural inputs, livestock , machinery and industrial raw materials to poor persons on credit and to act as agent for any association for the sale of such goods or livestock;
- p) investment in shares or equity of any body corporate, the objective of which is to provide microfinance services to poor persons;

- q) encouragement of investment in cottage industries and income generating projects for poor persons as may be prescribed by the CBN
- r) provision of services and facilities to customers to hedge various risks relating to microfinance activities;
- s) provision of professional advice to poor persons regarding investments in small businesses; rendering managerial, marketing, technical and administrative advice to customers and assisting them in obtaining services in such fields;
- t) mobilize and provide financial and technical assistance and training to micro- enterprises
- u) provision of loans to microfinance clients for home improvement and consumer credits; and
- v) performance of non-banking functions that relate to micro finance related business development services such as co-operatives and group formation activities, rural industrialization and other support services needed by micro enterprises.

No MFB shall undertake any business other than those permitted as stated above or activities as may be prescribed by the Central Bank of Nigeria from time to time.

4. PROHIBITED ACTIVITIES

No MFB shall engage in the provision of the following financial services:

- a. acceptance of public sector [government] deposit except for the permissible activities [f] and [g],
- b. foreign exchange transactions,
- c. international commercial papers,
- d. international corporate finance,
- e. international electronic funds transfer,
- f. cheque clearing activities,
- g. dealing in Land for speculative purposes,
- h. real estate except for its use as office accommodation,

- i. allow any facility for speculative purposes; and
- j. enter into leasing, renting, and sale/purchase of any kind with its directors, officers, employees or persons who either individually or in concert with their family members and beneficiaries own five percent [5%] or more of the equity of the MFB, without the prior approval in writing of the Central Bank of Nigeria.

5. Ownership

Microfinance banks can be established by individuals, group of individuals, community development associations, private corporate entities and foreign investors. Significant ownership diversification shall be encouraged to enhance good corporate governance of licensed MFBs. Universal banks that intend to set up any category of the MFBs as subsidiaries shall be required to meet the prescribed prudential requirements and availability of free funds and if in the view of the regulatory authorities, have satisfied all the requirements stipulated in the guidelines.

6. LICENSING REQUIREMENTS

Any promoter(s) seeking a licence for a Micro Finance Bank (MFB) business in Nigeria shall apply in writing to the Governor of the Central Bank of Nigeria. There shall be two [2] categories of licences available for promoters [both local and foreign] of Micro Finance Banks based on geographical coverage as specified below.

i) Micro Finance Bank licensed to operate as a unit bank [a.k.a Community banks] shall operate and open branches within a specified local government area [LGA]. The minimum capital requirement shall be ₦20 million [twenty million naira] or such amount as may be prescribed by the CBN from time to time.

ii) Micro Finance Bank licensed to operate in a State and open branches within a specified state or Federal capital territory. The minimum capital requirement of ₦1.0 billion (one billion naira) only or such an amount as may be prescribed by the CBN from time to time.

iii) Such application shall be accompanied with the following:

- a. non-refundable application fee of ₦ 50,000.00 and ₦100, 000.00 for Local and State microfinance banks, respectively in bank drafts, payable to the Central Bank of Nigeria;
- b. deposit of the minimum capital requirement for the relevant category of MFB, which shall be in bank draft payable to the CBN. The capital thus deposited together with the accrued interest shall be released to the promoters on the grant of a licence;
- c. satisfactory, verifiable and acceptable evidence of payment by the proposed shareholders of the minimum capital requirement for the category of licence being applied for; including personal statement that capital does not originate from bank credit, any form of credit or questionable sources and any activity that relates to money laundering;
- d. certificate of capital importation issued by an authorized dealer [banks] in the case of foreign capital;
- e. a copy of detailed feasibility report disclosing relevant information that shall include:
 - (i) the objectives and aims of the proposed MFB;
 - (ii) the justification for the establishment of the MFB;
 - (iii) the services that the MFB intends to provide;
 - (iv) the branch expansion programme [if any] within the first five years;
 - (v) the proposed training programme for staff and management succession plan;
 - (vi) a five-year financial projection for the operation of the MFB, indicating its expected growth and profitability;
 - (vii) details of the assumptions upon which the financial projection has been made;
 - (viii) the organizational structure of the MFB, setting out in detail, the functions and responsibilities of the top management team;
 - (ix) the composition of the Board of Directors and the Curriculum vitae (CV) of each member including other directorships held [if any];

- (x) appropriate management information systems, internal controls and procedures including manuals of operations and
 - (xi) the conclusions based on the assumptions made in the feasibility report.
- f. a copy of the draft Memorandum and Articles of Association;
 - g. a letter of intent to subscribe to the shares of the proposed MFB, signed by each subscriber;
 - h. a copy of the list of promoters/proposed shareholders in tabular form, showing their business and residential addresses [not post office addresses] and the names and addresses of their bankers;
 - i. names and CVs of the proposed members of the Board of Directors. The CVs must be personally signed and dated;

No proposed MFB under this policy shall incorporate/register its name with the Corporate Affairs Commission [CAC] until a written approval-in principle [AIP] has been communicated to the promoters by the CBN, a copy of which shall be presented to the Corporate Affairs Commission.

In considering an application for a licence, the CBN shall satisfy itself that:

- (i) the promoters and the proposed Management team are “fit and proper” persons to invest in/manage the financial services industry in Nigeria by regulatory standards;
- (ii) the promoters have submitted the names and curriculum vitae of the top management team of the proposed MFB;
- (iii) the minimum paid-up capital/shareholders’ funds of the relevant category being applied for is acceptable and the source is verifiable and satisfactory to the CBN;
- (iv) the quality of the management of the proposed MFB is sound;
- (v) the earnings prospect of the company is realisable; and

- (vi) the objects of the company as disclosed in its Memorandum and Articles of Association agree with the services listed in the provisions of Section 3 of these guidelines.
- J The CBN shall before the issuance of approval – in –principle [AIP] arrange an appraisal interview for the promoters of the proposed MFB. The date and time for the interview shall be communicated to the promoters in writing.
- k If satisfied, the Governor may grant a licence to the MFB; where the grant of licence is declined, the reason(s) for refusal shall be communicated in writing to the applicant.
- l The CBN may at any time vary or revoke any conditions of a licence or impose additional conditions.
- m Where a licence is granted subject to some conditions, the MFB shall comply with those conditions to the satisfaction of the CBN within such period, as the CBN may deem appropriate in the circumstances. Any MFB that fails to comply with such conditions shall be guilty of an offence under BOFIA, 1991 [as amended].
- n All licensed MFBs shall be required to add Micro Finance Bank (MFB) Ltd after their names which shall be registered with the Corporate Affairs Commission in compliance with the Companies and Allied Matters Act (CAMA)

7. FINANCIAL REQUIREMENTS

The application and licensing fees which may be varied at the instance of the CBN shall be as follows:

	Unit MFB	State MFB
a. Non-refundable Application fee	₦ 50,000.00	₦ 100,000.00
b. Non-refundable Licensing fee	₦ 100,000.00	₦ 250,000.00
c. Change of Name fee	₦ 20,000.00	₦ 50,000.00

A MFB wishing to convert its licence status shall be required to pay the applicable non-refundable licensing fee.

8. DIRECTORS

- a. The maximum number of directors [including executive directors] on the Board of a MFB shall be seven [7], while the minimum shall be three [3]. To qualify for the position of a director in a MFB, it is hereby required that the person must not be a current employee of a bank or other financial institution, except where the MFB is promoted by a bank or other financial institution and the person is representing the interest of such institutions. In the circumstance, where a current employee of bank or other financial institution is proposed for the position of director, the consent of the employer must be given in writing to the CBN. No person shall serve as a director in more than two [2] institutions under the regulatory purview of the CBN.
- b. At least two [2] members of the board of directors other than the executive management shall be required to have banking or related industry experience.
- c. The appointment of new directors and management staff shall be approved by CBN.

9. MANAGEMENT REQUIREMENTS

The following minimum qualifications and experience are mandatory for officers who may occupy the key/top management positions in the MFB:

- a. Managing Director/Chief Executive - a recognized university degree or its equivalent and or professional qualification with at least 7 years post-qualification experience in banking or related industry.
- b. Departmental Head - a recognized university degree or its equivalent and or professional qualification with at least 5 years post-qualification experience in banking or related industry
- c. A person with any other qualifications or experience that may be considered adequate by the CBN may hold any of positions [a] and [b] within the organization.

10. CERTIFICATION PROCESS

In recognition of the peculiarities of microfinance services and the management of the MFB, it shall be required that the top management possesses the requisite certification on microfinance management from recognized certification institutions acceptable to the Central Bank of Nigeria. To fulfill this requirement, members of the top management team of MFB shall be required to submit evidence of certification. Members of executive management shall be required to possess certification on microfinance management not later than three (3) years after the take off of the certification programme. A transition period of twenty four [24] months shall be allowed for the take-off of this programme following the implementation of the microfinance policy. Failure to comply with the above condition shall be a ground for the removal of the affected officer.

11. CONDITIONS PRECEDENT TO THE COMMENCEMENT OF OPERATIONS

- a. The promoters of an MFB shall submit the following documents to the CBN before it is permitted to commence operations:
 - i. a copy of the shareholders' register in which the equity interest of each shareholder is properly reflected [together with the original for sighting];
 - ii. a copy of the share certificate issued to each shareholder;
 - iii. a certified true copy of Form C02 [Return of Allotments] filed with the Corporate Affairs Commission;
 - iv. a certified true copy of Form C07 [Particulars of Directors], and a written confirmation that the Board of Directors approved by the CBN has been installed;
 - v. a certified true copy of the Memorandum and Articles of Association approved by the CBN and filed with the Corporate Affairs Commission;
 - vi. the opening statement of affairs audited by an approved firm of accountants practising in Nigeria;
 - vii. a certified true copy of the certificate of incorporation of the company [together with the original for sighting purposes only];

- viii. a copy each of the letters of offer and acceptance of employment by management staff and a written confirmation that the Management team approved by the CBN has been put in place; and
 - ix. a letter of undertaking to comply with all the rules and regulations guiding the operations of MFBs.
- b. The MFB shall inform the CBN of the location and address of its Head Office in Nigeria and shall confirm that all infrastructures for take off are in place. In addition, the MFB shall show evidence that appropriate management information system, internal controls, and procedures including manuals of operations have been put in place.
 - c. The MFB shall be informed in writing by the CBN that it may commence business after physical inspection of its premises.
 - d. The MFB shall inform the CBN in writing of the date of commencement of business after the physical inspection of its premises.

12. SOURCES OF FUNDS

The sources of funds of an MFB shall consist of the following:

- a. shareholders' funds - paid-up share capital and reserves;
- b. deposits/savings of customers;
- c. debenture/qualifying medium to long term loans;
- d. grants/donations from individuals, organizations, national government, and international sources;
- e. fees and commissions; and
- f. interest income.

13. BOOKS OF ACCOUNTS

- (i) The Board of Directors of a MFB shall ensure that the institution keeps proper books of account with respect to all transactions at the principal administrative office and in all its branches in English language or any other language approved by the Federal Government of Nigeria.

- (ii) For the purpose of sub-section (i) of this section, proper books of account shall contain all information necessary to explain all its transaction and give a true and fair view of the state of affairs of the MFB and be presented in compliance with the accounting standards issued by the Nigerian Accounting Standards Board.
- (iii) Where the books of account are not properly kept, in the opinion of the CBN, the Bank shall apply the provision of section 24 (5) of BOFIA, 1991 as amended.
- (iv) If any person being a Director, Manager or officer of a MFB fails to take all reasonable steps to secure compliance with any of the provisions of this section, he or she shall be appropriately sanctioned in line with the provisions of these guidelines.

14 PORTFOLIO- AT- RISK [PAR]

- a. PAR is the outstanding principal amount of all loans that have at least one installment past due for one or more days. The amount includes the unpaid principal balance including the accrued interest. Under PAR, loans are considered past due if payment has fallen due and remained unpaid. Loan payments are applied first to any interest due, and then to any installment of principal that is due but unpaid, beginning with the earliest installment. The number of days of lateness is based on the due date of the earliest loan installment that has not been fully paid.
- b. It shall be required that PAR shall not exceed 2.5% at any given time for a MFB.
- c. Past Due Micro finance Loans: This is any loan that has missed one day repayment in accordance with the agreed repayment term in the loan contract. Such loans whether restructured or refinanced shall attract appropriate provision for loan loss. The past due micro finance loans shall remain in the account of the MFB until it is fully repaid or arrangements are formalized for its reactivation/renewal/restructuring or collection case has been filed in court.

d. Accrual of Interest earned.

No accrual of interest shall be allowed after the microfinance loan has become past due. All interest accrued and or booked shall be reversed and no accrual of interest shall be allowed after the microfinance has become past due as defined in [c].

e. Restructured Microfinance loans:

These represent microfinance loans that have been renegotiated or modified to either lengthen or postpone the original scheduled installment payments, or substantially alter the original terms of the loans. Restructured loans, which shall include refinanced loans [i.e. loans disbursed to enable repayment or part repayment of prior loans that was past due], shall be treated as non-performing and no interest income shall be accrued thereon.

No micro loan shall be restructured more than two times.

f. Writing off of microfinance loans as bad debts.

Microfinance loans that have been past due for 91 days or more and are fully provisioned may be written off accordingly.

15. RENDITION OF RETURNS

In compliance with the provisions of section 58[2] b of BOFIA, 1991 [as amended] the following quarterly returns shall be submitted by MFBs:

- a. Statement of Assets and Liabilities.
- b. Profit and Loss account.
- c. Schedule of Loans and Investments on sector basis (number and value)
- d. Schedule of liabilities (deposits) on maturity basis (number and value)
- e. Interest rate structure
- f. Schedule of balances held with banks.
- g. Returns on
 - i. borrowings from other MFBs, other financial institutions, individuals and non-financial institutions.

- ii. credits to other MFBs, other financial institutions, individuals/non-financial institutions, shareholders, affiliates, directors/management staff and others.
- iii. non-performing credits.
- iv. off balance sheet engagements.
- v. non-performing other assets. and
- vi. other items as may be specified by the CBN.

All quarterly returns must reach the Director of Other Financial Institutions Department (OFID) of the CBN, Lagos not later than 14 days after the end of each quarter. The Managing Director/Chief Executive Officer and the Chief Accountant [or equivalent] of the MFB shall sign and to every return made to the CBN a declaration of authenticity of its contents. The frequency of the returns may be reviewed from time to time by the CBN.

Universal banks currently engaging in microfinance services either as an activity or product shall be required to submit the returns on their micro finance activities separately in accordance with stipulations of these guidelines.

16. COMPLIANCE WITH ANTI-MONEY LAUNDERING ACT AND KYC CIRCULARS

All MFB shall be required to comply with Anti-money Laundering Act 1995 as amended and the principles and procedures of Know Your Customer [KYC] and relevant circulars as issued by the CBN from time to time.

17. PUBLICATION OF AUDITED FINANCIAL STATEMENTS

Every MFB shall submit its audited financial statements and the abridged version of the accounts to the Director of OFID for approval not later than four months after the end of the company's financial year. The Domestic Report on the Accounts from the External Auditors shall be forwarded to the Director, OFID not later than three months after the end of the accounting year. After approval by the Central Bank of Nigeria, the MFB shall be required to display an abridged version of its audited financial statements in its head office and all its branches. Every approved audited account shall disclose in detail the penalties paid as a

result of the contravention of BOFIA, 1991 [as amended] and any policy guidelines in force during the year in question and the auditor's report shall reflect such contraventions. Any MFB that fails to comply with the above requirements shall be liable to a fine not exceeding ₦20, 000.00 for each day during which the offence continues.

18. PENALTIES FOR LATE OR FALSE/INACCURATE RETURNS OR OTHER INFORMATION

- a. For lateness in submitting a return/furnishing any information required, the penalty shall be a fine of ₦20, 000.00 for each day during which such failure occurs. Persistent failure/refusal to render returns in the prescribed form shall be a ground for the revocation of an MFB's licence.
- b. Where the Bank considers it necessary, it may appoint a firm of qualified accountants to prepare proper books of account or render accurate returns, as the case may be, for the MFB concerned and the cost of preparing the account or rendering the returns shall be borne by the MFB.
- c. If any Director or Officer of a MFB fails to take all reasonable steps to ensure that proper books of accounts are kept with respect to all transactions by the company at its Head Office and/or at its branches, the CBN may impose on him a fine not exceeding ₦20, 000.00 and in addition shall be removed and black-listed. If any default in this respect is caused by the willful act of any Director or Officer of the MFB, the CBN may impose on him a fine not exceeding ₦1.0 million or cause the removal of such Director or Officer in order to protect the integrity of the financial system. In addition, the Bank may impose on the MFB such other penalties as are deemed appropriate.

19. PRUDENTIAL REQUIREMENTS

Every MFB shall comply with the following requirements:

- a. Compulsory investment in treasury bill

All MFBs shall be required to maintain not less than 5% of their deposit liabilities in Treasury Bills [TBs]

b. Liquidity Ratio

The operation of MFBs requires the maintenance of high level of liquid assets to meet frequent request for funds from clients and for field operations. All MFBs shall be required to maintain a minimum ratio of twenty percent [20%] of their deposit liabilities including 5% compulsory investment in the Treasury Bills in the liquid assets.

c. Capital Funds Adequacy

A MFB shall at all times maintain a minimum capital adequacy ratio as may be prescribed by the CBN from time to time. The capital adequacy ratio shall be measured as a percentage of the capital base of a MFB to its risk-weighted asset exposure in accordance with the provisions which the CBN shall prescribe.

The minimum Capital Adequacy Ratio [Capital/Risk Weighted Assets Ratio] for each Micro- Finance Institution shall be 10%. Furthermore, a MFB is expected to maintain a ratio of not less than 1:10 between its shareholders fund unimpaired by losses and net credits.

The CBN may require a MFB to maintain additional capital as it considers appropriate in respect of specific concentration of risks or market risks or connected lending.

When any of the above ratios fall below the prescribed level, the MFB shall be prohibited from any or all of the following until the required ratio is restored:

- i. grant credits and undertake further investment;
- ii. pay dividend to shareholders; and
- iii. borrow from the investing public.
- iv. open branch/cash centre

In addition, the MFB shall be required to submit within a specified period, a recapitalization plan acceptable to the CBN. Failure to comply with the above may constitute grounds for the revocation of the operating licence of the MFB or such other penalties as may be deemed

appropriate. MFB are enjoined to ensure that their shareholders' funds do NOT fall below the required minimum paid-up capital.

c. Fixed Assets/Long-term Investments and Branch Expansion

No MFB shall be allowed to finance any of the following other than from the share holders' funds, unimpaired by losses:

- i. acquisition of fixed assets;
- ii. equity investments and investments in long-term debentures;
and
- iii. branch expansion.

In consideration of a request for any or a combination of the above options, reference shall be made to the aggregate value of the listed items against the shareholders' funds, unimpaired by losses.

d. Maintenance of Capital Funds

MFBs are generally expected to pay less emphasis on collaterals in granting credits. The impact of delinquent risk assets, which may result in capital erosion, calls for stringent maintenance of capital funds.

Every MFB shall therefore maintain a reserve fund into which shall be transferred out of its net profits for each year before it declares any dividend and after it has made provision for any taxes, the following amounts:-

- (i) Where the amount of the MFB's reserve fund is less than 50 percent (50%) of its paid-up capital, an amount which shall not be less than 50 percent(50%) of the MFB's net profit for the year;
- (ii) Where the amount of the MFB's reserve fund is 50 percent (50%) or more, but less than 100 percent (100%) of its paid-up capital, an amount which shall not be less than 25 percent (25%) of the MFB's net profit for the year; or
- (iii) Where the amount of the MFB's reserve fund is equal to 100 percent(100%) or more of its paid up capital, an amount equal to 12.5percent(12.5%) of the MFB's net profit for the year.

A MFB shall not appropriate any sum or sums from the balance in its reserve fund unless prior approval in writing is obtained from the CBN for the purpose, which may be granted for such amount and subject to compliance with such conditions as the CBN may determine.

The CBN may, from time to time, vary the proportion of net profit transferable to Statutory Reserves.

No accretion shall be made to the reserve fund until:

- i. all preliminary and pre-operational expenses have been written off;
- ii. adequate provision has been made for loan loss/assets deterioration; and
- iii. all identifiable losses have been fully provided for.

e. Restrictions on Declaration of Dividend

A MFB shall not declare or pay a dividend on its shares until it has,

- (i) Completely written-off all its preliminary and pre-operational expenses;
- (ii) Made the required provisions for non-performing loans and other erosions in asset values;
- (iii) Satisfied the minimum capital adequacy ratio requirement and
- (iv) Met all matured obligations.

1. Where the payment of dividend would result in withdrawal of any part of the free reserves due to inadequacy of the profit for the year or where the statutory report of the auditors on the Annual Accounts of the bank is not satisfactory, the MFB may declare any dividend on its shares only after obtaining the prior approval of the CBN
2. Where a MFB declares or pays any dividend in contravention of this provision, every director and chief executive officer of the MFB shall be liable to pay to the CBN a penalty, the sum of which shall be determined by the CBN

f. Limit of Lending to a Single Borrower and Related Party

The maximum loan by MFB to any individual borrower or director, related borrowers shall not exceed one [1%] percent, while group borrower is restricted to a maximum of 5% of the MFB's shareholders' fund unimpaired by losses or as may be prescribed by the CBN from time to time.

In addition, aggregate insider-related lending shall not exceed 5% of the paid up capital of the MFB at any time. For this purpose, loans under staff scheme shall not apply, but shall be in accordance with the staff conditions of service.

Any contravention will attract a penalty of ₦1.0million on the MFB and a fine of ₦100, 000.00 on the director/manager who fails to comply.

g. Maximum Equity Investment Holding Ratio

The aggregate value of the equity participation of a MFB in all permissible enterprises shall NOT exceed 7.5% of its shareholders fund unimpaired by losses without prior approval in writing by the CBN.

h. Provision for Classified Assets

All performing risk assets formed by MFBs shall attract 1% general provision. Provision for non-performing risk assets and other assets shall be as stated hereunder.

Days at Risk [No of days missed payment]	Description	Provisioning Requirement or allowance for probable losses [%]
0	Performing	1%
1- 30 days	Pass and watch	5%
31-60 days	Substandard	20%
61-90 days	Doubtful	50%
91 or more days and /or restructured loans	Lost	100%

Each MFB shall review at least once every thirty days, its loans and advances and other investments and make appropriate provisions for loan losses or assets deterioration.

Every MFB must send to the OFID every month a schedule of loans/investments showing the provisions made for losses or deterioration in the quality of the loans/investments.

i. Contingent Items

The concept, use and treatment of Bankers Acceptances [BAs] and Commercial Papers [CPs] to banks and discount houses and other financial institutions shall apply to MFB.

j. Limit of Investment in Fixed Assets

The maximum amount, which a MFB can invest in fixed assets, is 20% of its shareholders' funds unimpaired by losses. Any contravention shall attract a penalty not exceeding ₦2million or suspension of the licence.

k. Revaluation of Fixed Assets

Prior approval of the CBN must be obtained by any MFB before the recognition of the revaluation surplus on fixed assets in its books, taking into consideration that:

- i. the basis of the underlying fixed assets valuations are stated and the valuation made by qualified professional valuers whose identity and qualifications are stated;
- ii. the difference between the market and the historic values of the eligible fixed assets being revalued is to be discounted by 55%;
- iii. the revaluation of fixed assets is applicable to own premises only; and
- iv. the revaluation of fixed assets (owned premises only) is permissible within a minimum period of 5 years after the date of the purchase of the asset or the last revaluation.

20 Special Prudential standards

Some regulations common in traditional banking shall be adjusted at the full discretion of the CBN from time to time, to accommodate the peculiarity of microfinance services as detailed in this section.

a) Unsecured Lending limits:

In accordance with the provisions of BOFIA section 20(2)(a), any unsecured advances or loans or credit facilities of an aggregate amount in excess of fifty thousand naira [N50,000.00] is not permitted. For the purpose of applying this regulation to MFB, group guarantees or third party guarantees of an individual acceptable to the MFB shall qualify as collateral for microfinance loans.

b) Loan documentation requirement:

Given the nature of microfinance loan sizes and customers, collateral registration, financial statements of borrowers or evidence that those businesses are formally registered shall not be required.

c) Restriction of Co-signers as Borrowers:

The restriction prohibiting a bank from lending to someone who has co-signed or other wise guaranteed a loan from the same bank shall not apply to Micro Finance Bank.

d) Reporting Requirements:

The reporting requirements for microfinance banks shall be simplified to minimize administrative costs to them.

e) Cash Reserve Requirements:

The mandatory cash reserve requirements [CRR] for banks shall not apply to an MFB, rather an MFB shall be required to have compulsory investment of 5% of its total deposit liabilities in the treasury bills which shall qualify as specified liquid asset in computation of its liquidity ratio.

21 ASSESSMENT OF SOUNDNESS

MFB rating is a standard measurement for the assessment of its performance in capital, asset quality, management, earnings, and liquidity (CAMEL), with weightings as follows:

<u>CAMEL FACTORS</u>	<u>WEIGHT</u>
Capital	30%
Asset quality	30%
Management	20%
Earnings	10%
Liquidity	10%

The factors that may affect rating are violations of the Legal Lending Limit and Judgment factors.

Judgmental factors may reduce bank rating to Unsound in the event of Internal disputes, intervention by third parties, window dressing, unsound banking Practices, financial difficulties, and other irregular banking practices. Rating is divided into four categories: sound, satisfactory, marginal and unsound.

22. REQUIREMENTS FOR INCREASE IN SHARE CAPITAL

All increases in share capital in any form shall be approved by the CBN. Application in respect of this shall be supported with the following:

- a. board resolution authorizing the increase;
- b. evidence of payment of stamp duty;
- c. Corporate Affairs Commission [CAC] registration of the increase;
- d. Form C02 showing the additional capital;
- e. share certificate issued to shareholders;
- f. photocopy of share register showing the entries of allotment,
- g. evidence of payment for the new allotment of shares by the shareholders [photocopies of cheques lodged should be attached]. No cash payment is allowed for significant acquisition i.e up to 5% of share in MFB;
- h. statements of accounts from banks reflecting the cheques lodged and cleared;
- i. vouchers showing evidence of internal transfer or payment for the right issues allotted;
- j. copies of letters to shareholders conveying allotment of shares; and
- k. any other information that may be required or stipulated by the CBN.

23. DISCLOSURE OF INTEREST BY DIRECTORS AND OFFICERS OF MFBs.

Every Director and Officer of a MFB, who has any personal interest, whether directly or indirectly, in an advance, loan or credit facility or proposed advance, loan or credit facility, vendor services from the MFBs in which he/she is serving, shall promptly declare the nature of his/her

interest in writing to the Board of Directors of the MFB and the declaration shall be circulated to all the directors.

Every Director or Officer of a MFB who holds any office or possesses any property whereby, whether directly or indirectly, duties or interests might be created in conflict with his duties or interest as a Director or Officer of the MFB, shall declare at a meeting of the Board of Directors of the MFB, the fact and the nature, character and extent of such interests. Any Director or Officer who contravenes either of these regulations shall be liable to a fine of ₦500, 000.00 or removal from office.

24. DISCLOSURE OF REQUIRED INFORMATION TO CREDIT REFERENCE BUREAU

Every MFB shall be required to supply information on all its credit clients to the Credit Bureau from time to time. In addition, all MFBs shall provide:

(a) details of non-performing loans or credit accommodations classified as doubtful or lost in its portfolio, where the amount owed is not in dispute, the customer has not made any satisfactory proposals for repayment following formal demand, and the customer has been given at least twenty-eight days' notice of the intention to disclose that information to the Credit Reference Bureau;

(b) information on its customers involved in financial malpractices including dud cheques.

(c) No information other than that referred to in the above subsection shall be divulged by any institution to the Credit Reference Bureau without customers' consent.

(d) Where (i) the credit reference bureau; or (ii) an institution, discloses to an institution or its officer, the Credit Reference Bureau or its officer, the information referred to in sub-section (a) and (b) in good faith, in the performance of their duties, no right of action shall accrue to or against the customer for breach of any duty of confidentiality.

(e) Any customer of an MFB has a right to know his credit status forwarded to Credit Reference Bureau.

25. OPENING/RELOCATION AND CLOSING OF BRANCHES

Prior approval of the CBN is required for the opening, relocation or closing of branches or cash centres. In the case of relocation, appropriate notice of intention to relocate principal place of business shall be given to the general public by the MFBs after the CBN's approval.

In contravention, the MFB shall be made to pay a fine not exceeding ₦ 200, 000.00 and also close or reopen the branch as the case may be and in addition, a fine of ₦ 20, 000.00 for each day during which the offence continues.

26. CHANGE OF NAME BY LICENSED MFBs.

The MFB shall be required to obtain CBN approval before effecting change of name as contained in its operational licence.

27. DISPLAY OF LICENCE

A copy of a MFB's licence shall be displayed in a conspicuous position at its Head Office as well as in the branches. In contravention, the MFB shall be penalized in line with Section 60[i] of the Bank and Other Financial Institutions Act [BOFIA] 1991 (as amended).

28. DISPLAY OF INTEREST RATES

Every MFB shall display on a daily basis in a conspicuous place at its Head Office and branches, its rates of interest. Interest rates shall be quoted on annual basis and not monthly. In contravention, the MFB shall be liable to a fine of ₦50, 000.00 and ₦5, 000.00 in addition, for every day during which the offence continues or such other penalties deemed appropriate.

29. INTERNAL CONTROLS

Every MFB shall have an Internal Audit Unit, which shall ensure that the operations of the company conform to the law as well as to its internal

rules and regulations. The Internal Auditor shall forward his report directly to the Board of Directors to strengthen corporate governance in the MFB. Every fraud or attempted fraud must be promptly reported to the Director of OFID by the head of the unit. Also, a quarterly report on frauds and forgeries affecting the company and any default in meeting any obligation to lenders or investors shall be submitted to the Director, OFID. Where no frauds/forgeries and defaults occurred during the quarter, a nil return shall be forwarded. The report shall be made along with the quarterly returns on assets and liabilities. Failure to comply with this requirement shall attract a fine of ₦50, 000.00 per quarter.

30. APPOINTMENT OF CHIEF EXECUTIVE AND PRINCIPAL OFFICER

The appointment or replacement of the Chief Executive Officer or any of the Principal Officers of any MFB shall be cleared with the CBN before such appointments are made. Where the turnover of principal and senior officers is considered to be unduly high or where the reason for leaving by an officer suggests an attempt to cover up a fraud or other illegal activity, or punish the officer for attempting to prevent illegal activities, the CBN shall cause an investigation to be conducted into the matter and other affairs of the MFB as may be considered necessary. The report of such investigation or special examination shall determine the penalty to be imposed on the MFB concerned.

31. APPOINTMENT OF EXTERNAL AUDITOR

Every MFB shall appoint an approved external auditor, whose duties shall be to make to the shareholders a report on the annual financial statements of the company and every such report shall contain true and fair statements as to the matters and such other information as may be prescribed from time to time by the CBN.

The approved auditor shall satisfy the following requirements:

- a. a member of a recognized professional accountancy body in Nigeria;
- b. continues in professional practice as accountant and auditor in Nigeria;
- c. no person shall be appointed as the auditor of a MFB if:

- i. He has interest in that MFB other than as a depositor
 - ii. He is a director, officer or agent of such institution
 - iii. It is a firm in which a director of the MFB has interest as partner or director
 - iv. He is indebted to the MFB.
- d. any auditor who is subsequently affected by Section 24(C) above shall immediately cease to continue as the auditor of the MFB.
- e. an approved auditor in the course of his duties shall immediately report to the CBN formally if it is certified that:
- i. there has been a contravention of BOFIA, 1991 (as amended) or that an offence under any other law, guidelines, circulars, etc has been committed by the MFB or any of its officers; or
 - ii. losses have been incurred by the MFB which substantially reduce its capital funds; or
 - iii. any irregularity which jeopardizes the interest of depositors or creditors of the MFB or any other irregularity has occurred, or
 - iv. he is unable to confirm that the claims of the depositors or creditors are covered by the assets of the MFB.
- f. The approved auditor shall also forward to the CBN two (2) copies of the domestic report on the activities of the MFB not later than three (3) months after the end of the financial year of such MFB.
- g. The approved auditor shall have the right of access at all times to all books, accounts and vouchers of the MFB and shall be entitled to require from directors, managers and officers of the MFB all information and explanation he considers necessary for the performance of his audit.
- h. If any MFB fails to appoint or fill a vacancy for an approved auditor, the CBN shall appoint a suitable person for that purpose

and shall fix the remuneration to be paid by the MFB to such auditor.

- i. The appointment of an approved auditor shall not be determined without a prior written approval of the CBN.
- j. Any approved auditor who acts in contravention of the foregoing requirements or fails deliberately or negligently to comply with the requirements of this section shall be liable to a fine of a maximum of ₦50,000.00 or a determination of his status as an approved auditor to all financial institutions under the supervisory purview of the CBN.
- k. No Audit Firm shall serve the same institution as External Auditor for a continuous period exceeding three [3] years in order to enhance transparency in reporting.

32. SCHEME OF ARRANGEMENT

No MFB shall enter into any “Scheme of Arrangement” with its creditors/investors without obtaining the prior approval of the CBN. Any MFB that is unable to meet its obligations to its creditors or investors shall submit its proposals to restore liquidity or viability and for eventual settlement of its outstanding obligations to the Director of OFID for consideration and approval. Failure to comply with this will attract a penalty of ₦2,500.00 for each day during which the contravention exists.

33. RESTRUCTURING AND REORGANIZATION

Except with the prior consent of the Governor of the CBN, no MFB shall enter into an agreement or arrangement:

- a. which results in a change in the control of the MFB;
- b. for the sale, disposal or transfer of the whole or any part of the business of the MFB;
- c. for the amalgamation or merger of the MFB with any other company;
- d. for the restructuring of the MFB ; and
- e. to employ a management agent or to transfer its business to any such agent.

34. TRANSFORMATION OF OTHER INSTITUTIONS TO MICRO FINANCE BANK (MFB)

Any financial institution under the purview of the Central Bank of Nigeria that intends to transform to a Micro Finance Bank shall apply to the Bank and ensure that the licensing requirements for MFB are met.

a) Universal banks:

A universal bank could operate a microfinance bank by setting up a subsidiary MFB and obtaining a licence for it. Universal banks currently engaging in microfinance services either as an activity or product and do not wish to set up a subsidiary shall be required to set up a department/unit for such services and shall be subjected to the provisions of the MFB regulatory and supervisory guidelines. The department /unit shall be headed by a staff of not less than a Deputy General Manager or its equivalent for that purpose. Due to the peculiarity of microfinance practice and the nature of assets formed, the micro finance department of such a bank shall be required to have the following:

- I. Management team,
- II. Internal Control and Procedure, and Manuals of Operations specifically designed for microfinance.
- III. Management Information System [MIS] and loan tracking mechanism.
- IV. Dedicated unit at branch level that is equipped for deposit mobilization and credit monitoring.
- V. reporting format and policy for income recognition for MFBs- i.e loan loss provision.
- VI. Management that have completed the Certification Programme and any other condition that the CBN may require from time to time.

Any Universal bank that engages in micro finance services as an activity or product shall be required to submit separate quarterly returns of its micro finance portfolio aside from its other lending activities.

b) Community banks:

All licensed community banks prior to the approval of this policy shall transform to Unit microfinance banks on meeting the prescribed new

capital and other conversion requirements within a period of 24 months from the date of approval of this policy. Any community bank that fails to meet the new capital requirement within the stipulated period shall cease to operate as a community bank. A community bank can apply to convert to a microfinance bank licensed to operate in a state if it meets the capital and other conversion requirements.

Specifically, Community Banks [CBs] wishing to transform to MFBs shall meet the following requirements:

- (i) The minimum shareholders' funds must be raised to a minimum of N20million for LGA coverage, while that of State wide coverage shall be N1.0 billion.
- (ii) Upgrade its Management team, Internal Control, Management Information System [MIS] and Procedure and Manuals of Operations.
- (iii) May wish to have a branded name not limited to the catchment's area of its original location.
- (iv) Meet criteria for branch network when it applies.
- (v) Adopt the reporting format and policy for income recognition for MFBs- i.e loan loss provision.
- (vi) Board and Management to undergo Certification Programme.
- (vii) Board and Management re-orientation on commercial Micro finance vision.

c) Non Governmental Organization (NGOs)-MFIs

A transforming NGO-MFI shall be required to provide an Institutional Assessment by a rating agency with specialization in micro financing and a certified statement of affairs by a firm of chartered accountants acceptable to the CBN. The institutional assessment shall include the NGO financial position, governance structure, human resources, risk management policy, control procedures, accounting and management information systems. The application for conversion to MFB shall be supported by:

- I. Board resolution approving transformation and stating the objectives
- II. Detailed feasibility report including a business plan specifying what the MFB plans to achieve in the next five years

- III. Detailed CVs of the proposed board members of the MFB and commitment letters to serve as board member and subscribed capital, if any.
- IV. Draft Memorandum and Articles of Association
- V. Proposed name of the MFB
- VI. Details of assets & liabilities to transfer to the MFB- the transfer shall be admissible at the value assessed/ determined by the audit/consulting team during institutional assessment phase.
- VII. Payment of the MFB application fee as specified in this guidelines

The institution shall be required to submit separate quarterly returns of its micro finance portfolio aside from its other lending activities.

In consideration of meeting the minimum capital requirement/ shareholders' funds, an existing institution shall be exempted from depositing the paid-up capital requirement (as the case may be) with the Central Bank of Nigeria. Its capital shall however be subject to verification by the CBN for confirmation.

35. Collaboration to regulate deposit/savings mobilizing Institutions

To prevent regulatory arbitrage at the lower end of the financial market, the CBN shall collaborate with other relevant agencies of the government to supervise the activities of financial cooperative and NGOs that have significant operations due to their micro savings/deposit taking activities from their members. Any of these Institutions that attains a total assets of twenty million [N20 million] naira and or total membership/clients of two thousand [2000] shall be required to transform to relevant category of MFB subject to the licensing requirements.

Collaboration between the CBN, CAC and relevant government agencies shall be promoted to reduce arbitrage in the practice of microfinance.

36. CONDITIONS FOR GRANT OF APPROVAL-IN-PRINCIPLE

The Central Bank of Nigeria, on receipt of an application, which is complete in all respect, shall process the application and if satisfied with

the overall quality of the proposal, shall grant Approval-in-Principle for establishing the MFB within three[3] month of receipt of the application.

37. CONDITIONS FOR FINAL LICENCE AND COMMENCEMENT OF BUSINESS

A proposed MFB with Approval-in-principle shall be granted a final operating licence after satisfying the conditions stated in section 6 of this guideline. Before being granted approval to commence operation, a newly licensed MFB shall be required to comply with conditions precedent to the commencement of operations as contained in section 7 of this guideline.

38. CONDITIONS FOR REVOCATION OF LICENCE

The grounds for revoking a licence granted to an MFB may be any or all of the following:

- a. submission of false information/data during and/or after the processing of the application for licence;
- b. the use of proxies or disguised names to obtain a licence of MFB;
- c. engaging in functions/activities outside the permissible scope of its licence as specified in Section 1 of these guidelines;
- d. persistent failure to comply with request for information/data in the form required/specified by CBN;
- e. engaging in activities prejudicial to the Nigerian economy;
- f. failure to redeem matured obligations to customers;
- g. unauthorized shop closure;
- h. failure to comply with any directive issued by CBN;
- i. any other act[s] which in the opinion of CBN constitute[s] a violation or a serious default;
- j. Engage in prohibited activities as listed in these guidelines and
- k. such other conditions that are applicable to banks and other financial institution that constitute a ground for revocation .under Banks and Other Financial Institutions Act [BOFIA] 1991. [as amended].

39. EXIT CONDITIONS

The condition for exit of a licensed MFB shall be as prescribed by the relevant sections of the Banks and Other Financial Institutions Act [BOFIA] of 1991[as amended] as applicable to deposit taking financial institutions and the Companies and Allied Matters Act [CAMA] 1990

40. GENERAL

The list of valid licences shall be published by the CBN from time to time.

CBN, ABUJA,
December 2005