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Diagnostic Review of Consumer Protection and Financial Literacy

Volume II

Comparison with Good Practices

THE WORLD BANK

Islamic Republic of Pakistan

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Comparison with Good Practices

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Abbreviations and Acronyms

ACMFD	Agricultural Credit and Microfinance Department
AMC	Asset Management Companies
AML/CFT	Anti-Money Laundering/Combating the Financing of Terrorism
BCO	Banking Companies Ordinance
BID	Banking Inspection Department
BPD	Banking Policy Department
BPRD	Banking Policy and Regulation Department
BSP	Banking Surveillance Department
CCP	Competition Commission of Pakistan
CDA	Central Depository Act
CDS	Central Depository System
CIB	Credit Information Bureau
CIS	Collective Investment Schemes
CIU	Collective Investment Undertaking
CP	Consumer Protection
CPD	Consumer Protection Department
CPFL	Consumer Protection and Finance Literacy
CRR	Cash Reserve Requirements
DFI	Development Finance Institutions
DFID	Department for International Development
DPS	Deposit Protection Scheme
eCIB	Electronic Credit Information Bureau
EFT	Electronic Fund Transfer
FATF	Financial Action Task Force
FIA	Federal Investigation Agency
FSA	Financial Sector Assessment
FSAP	Financial Sector Assessment Program
GOP	Government of Pakistan
IAP	Insurance Association of Pakistan
ICAP	Institute of Chartered Accountants of Pakistan
ICM	Institute of Capital Markets
ICMAP	Institute of Cost and Management Accountants of Pakistan
IOSCO	International Organization of Securities Commissions
IPO	Initial Public Offerings
KFS	Key Facts Statement
KPK	Khyber Pakhtunkhwa
KYC/CDD	Know Your Customer/Customer Due Diligence
LEA	Law Enforcement Agencies
MCGF	Microfinance Credit Guarantee Facility
MFB	Microfinance Banks
MFCG	Microfinance Consultative Group
MFI	Microfinance Institutions
MOU	Memorandum of Understanding
MSP	Microfinance Service Provider
MUFAP	Mutual Fund Association of Pakistan
NAB	National Accountability Bureau

NCC	National Clearing Company
NCCPL	National Clearing Corporation of Pakistan Limited
NFLP	Nationwide Financial Literacy Programme
NGO	Non-Government Organization
NICL	National Insurance Company Limited
OBM	Office of the Banking Mohtasib
OGCC	Operational Guidelines for Credit Cards
PBA	Pakistan Banks' Association
PKR	Pakistani Rupee
PLI	Postal Life Insurance
PLS	Profit and Loss Sharing
PMN	Pakistan Microfinance Network
PPAF	Pakistan Poverty Alleviation Fund
PRCF	Prudential Regulations for Consumer Financing
PRISM	Program for Increasing Sustainable Microfinance
PRCL	Pakistan Reinsurance Company Limited
PRMFB	Prudential Regulations for Microfinance Banks
RSP	Rural Support Programs
SAOF	Standardized Account Opening Form
SBP	State Bank of Pakistan
SECP	Securities & Exchange Commission of Pakistan
SI	Securities Intermediaries
SLIC	State Life Insurance Corporation
SLR	Statutory Liquidity Requirements
SRO	Self-Regulatory Organizations

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1. Banking Sector: Good Practices

SECTION A	CONSUMER PROTECTION INSTITUTIONS
Good Practice A.1.	***Consumer Protection Regime*** **The law should provide clear consumer protection rules regarding banking products and services, and all institutional arrangements should be in place to ensure the thorough, objective, timely, and fair implementation and enforcement of all such rules.** **a. Specific statutory provisions should create an effective regime for the protection of a consumer of any banking product or service.** **b. A general consumer agency, a financial supervisory agency, or a specialized financial consumer agency should be responsible for implementing, overseeing, and enforcing consumer protection regarding banking products and services, as well as for collecting and analyzing data (including inquiries, complaints, and disputes).** **c. The designated agency should be funded adequately to enable it to carry out its mandates efficiently and effectively.** **d. The work of the designated agency should be carried out with transparency, accountability, and integrity.** **e. There should be coordination and cooperation between the various institutions mandated to implement, oversee, and enforce consumer protection and financial system regulation and supervision.** **f. The law should also provide for, or at least not prohibit, a role for the private sector, including voluntary consumer organizations and self-regulatory organizations, in respect of consumer protection regarding banking products and services.**
Description	The laws and regulations of Pakistan do not yet provide clear consumer protection rules regarding any financial products and services, including those of banks. An effective regime for the protection of consumers seeking or acquiring banking products or services remains to be created. The Constitution of Pakistan refers to a Federal Legislative List. This list defines the distribution of legislative powers between the federation and provinces. The federation has the power to regulate the State Bank of Pakistan (SBP) and banking, that is, the conduct of banking business by corporations other than corporations owned or controlled by a province and carrying on business only within that province. However, general consumer protection is deemed to be a provincial matter. There are provincial Consumer Protection Acts in place[1] in all provinces except Sindh and the Federal Capital Territory. Although general in their coverage, they do ostensibly cover "services," which includes financial services. However, with the exception of the province of Punjab, these laws have not become fully operational or have lapsed.

[1] See, for example, the Punjab Consumer Protection Act, 2005.

	The provincial laws focus primarily on goods and manufactured materials, but also cover services. Under Pakistan's legal system, specialized laws are deemed to have precedence over general laws, so most observers believe that the federal laws governing banking and other financial services that include provisions for protection of the public and investors would take precedence over the more general provincial consumer protection laws. SBP derives its powers principally from SBP Act, 1956, and the Banking Companies Ordinance (BCO), 1962. Neither law gives SBP an explicit consumer protection mandate, but they do provide broad powers to SBP to, among other things, give directions, where it is satisfied that it is "(a) in the public interest; or (b) to prevent the affairs of any banking company being conducted in a manner detrimental to the interests of the depositors or in a manner prejudicial to the interests of the banking company; or (c) to secure the proper management of any banking company generally." Banks are legally bound to comply with such directions. SBP's powers and the binding nature of its directions on regulated entities have been demonstrated in practice and upheld by the Supreme Court. SBP has used these powers extensively to issue secondary legislation, rules, regulations, and other directives to banks on consumer protection matters in recent years. Recent legislation prompted by the rapid expansion of electronic banking has explicitly included clauses related to consumer protection, to avoid any ambiguity with regard to new products, services, and terminologies. Accordingly, different sections of the Payment Systems and Electronic Fund Transfers Act, 2007, contain details about the Requirement of Notice (Section 29) for ATM Fees, Terms & Conditions of Transfers (Section 30), Availability of Documentation & Proof (Section 32), Issuance of Periodic Statements (Section 33), Consumer's Liability in Case of Electronic Fund Transfers and Burden of Proof (Section 41), etc. The law itself and the quoted Sections provide further clarity and coverage to consumers. The following are the principal laws and regulations governing consumer protection in the banking sector: 1. State Bank of Pakistan Act, 1956 (SBP Act) 2. Banking Companies Ordinance (BCO), 1962, and associated regulations 3. Provincial consumer protection laws; notably the Punjab Consumer Protection Act, 2005 4. Competition Ordinance, 2007 5. Payments and Electronic Funds Transfers Act, 2007 6. Banks (Nationalization) Act, 1974 7. Various regulations, circulars, guidelines, and operational guidelines issued by SBP, including but not limited to the following:

	• Prudential regulations for consumer financing (PRCF) (updated June 2011), which establishes rules for various types of consumer loans, including credit card debt, housing loans, and auto loans, and requires banks to limit customer exposure by income and ability to service the loan. • Branchless Banking Guidelines, 2007 • Banking Policy Department (BPD) Guidelines 17, 2004, on Dealing with Customer Complaints • BPRD Circular 01, 2012, on Minimum Return on Savings Deposits • Consumer Protection Department (CPD) Circular 02, 2012, on Sale of Third Party Products by Banks • Banking Policy and Regulations Department (BPRD) Circular No. 23, 2003, on service charges on deposit accounts • BPD Circular No. 30, 2005, on basic bank accounts • BPRD Circular No. 7, 2011, on Service Charges on Profit and Loss Sharing (PLS) Deposit Accounts • BPRD Circular No. 12, 2011, which prohibits charging for cash handling/deposit services at counters • BPD Circular Letter No. 21, 2004, and BPD Circular No. 7, 2006, on unclaimed deposits • BPD Circular No. 7, 2006, on statement of accounts to PLS/current account holders and basic bank account holders • Operational Guidelines for Credit Card Business in Pakistan The two main entities responsible for implementing, overseeing, and enforcing consumer protection with respect to banking products and services are SBP (notably but not exclusively the Consumer Protection Department) and the Office of the Banking Mohtasib (OBM). These two entities also have responsibility for collecting and analyzing data (including inquiries, complaints, and disputes). Both institutions are adequately funded, and carry out their work with transparency, accountability, and integrity. SBP monitors consumer protection practices on an ongoing basis, and also receives consumer complaints directly from the public, occasionally leading to issuance of further clarifications of regulations in force and standards expected of the financial sector. SBP has extensive powers to give directions and impose monetary/restrictive penalties for violations. Within SBP, various departments are engaged in different aspects pertaining to consumer protection and financial literacy (CPFL). These include the Consumer Protection Department; the Banking Policy and Regulations Department, which develops and generates new rules and regulations, including in the CPFL; the Agricultural and Microfinance Department (AMD) of SBP, which deals with some policy issues pertaining to microfinance banks (MFBs), including in the area of the CPFL; and the Banking Inspection Department (BID), which conducts annual onsite inspections covering both prudential and market conduct

	issues. The Office of the Banking Mohtasib (OBM), or banking ombudsman, is an independent statutory body established by law to resolve disputes between consumers and banks. It is the first authority where a consumer, if not satisfied with a bank's decision, can lodge a complaint. It also collects, analyzes, and publishes data on consumer protection inquiries and disputes. The services performed by the ombudsman are free of charge. As is the case in some other countries, banks share the costs of the institution, with the cost to each bank determined by the central bank. The Competition Commission of Pakistan (CCP) is also involved in consumer protection. It is an independent quasi-regulatory, quasi-judicial body responsible for ensuring healthy competition among companies for the benefit of the economy. The CCP was established under the Competition Ordinance, 2007. The major aim of this ordinance was to provide a legal framework to create a business environment based on healthy competition for improving economic efficiency, developing competitiveness, and protecting consumers from anti-competitive practices. It has the legal power to, among other things, initiate proceedings, make orders, and impose penalties in cases of contravention of the Competition Ordinance. It has, from time to time, initiated investigations and issued directives involving anti-competitive practices by banks. There is regular, albeit informal, coordination and cooperation between SBP and OBM. There are no legal restrictions on the creation of voluntary consumer organizations; however, very few consumer protection nongovernmental organizations (NGOs) are active in the area of consumer financing.

Recommendation	The legal framework for financial consumer protection would benefit from strengthening and clarification, along with consistent enforcement of existing provisions. There are several ways to create an effective regime for the protection of consumers of banking products or services. One way would be to introduce a Consumer Financial Protection Act at the federal level in accordance with international good practices, which would legislate on a range of issues, including transparency, confidentiality, availability of statements, account servicing, protection against unfair contracts and lending practices, and so forth. This would have the advantage of consolidating the body of knowledge, case law, and best practices into a single piece of law. Another way would be to amend the BCO by introducing a new section specific to protection of consumers of financial services. However, given the very long delays involved in passing or amending financial legislation in Pakistan, SBP has opted in the interim to use its broad banking sector regulatory powers to issue relevant regulations, directives, and circulars in the area of consumer protection. Although not optimal, SBP has used its powers in this area effectively. Since the legal, regulatory, and institutional frameworks remain fragmented, a high-level consensus should be sought among SBP, Ombudsman of Pakistan, Competition Commission, Provincial Consumer Councils, and others, that SBP plays the primary role in regulating matters of consumer protection for licensed financial institutions under its jurisdiction. Procedural matters also need to be clarified. For example, consumers often complain directly to SBP rather than to the OBM because they are not fully aware of the complaints process. The complaints process should be in the hands of the OBM, which should regularly inform SBP on current issues in consumer financing and should have the right to give its own recommendations regarding the regulations that concern consumer financing. There should be a Memorandum of Understanding (MOU) between SBP and the ombudsman. The MOU should clearly define the rights and duties of the institutions, manner of communication, sharing of information, and oversight and enforcement of consumer protection provisions. SBP should establish an ongoing dialog with relevant NGOs and volunteer associations that are promoting consumer protection, and consult with these organizations regarding draft regulations on consumer protection. Their role should be recognized, in order to provide them with legitimacy and enable them to obtain funding and gather resources.
Good Practice A.2	***Code of Conduct for Banks*** **a. There should be a principles-based code of conduct for banks that is devised by all banks or the banking association in consultation with the financial supervisory agency and consumer associations, if possible. Monitored by a statutory agency or an effective self-regulatory agency, this code should be formally adhered to by all sector-specific institutions.**

	b. If a principles-based code of conduct exists, it should be publicized and disseminated to the general public. **c. The principles-based code should be augmented by voluntary codes of conduct for banks on such matters as facilitating the easy switching of consumers' current accounts and establishing a common terminology in the banking industry for the description of banks' charges, services, and products.** **d. Every such voluntary code should likewise be publicized and disseminated.**
Description	Currently there is no code of conduct for banks. Pakistan Banks' Association (PBA), which represents the Pakistan banking industry, was established in 1953, with a view to coordinate the efforts of the banking industry and to share a common vision of progress and development with its members. PBA membership is institutionalized and is available only to banks operating in Pakistan. The 46 current members are categorized into six groups (one of these groups is under formation). SBP, in its 10-year strategy, has plans to encourage the PBA to adopt a Banking Code of Ethics, which will be used as a basis for committing all banks to fairness, disclosure, and proper ethical standards. Moreover, individual banks do not appear to have developed their own codes of conduct. While most banks interviewed indicated they had internal codes of ethics, these appear to be limited to staff conduct, and are not disseminated to the public. The mission was unable to obtain a copy of any of these codes of ethics.
Recommendation	Pakistan Banks' Association (PBA) should adopt a code of conduct for banks. The code should be a principles-based, statutory Code of Conduct for banks devised in consultation with SBP. It should be widely publicized and disseminated to the general public. The performance of the banks in accordance with the requirements of the code would then need to be monitored by an appropriate body, which could be SBP or OBM, for example. Good examples of codes of banking practices that have been adopted and enforced include those of Australia, Canada, New Zealand, the United Kingdom, Hong Kong, and South Africa. These codes are principles-based and their compliance is monitored by the regulatory authority, as in the case of Hong Kong, or subject to the jurisdiction of the ombudsman, as in the case of South Africa and Australia. The principles-based code should be complemented by voluntary codes of conduct for banks on such matters as facilitating the easy switching of consumers' current accounts and establishing a common terminology in the industry for the description of banks' charges, services, and products. All such voluntary codes should also be widely publicized and disseminated.

Good Practice A.3	***Appropriate Allocation between Prudential Supervision and Consumer Protection*** **Whether prudential supervision of banks and consumer protection regarding banking products and services are the responsibility of one organization or two institutions, the allocation of resources to these functions should be adequate to enable their effective implementation.**
Description	SBP has established a Consumer Protection Department that is entrusted with the responsibility to redress the grievances of aggrieved financial consumers. The CPD works independently, duly supported by other supervisory departments in conducting consumer protection functions. The CPD director independently manages the department and reports to the same executive director as the Banking Policy and Regulation Department, which establishes rules and regulations. SBP's Inspection Department verifies compliance with both prudential and consumer protection rules, regulations, and other directives during annual onsite inspections at banks. The executive directors of Banking Policy and Banking Supervision report to the Deputy Governor, Banking. SBP allocates adequate resources to effectively oversee both prudential and consumer protection matters.
Recommendation	The allocation of resources to these functions is adequate to enable their effective implementation. However, the team is of the view that the CPFL framework would benefit from clearer delineation of the internal roles and responsibilities of various departments involved with the CPD. Moreover, the channels through which the various departments exchange information on a regular basis and establish priorities should be formalized.
Good Practice A.4	***Other Institutional Arrangements*** **a. The judicial system should ensure that the ultimate resolution of any dispute regarding a consumer protection matter regarding a banking product or service is affordable, timely, and professionally delivered.** **b. The media and consumer associations should play an active role in promoting banking consumer protection.**
Description	The judicial system in Pakistan does not currently ensure affordable, timely, and professional resolution of consumer protection disputes. As noted earlier, general consumer protection laws in Pakistan are provincial. Consumer protection laws were approved for the Islamabad Federal Capital Territory in 1995, Khyber Pakhtunkhwa (KPK) Province in 1997, Baluchistan Province in 2003, and Punjab Province in 2005, and they are pending for Sindh Province. The provincial consumer protection laws call for the creation of consumer councils and courts to deal with dispute resolution relating to

	consumer protection cases, but these are fully operational only in Punjab. The consumer courts must adjudicate cases within 60 days, which represents a major improvement over the timelines in the general court system, where final adjudication of cases can take several years. Punjab has established consumer councils and courts under The Punjab Consumer Protection Act 2005, and reports that it has dealt with some 700 cases involving financial services. Further, in terms of Section 5 (1) of the Financial Institutions (Recovery of Finances) Ordinance, 2001, the federal government has established Banking Courts throughout Pakistan to ensure quick recovery of bank loans from defaulters, but these cannot be used for consumer grievances. Outside of the Punjab Consumer Courts, court proceedings are very slow, given the huge backlog of pending cases within the judicial system. As a consequence, financial consumers' complaints and grievances are generally resolved or settled out of court, by the banks themselves, by the banking ombudsman or by the CPD at SBP. Neither the media nor NGOs have traditionally played a significant role in fostering consumer protection in banking, and SBP has not engaged actively with either group in this area. That said, there are some indications of increased media coverage of perceived unfair practices or unsatisfactory service levels. Such issues, though generally localized, are covered as if they were pervasive. Financial institutions are keenly aware of the reputational risk, which in turn has encouraged banks to adopt a more proactive approach to consumer protection and dispute resolution.
Recommendation	The judiciary (courts) should be an effective final arbiter of consumer disputes, and should be recognized as capable of rendering a final and binding decision in a professional, timely, and cost-effective manner. This is not currently the case in Pakistan. Judicial reform is a lengthy process, and falls outside of the scope of this exercise. However, the establishment of provincial consumer courts in provinces other than Punjab would be a positive step, because they have specialized knowledge and must observe strict timelines for adjudication of disputes. SBP or the Government of Pakistan (GoP) might also wish to consider organizing seminars, workshops, and conferences for judges and the media, covering current issues in consumer protection. The regulator can encourage responsible media coverage and NGO focus by establishing an ongoing dialog with both groups.
Good Practice A.5	***Licensing*** **All banking institutions that provide financial services to consumers should be subject to a licensing and regulatory regime to ensure their financial safety and soundness and effective delivery of financial services.**

Description	All banking companies must obtain a license from SBP before commencing operations and are bound by all the directives, advice, guidelines, and regulations of the regulator. Under Section 27 of the BCO, before granting a banking license, SBP must be satisfied that (i) the company is in or will be in a position to pay its depositors and (ii) the affairs of the company are not being or are not likely to be conducted in a manner detrimental to the interest of depositors. The consent of the home country supervisor is obtained when considering the licensing of a foreign bank. Minimum capital requirements are also stipulated. In the Basel Core Principles Assessment conducted during the Financial Sector Assessment Program (FSAP), SBP was assessed as fully compliant with all principles related to licensing and permissible activities. The prudential regulation for consumer financing requires that, before undertaking consumer financing activities, banks meet the following requirements: - prepare a comprehensive consumer credit policy duly approved by the board of directors of the banks and development finance institutions (DFIs), - establish separate risk management institutional capacity staffed by expert and experienced personnel, - develop and implement efficient computer-based management information system capable of generating periodic reports, - develop comprehensive recovery procedures for delinquent consumer loans, - prepare a standardized set of borrowing and recourse documents, and - become a member of at least one credit information bureau
Recommendation	No recommendation.
SECTION B	**DISCLOSURE AND SALES PRACTICES**
Good Practice B.1	***Information on Customers*** **a. When making a recommendation to a consumer, a bank should gather, file, and record sufficient information from the consumer to enable the bank to render an appropriate product or service to that consumer.** **b. The extent of information the bank gathers regarding a consumer should** **(i) be commensurate with the nature and complexity of the product or service being proposed to or sought by the consumer, and**

	(ii) enable the bank to provide a professional service to the consumer in accordance with that consumer's capacity.
Description	According to the PRCF, the bank must, while carrying out consumer financing activities, include risk management processes, such as identification of repayment source and assessment of customers' ability to repay, records of customers dealing with banks/DFIs, and the latest information obtained from the Credit Information Bureau (CIB) about the creditworthiness of the customer. The regulation also requires banks to obtain a written declaration from the customer with details of all consumer financing facilities they use at other banks. These aspects are covered in "PART-B: Minimum Requirements for Consumer Financing" (pre-operations and operations sections) under the Prudential Regulations for Consumer Financing. Before extending any financial facilities to existing or prospective customers, the regulations require that: - Banks/DFIs shall prepare a standardized set of borrowing and recourse documents (duly cleared by their legal counsel) for each type of consumer financing. - For every type of consumer finance activity, the bank/DFI shall develop a specific program. The program shall include the objective/quantitative parameters for the eligibility of the borrower and determining the maximum permissible limit per borrower. - The banks/DFIs must clearly disclose all the important terms, conditions, fees, charges, and penalties, which include annualized percentage rate, prepayment penalties, and the conditions under which they apply. Their customers' reference, banks/DFIs are encouraged to publish brochures with frequently asked questions. Anti-money-laundering/combating the financing of terrorism (AML/CFT) regulations issued in BPRD Circular No. 2 of September 13, 2012, require that banks should formulate and put in place risk-based customer due diligence policies duly approved by their board. Regulation-1, among other things, specifies minimum documents to be obtained, verified, and recorded on a know your customer/customer due diligence (KYC/CDD) form.
Recommendation	No recommendations.
Good Practice B.2	***Affordability*** **a. When a bank makes a recommendation regarding a product or service to a consumer, the product or service it offers to that consumer should be in line with the need of the consumer.** **b. The consumer should be given a range of options to choose from to meet his or her requirements.** **c. Sufficient information on the product or service should be provided to the consumer to enable him or her to select the most suitable and affordable product or service.** **d. When offering a new credit product or service that will significantly**

	increase the amount of debt assumed by the consumer, the consumer's creditworthiness should be properly assessed.
Description	While extending financing facilities to their customers, banks/DFIs should ensure that the total installment of the loans extended by the financial institution is commensurate with the borrower's monthly income and repayment capacity. The banks/DFIs shall ensure that the total monthly amortization payments of consumer loans should not exceed 50 percent of the net disposable income of the prospective borrower. Policies of banks in all major areas of their activities are required to be provided to SBP with updates as and when incorporated. Though SBP does not "approve" such policies, they are thoroughly examined for adherence to laws, regulations, and prudent practices. SBP makes suggestions for changes if needed. As stated above (B.1), banks are required under Prudential Regulations for Consumer Financing to develop specific programs for each consumer finance activity, along with objective/quantitative parameters for the eligibility of the borrower and determining the maximum permissible limit per borrower. In addition, it is mandatory for banks to obtain a credit report and assess repayment capacity of the borrower before extending any consumer financial facilities.
Recommendation	Although regulation requires that banks develop specific programs for each consumer finance activity, and bank policies must be provided to SBP, there is nothing in the regulation that specifically requires that products or services be in line with consumer requirements or that various options be presented to the consumer. It is recommended that this be rectified. The regulation should also require banks to give the consumer a range of options to choose from to meet his or her requirements. In addition, sufficient information on the product or service should be provided to the consumer to enable him or her to select the most suitable and affordable product or service.
Good Practice B.3	***Cooling-off Period*** **a. For financial products or services with a long-term savings component, a bank should provide the consumer a reasonable cooling-off period (at least three to five business days) immediately following the signing of any agreement between the bank and the consumer.** **b. On his or her written notice to the bank during the cooling-off period, the consumer should be permitted to cancel or treat the agreement as null and void without penalty to the consumer of any kind.**
Description	There is no regulation that provides the consumer a cooling-off period. The Consumer Protection Department through Circular No. 2 dated June 29, 2012, on the subject of "sale of third party products by banks" stipulates that the banks shall provide, among other things, a free look period for bancassurance products. However, there is no specific requirement for other banking products or services.

Recommendation	For all financial products or services with a long-term savings component, or those subject to high-pressure sales tactics, banks should be required to provide the consumer a reasonable cooling-off period (at least three to five days) immediately following the signing of any agreement. This is especially important in countries such as Pakistan where the terms of services and products are not readily available or cannot easily be compared.
Good Practice B.4	***Bundling and Tying Clauses*** **a. As much as possible, banks should avoid bundling services and products and the use of tying clauses in contracts that restrict the choice of consumers.** **b. In particular, whenever a borrower is obliged by a bank to purchase any product, including an insurance policy, as a precondition for receiving a loan from the bank, the borrower should be free to choose the provider of the product and this information should be made known to the borrower.**
Description	Banking Policy and Regulations Department Circular No. 11 dated August 1, 2006, requires banks to obtain prior consent from the existing or prospective customers for availing any insurance or other product or service. This consent may be obtained using any mode, for example, IVR (integrated voice recording), ATM screen pop-up, in writing, and by telephone (after due verification). In addition to BPRD Circular No. 11 quoted above; CPD Circular No. 2 dated June 29, 2012, directs the banks to provide a "disclaimer stating that it is only working in the capacity of a distributor." Furthermore, the Competition Act 2007, Section 3, prohibits tie-ins when they prevent, restrict, reduce, or distort competition.
Recommendation	The prudential regulation or other directive should require banks to avoid as much as possible bundling services and products and using tying clauses in contracts that restrict the choice of the consumer. The regulation should also define tying and bundling. For example, tying occurs when two or more products are sold together in a package and at least one of these products is not sold separately. Bundling occurs when two or more products are sold together in a package, although each of the products can also be purchased separately on the market. Where insurance is required, consumers should, insofar as possible, be allowed to select the provider. Further, SBP should consider establishing, in coordination with the PBA, a standardized disclosure format that includes all fees, including bundled

	insurance.
Good Practice B.5	***Preservation of Rights*** **Except where permitted by applicable legislation, in any communication or agreement with a consumer, a bank should not exclude or restrict, or seek to exclude or restrict** **(i) any duty to act with skill, care, and diligence toward the consumer in connection with the provision by the bank of any financial service or product; or** **(ii) any liability arising from the bank's failure to exercise its duty to act with skill, care, and diligence in the provision of any financial service or product to the consumer.**
Description	There does not appear to be a law, regulation, or directive that regulates this issue.
Recommendation	The prudential regulation or other directive should prohibit banks, except where permitted by law, in any communication or agreement with a consumer, to exclude or restrict, or seek to exclude or restrict any duty to act with skill, care, and diligence toward the consumer or any liability arising from the bank's failure to exercise its duty to act with skill, care, and diligence in the provision of any financial service or product to the consumer.
Good Practice B.6	***Regulatory Status Disclosure*** **In all of its advertising, whether by print, television, radio, or otherwise, a bank should disclose the fact that it is a regulated entity and the name and contact details of the regulator.**
Description	There is no regulation requiring banks to disclose their regulatory status, or the name and contact details of the regulator. SBP is of the view that this is not required, because it is the sole regulator of all banks in Pakistan. However, this fact (and SBP's contact details) may not be known to the general public.
Recommendation	The prudential regulation should require banks, in all advertising, whether by print, television, radio, or otherwise, to disclose the fact that it is a regulated entity and the name and contact details of the regulator.

Good Practice B.7	***Terms and Conditions*** **a. Before a consumer opens a deposit, current (checking), or loan account at a bank, the bank should make available to the consumer a written copy of its general terms and conditions, as well as all terms and conditions that apply to the account to be opened. Collectively, these terms and conditions should include:** **(i) disclosure of details of the bank's general charges;** **(ii) a summary of the bank's complaints procedures;** **(iii) a statement regarding the existence of the office of banking ombudsman or equivalent institution and basic information relating to its process and procedures;** **(iv) information about any compensation scheme that the bank is a member of;** **(v) an outline of the action and remedies the bank may take in the event of a default by the consumer;** **(vi) the principles-based code of conduct, if any, referred to in A.2;** **(vii) information on the methods of computing interest rates paid by or charged to the consumer, and any relevant noninterest charges or fees related to the product offered to the consumer;** **(viii) any service charges to be paid by the consumer; restrictions, if any, on account transfers by the consumer; and the procedures for closing an account; and** **(ix) clear rules on the reporting procedures that the consumer should follow in the case of unauthorized transactions in general, and stolen cards in particular, as well as the bank's liability in such cases** **b. The terms and conditions should be written in plain language and in a font size and spacing that facilitates easy reading.**
Description	BPRD Circular No. 07 dated May 27, 2011, stipulates that all terms and conditions of operation of an account shall be made known to the opener of the account at the time the account is opened. The terms and conditions shall be clearly, explicitly, and fully documented in the account opening form or application and must be signed by the prospective depositor or account holder to signify having been read and understood. Banks are required to provide a copy of signed contracts to clients. Banks are also required to clearly disclose all the important terms, conditions, fees, charges, and penalties, which include annualized percentage rate, prepayment penalties, and the conditions under which they apply (minimum disclosure required under the PRCF). BPD Circular No. 6 dated July 14, 2006, requires disclosure of all lending and deposit rates on bank websites and branch locations. To facilitate comparisons, rates must be disclosed on an annualized percentage rate basis (method of

	calculation is prescribed), and whether the loans are priced on a fixed or floating rate basis must also be disclosed. BRPD Circular No. 12 of 2007 further elaborates these requirements. Banks are obliged to stipulate whether a loan is fixed or floating, the benchmark and margin, all fees payable, a complete amortization schedule, a yearly statement of principal, and interest. Under BPD Circular No. 33 of 2003, banks are required to fix charges on a half-yearly basis in advance, and to notify customers of the charges at least seven days before the commencement of the half year. Under BPRD Circular No. 7 of 2011, permissible service charges and fees on deposit accounts are outlined. Banks are required to inform customers of all relevant terms and conditions on such deposit accounts. BPD Circular No. 17 of 2004 provides minimum instructions to banks for dealing with customer complaints, which include the requirement to provide leaflets on complaint procedures and resolution, in both Urdu and English, to customers on request, and to post that information in bank branches and online. Banks are further required to inform customers of the existence and contact information of the ombudsman (OBM) in all bank statements.
Recommendation	Most of the information requirements outlined in B.7 are met. However, the information is fragmented, and SBP may wish to consider requiring banks to place some this information in the terms and conditions it provides to its customers when an account is opened. There is also a need to publish clear rules on reporting procedures for consumers to follow in cases of unauthorized transactions, and the liability of banks in such cases.
Good Practice B.8	***Key Facts Statement*** **a. A bank should have a summary statement, such as a Key Facts Statement (KFS), for each of its accounts, types of loans, or other products or services and provide these to its customers and potential customers.** **b. The summary statement should be written in plain language and summarize in a page or two the key terms and conditions of the specific banking product or service.** **c. Prior to a consumer opening any account at, or signing any loan agreement with, the bank, the consumer should have delivered a signed statement to the bank to the effect that he or she has duly received, read, and understood the relevant summary statement from the bank.** **d. Summary statements throughout the banking sector should be**

	written in such a way as to allow consumers the possibility of easily comparing products that are being offered by a range of banks.
Description	In the PRCF, banks are required to communicate the terms and conditions of each product or service to the customers under "PART-B: Minimum Requirements for Consumer Financing." Banks must disclose all the important terms, conditions, fees, charges, and penalties, including annualized percentage rates, prepayment penalties, and the conditions under which they apply. However, no standardized Key Facts Statement is required. Requirements with respect to account opening are defined under BPRD Circular No. 07 of 2011, while requirements for bancassurance-related information are stipulated under CPD Circular No. 02 dated June 29, 2012. Again, while minimum contents are outlined, no standardized KFS is required. BPRD Circular No. 7 of 2011 requires banks to provide key features of the account opening form in Urdu.
Recommendation	A KFS should provide consumers with simple and standard disclosure of key contractual information of a banking product or service, contributing to the consumers' better understanding of the product or service. KFSs should also allow consumers to compare offers provided by different banks before they purchase a banking product or service and provide a useful summary for later reference during the life of the banking product or service. For credit products, KFSs would constitute an efficient way to inform consumers about their basic rights, the credit reporting systems, and the existing possibilities for disputing information. Examples of KFSs include the U.K. FSA's initial disclosure documents applicable to housing credit products, the European Union's Standard European Consumer Credit Information form, the U.S. Truth in Lending Act's "Schumer Box" for credit cards, Peru's "Hoja Resumen" (Summary Sheet), South Africa's Pre-Agreement Statement & Quotation for Small Credit Agreements, and Ghana's Pre-Agreement Truth in Lending Disclosure Statement. Of special concern is the need to provide basic information to consumers in a language widely understood by them. In Pakistan, although Urdu is spoken by a majority of the population, much written banking information appears to be available only in English. While SBP requires banks to translate key features of the account opening form in Urdu, it would be preferable to have a standardized KFS provided in Urdu as well as English.
Good Practice B.9	***Advertising and Sales Materials*** **a. Banks should ensure that their advertising and sales materials and procedures do not mislead customers.** **b. All advertising and sales materials of banks should be easily readable and understandable by the general public.**

	c. Banks should be legally responsible for all statements made in their advertising and sales materials (i.e., be subject to the penalties under the law for making any false or misleading statements).
Description	The Prudential Regulations for Consumer Financing clearly indicate under Disclosure/Ethics that banks/DFIs must clearly disclose all the important terms and conditions, fees, and charges and penalties, which include annualized percentage rate, prepayment penalties, and the conditions under which they apply. For their customers' reference, banks/DFIs are encouraged to publish brochures of frequently asked questions. Further, BPD Circular Letter No. 33 dated September 1, 2005, and BPD Circular No. 6 dated July 14, 2006, explicitly require banks not to declare misleading information about lending and deposit rates. Banks, and for that matter any advertiser, would be legally bound by the statements made unless a suitable clause or disclaimer is added giving the bank the right to modify terms. Such responsibilities are derived from general law. In addition, instructions issued by SBP, like the one stated above, are binding on banks, and have the backing of the relevant provisions of the BCO. In case of any instance of violation of regulatory instructions, enforcement action is taken under the provisions of the BCO. This aspect is clearly highlighted in most of the circulars and regulations issued by SBP. Further, the Competition Ordinance 2007, Section 10, prohibits deceptive marketing, which includes providing false or misleading information to consumers.
Recommendation	Although the advertising is covered by general law, SBP may wish to consider issuing specific regulations or directives dealing with advertising and sales materials, to prohibit misleading statements and require disclosure of key product characteristics. There are useful provisions of this type in the Operational Guidelines for Credit Cards. These requirements should then be subject to monitoring.
Good Practice B.10	***Third-Party Guarantees*** **A bank should not advertise either an actual or future deposit or interest rate payable on a deposit as being guaranteed or partially guaranteed unless there is a legally enforceable agreement between the bank and a third party that has provided such a guarantee. In the event such an agreement exists, the advertisement should state** **(i) the extent of the guarantee;** **(ii) the name and contact details of the party providing the guarantee; and** **(iii) in the event the party providing the guarantee is in any way connected to the bank, the precise nature of that relationship.**
Description	Because banks are all technically required to work on a profit and loss sharing

	(PLS) basis, all rates are "expected rates of return" and banks may give details of actual rates paid in the past. As such, there are no guaranteed rates offered and in practice actual rates paid are slightly above or below the expected rates of return. However, since 2008, SBP has introduced a minimum rate of return for all categories of savings, PLS saving, or term deposits, which is presently 6 percent. However, banks are free to pay a profit rate on daily products or on average balance basis.
Recommendation	No recommendation in light of above constraint.
Good Practice B.11.	***Professional Competence*** **a. In order to avoid any misrepresentation of fact to a consumer, any bank staff member who deals directly with consumers, or who prepares bank advertisements (or other materials of the bank for external distribution), or who markets any service or product of the bank should be familiar with the legislative, regulatory, and code of conduct guidance requirements relevant to his or her work, as well as with the details of any product or service of the bank that he or she sells or promotes.** **b. Regulators and associations of banks should collaborate to establish and administer minimum competency requirements for any bank staff member who (i) deals directly with consumers, (ii) prepares any Key Facts Statement or any advertisement for the bank, or (iii) markets the bank's services and products.**
Description	CPD Circular No. 02 of June 29, 2012, requires that the personnel involved in sales have adequate understanding of the product and are familiar with the bank's policy in this regard. For this purpose, banks must train their existing staff to improve their understanding and knowledge of the product. Qualification requirements for bank staff are not specified. Most of the regulatory instructions issued by SBP require that banks should ensure compliance with relevant laws, rules, and regulations while offering various products and services. Failure to do so attracts action under the provisions of the BCO. It is customary for banks to have specialized marketing personnel who, in conjunction with established advertising agencies, develop marketing themes and advertisements. As a matter of practice (but not regulation), all external communications including advertisements are vetted by banks' legal departments to safeguard against any legal, regulatory, or reputational risk.
Recommendation	SBP and PBA should collaborate to establish and administer minimum competency requirements for any bank staff member who (i) deals directly with consumers, (ii) prepares any advertisement or KFS for the bank, or (iii) markets any of the bank's services and products to consumers.

SECTION C	CUSTOMER ACCOUNT HANDLING AND MAINTENANCE
Good Practice C.1	***Statements*** **a. Unless a bank receives a customer's prior signed authorization to the contrary, the bank should issue, and provide the customer free of charge, a monthly statement of every account the bank operates for the customer.** **b. Each such statement should (i) set out all transactions concerning the account during the period covered by the statement and (ii) provide details of the interest rate(s) applied to the account during the period covered by the statement.** **c. Each credit card statement should set out the minimum payment required and the total interest cost that will accrue, if the cardholder makes only the required minimum payment.** **d. Each mortgage or other loan account statement should clearly indicate the amount paid during the period covered by the statement, the total outstanding amount still owed, the allocation of payment to the principal and interest, and, if applicable, the up-to-date accrual of taxes paid.** **e. A bank should notify a customer of long periods of inactivity for any of their accounts and provide a reasonable final notice in writing to the customer if the funds are to be treated as unclaimed money.** **f. When a customer signs up for paperless statements, such statements should be in an easy-to-read and readily understandable format.**
Description	Section 33 of Payment Systems and Electronic Fund Transfers Act, 2007, states that a financial institution shall provide each consumer with a periodic statement for each account of such consumer that may be accessed electronically, at a period as the state bank may determine from time to time. Under the Operational Guidelines for Credit Card Business in Pakistan issued by the Payment Systems Department in PSD Circular No. 01 of January 2009, all banks/DFIs are required to dispatch a monthly statement of account to credit card holders at least 15 days before the due date. Toward this end, banks/DFIs may offer online, e-mail, or IVR billing facilities, with appropriate security measures. The minimum content of such statements is specified in the Operational Guidelines, and is comprehensive. In terms of BPRD Circular No. 02 of January 5, 2010, banks are required to dispatch, free of charge, statements of accounts to their account holders having a closing balance equal to or exceeding PRs 10,000 at least twice a year on a six-month basis within one month from the close of the half year (i.e., June 30 and December 31). However, banks also provide statements of account to their accountholders on their own (monthly, quarterly, biannual, or annual). There is no specific regulation on the content of statements of account, which at minimum are understood to contain all individual debits and credits in the account with brief details. AML/CFT regulations define an inactive account as a "Dormant or in-operative account," meaning an account in which no transaction has taken place for the

	past year. In addition, most banks observe an internal policy of designating an account as inactive if no transaction takes place in the account for an extended period of time. Such accounts are reactivated after appropriate verifications as and when approached by the account holders. For accounts that have remained inactive for an extended period, SBP has issued a Master Circular on unclaimed deposits (BPD Circular No. 07 dated July 21, 2006, under Section 31 of the BCO) whereby banks must notify the account holder about the inactive status of the account. In Pakistan, it is difficult to send monthly statements by post, because the postal service is slow and unreliable. As a result, sending account statements is costly because it requires costly courier services. This explains the biannual frequency. Although banks deliver statements every six months as required, most indicate they also use electronic means (e-mail, text) to advise customers of debits, credits, and balances.
Recommendation	Given the lack of reliability of the postal services, SBP may wish to require that banks offer monthly statements by electronic means, or if the customer does not have access to such means, that the bank make statements available at the nearest branch at the request of the customer. SBP should also set minimum standards for the language, content, and format of account statements.
Good Practice C.2	***Notification of Changes in Interest Rates and Noninterest Charges*** **a. A customer of a bank should be notified in writing by the bank of any change in** **(i) the interest rate to be paid or charged on any account of the customer as soon as possible; and** **(ii) a noninterest charge on any account of the customer a reasonable period in advance of the effective date of the change.** **b. If the revised terms are not acceptable to the customer, he or she should have the right to exit the contract without penalty, provided such right is exercised within a reasonable period.** **c. The bank should inform the customer of the foregoing right whenever a notice of change under paragraph a. is made by the bank.**
Description	Banks are required to notify any change in loan or lending product provisions as per BPRD Circular 12 dated August 01, 2007, and BPRD Circular Letter No. 33 dated November 13, 2008, pertaining to "pricing of lending products and loan documentation." Under the Operational Guidelines for Credit Cards (OGCC) mentioned above, the statement of account to credit card holders must contain annualized rate of interest and interest amount, along with the method of

	calculating rates for purchases of goods and services, cash advances, and other benefits of the credit card whenever these rates change. The customer must be notified of changes in terms at least 30 days before they become effective. Banks cannot change the interest rate payable on fixed-rate loans during the duration of the loan. For variable-rate loans, the margin cannot change, and the base rate can change only with periodic changes in the agreed benchmark. The Payment and Electronic Funds Act provides that customers must be notified of relevant charges at least 21 days prior to the effective date of any material change in any terms or conditions. There does not appear to be a specific provision allowing customers to exit agreements without penalty in the event of changes in terms and conditions.
Recommendation	SBP should clarify by directive that customers can exit contracts without penalty if they are dissatisfied with changes in terms and conditions, and specify that banks should inform customers of this right.
Good Practice C.3	***Customer Records*** **a. A bank should maintain up-to-date records on each customer of the bank, which contain the following:** **(i) a copy of all documents required to identify the customer and provide the customer's profile;** **(ii) the customer's address, telephone number, and all other contact details;** **(iii) any information or document in connection with the customer that has been prepared in compliance with any statute, regulation, or code of conduct;** **(iv) details of all products and services provided by the bank to the customer;** **(v) a copy of correspondence from the customer to the bank and vice-versa, and details of any other information provided to the customer, in relation to any product or service offered or provided to the customer;** **(vi) all documents and applications of the bank completed, signed, and submitted to the bank by the customer;** **(vii) a copy of all original documents submitted by the customer in support of an application by the customer for a product or service by the bank; and** **(viii) any other relevant information concerning the customer.** **b. A law or regulation should provide the minimum permissible period for retaining all such records and, throughout this period, the customer should be provided ready access to all such records free of charge or for a reasonable fee.**

Description	AML/CFT Regulation-1, requires banks/DFIs to periodically review the adequacy of information obtained in respect of customers and beneficial owners and ensure that the information is kept up to date, particularly for higher-risk categories of customers. The review period and procedures thereof should be defined by banks/DFIs in their AML/CFT policies, on a risk-based approach. AML/CFT Regulation-5 states, "Banks/DFIs shall maintain all necessary records on transactions, both domestic and international, including the results of any analysis undertaken (e.g., inquiries to establish the background and purpose of complex, unusual large transactions) for a minimum period of ten years from completion of the transaction." There are no restrictions imposed by banks on their customers to have access to records, except the unadvised and confidential STR-related information. The Electronic Transactions Ordinance, 2002, Section 6, and the Payments and Electronic Transfers Act, 2007, Section 7, require financial institutions providing funds transfers to maintain complete records for periods determined by SBP. Branchless banking guidelines also require agents to ensure safekeeping of all relevant data and files for a period of five years.
Recommendation	No recommendation.
Good Practice C.4	***Paper and Electronic Checks*** **a. The law and code of conduct should provide for clear rules on the issuance and clearing of paper checks that include rules on** **(i) checks drawn on an account that has insufficient funds;** **(ii) the consequences of issuing a check without sufficient funds;** **(iii) the duration within which funds of a cleared check should be credited into the customer's account;** **(iv) the procedures on countermanding or stopping payment on a check by a customer;** **(v) charges by a bank on the issuance and clearance of checks;** **(vi) liability of the parties in the case of check fraud; and** **(vii) error resolution.** **b. A customer should be told of the consequences of issuing a paper check without sufficient funds at the time the customer opens a checking account.** **c. A bank should provide the customer with clear, easily accessible, and understandable information regarding electronic checks, as well the cost of using them.** **d. In respect of electronic or credit card checks, a bank should inform each customer in particular** **(i) how the use of a credit card check differs from the use of a credit card;** **(ii) of the interest rate that applies and whether this differs from the rate charged for credit card purchases;** **(iii) when interest is charged, whether there is an interest-free**

	period, and if so, for how long; **(iv) whether additional fees or charges apply and, if so, on what basis and to what extent; and** **(v) whether the protection afforded to the customer making a purchase using a credit card check differs from that afforded when using a credit card and, if so, the specific differences.** **e. Credit card checks should not be sent to a consumer without the consumer's prior written consent.** **f. There should be clear rules on procedures for dealing with authentication, error resolution, and cases of fraud.**
Description	The Negotiable Instrument Act, 1881, and Payment Systems and Electronic Fund Transfers Act, 2007, provide some relevant rules regarding the above matters. BPD Circular Letter No. 22 dated June 14, 2005, and BPRD Circular Letter No. 31 dated October 12, 2009, direct the banks to mention specific and clear reason for dishonoring checks issued by their customers. The Criminal Law (Amendment) Ordinance, 2002, made drawing a check with insufficient funds a criminal offense and liable to prosecution under the provision of the Code of Criminal Procedure, 1898. Electronic checks are yet to be introduced in Pakistan. In Pakistan, commercial banks do not currently send credit card checks to consumers. For electronic fund transfers, the Payment Systems and Electronic Fund Transfer Act, 2007, contains details about "Notification of Errors," "Correcting Errors," "Violations Affecting Electronic Commerce," and "Cheating by Use of Electronic Device"; however, these do not appear to cover paper checks.
Recommendation	The rules and regulations regarding checks are very dated and appear incomplete. Additional instructions should be issued: (i) Given the very severe criminal penalties that may be imposed for issuing checks with insufficient funds, banks should be required to inform customers of these consequences when they open a checking account. Charges for check issuance and clearing should also be disclosed. (ii) Liabilities of parties for fraud should be specified. (iii) The delay within which funds for cleared checks should be credited to accounts should be disclosed. Even though electronic checks and credit card checks are not currently used in Pakistan, given their usage elsewhere, SBP may wish to be proactive in considering the rules that should apply to these products.

Good Practice C.5	*Credit Cards* **a. There should be laws on the issuance of credit cards and related customer disclosure requirements.** **b. Banks, as credit card issuers, should ensure that personalized disclosure requirements are made in all credit card offers, including fees and charges (including finance charges), credit limit, penalty interest rates, and method of calculating the minimum monthly payment.** **c. Banks should not be permitted to impose charges or fees on preapproved credit cards that have not been accepted by the customer.** **d. Consumers should be given personalized minimum payment warnings on each monthly statement and the total interest costs that will accrue if the cardholder makes only the requested minimum payment.** **e. Among other things, the legal rules should also** **(i) restrict or impose conditions on the issuance and marketing of credit cards to young adults who have no independent means of income;** **(ii) require reasonable notice of changes if fees and interest rates increase;** **(iii) prevent the application of new higher-penalty interest rates to the entire existing balance, including past purchases made at a lower interest rate;** **(iv) limit fees that can be imposed, such as those charged when consumers exceed their credit limits;** **(v) prohibit a practice called double-cycle billing, by which card issuers charge interest over two billing cycles rather than one;** **(vi) prevent credit card issuers from allocating monthly payments in ways that maximize interest charges to consumers; and** **(vii) limit upfront fees charged on subprime credit cards issued to individuals with bad credit.** **f. There should be clear rules on error resolution and reporting unauthorized transactions and stolen cards, with the ensuing liability of the customer being made clear to them prior to their acceptance of the credit card.** **g. Banks and issuers should conduct consumer awareness programs on the misuse of credit cards, credit card over-indebtedness, and prevention of fraud.**
Description	The Operational Guidelines for Credit Card Business in Pakistan (issued in 2009) contain reasonably comprehensive and detailed consumer protection rules, including instructions on marketing of credit cards, the credit card application process, information on interest rates and other charges, billing processes, the collection/recovery process, the complaint resolution process, and the merchant relationship.

	Interest rates must be stipulated on an annual basis, and sent to customers through advertisements or mail. All fees and charges must be explicitly notified in the user guide or application form, or the schedule of charges must be given to the customer at the time of sale. The customer must be notified of any changes to terms or conditions 30 days before they take effect. There is a clear framework for error resolution and liability in the OGCC, complemented by rules imposed by issuers such as Visa and MasterCard, and banks must monitor card usage and maintain data on fraudulent usage. Curtailment of customer rights is expressly prohibited by the OGCC. There are further guidelines issued under the heading "Disclosure/Ethics" in "PART-B: Minimum Requirements for Consumer Financing" (pre-operations and operations sections) of the Prudential Regulations for Consumer financing. These require, among other things, monthly statements, due dates, penalty rates, and the prohibition of charging insurance premia without written consent. SBP has established a code of conduct that prohibits aggressive selling of credit cards. Although monthly statements do invariably indicate the minimum amount payable, total interest costs are not quantified, as they are understood to be charged at the contracted or agreed rate with the customer when the credit card is issued. Banks/DFIs should take reasonable steps to satisfy themselves that cardholders have received the cards, in person or by mail. Banks/DFIs should advise the cardholders of the need to take reasonable steps to keep the card safe and the identification number secret to avoid fraud. There are no restrictions on upfront fees chargeable on subprime (or any other) cards, though subprime credit card issuance is not currently practiced in Pakistan. The PRCF restricts unsecured credit card limits, and requires mandatory credit checks. Some banks have conducted consumer awareness programs on the misuse of credit cards and consumer over-indebtedness, but more needs to be done in this area.
Recommendation	The rules and regulations regarding credit cards are broadly appropriate, but SBP might wish to review them to address areas in C.5 not currently covered, such as most of those detailed in point e. above. SBP should also include awareness on credit card usage and indebtedness in its planned financial education programs.
Good Practice C.6	***Internet Banking and Mobile Phone Banking***[2]

[2]"Internet banking" is defined as banking services that customers may access via the Internet. This access could be through a computer, mobile phone, or other device. Payment services that are initiated only via the Internet using a mobile phone (e.g., by a mobile banking application using an app on a smartphone) are not considered to be mobile payments; instead, they are categorized

	a. The provision of Internet banking and mobile phone banking (m-banking) should be supported by a sound legal and regulatory framework. **b. Regulators should ensure that banks or financial service providers providing Internet and m-banking have in place a security program that ensures** **(i) data privacy, confidentiality, and data integrity;** **(ii) authentication, identification of counterparties, and access control;** **(iii)non-repudiation of transactions;** **(iv)a business continuity plan; and** **(v) the provision of sufficient notice when services are not available.** **c. Banks should also implement an oversight program to monitor third-party control conditions and performance, especially when agents are used for carrying out m-banking.** **d. A customer should be informed by the bank whether fees or charges apply for Internet or m-banking and, if so, on what basis and how much.** **e. There should be clear rules on the procedures for error resolution and fraud.** **f. Authorities should encourage banks and service providers to undertake measures to increase consumer awareness regarding Internet and m-banking transactions.**
Description	The provision of Internet banking and mobile phone banking are covered in the following laws and regulations: 1. Electronic Transactions Ordinance, 2002 2. Payment Systems and Electronic Fund Transfer Act, 2007 3. Branchless Banking Regulation (originally issued in 2008 and revised in 2011) 4. Banking Companies Ordinance, 1962 The Payment Systems and Electronic Fund Transfer Act, 2007, requires, among other things, that "Financial Institutions and other institutions providing Electronic Funds Transfer facilities shall ensure that secure means are used for transfer, compliant with current international standards and as may be prescribed by the State Bank from time to time." SBP has also issued Guidelines on Information Technology Security (BSD Circular No. 15) and Guidelines on Branchless Banking, which address technology-related risks and their implications. However, there is no separate guidance on Internet banking and mobile phone banking per se. Internet banking and m-banking payments are not considered as new payment instruments but rather as other access methods to activate existing means of payment for

as Internet payments. This interpretation is consistent with the view of the Committee on Payment and Settlement Systems of the Bank for International Settlements, the relevant standard-setting body on payment and settlement systems. However, for practical reasons and due to the importance of mobile money in the country, Good Practice C.6 is intended here as also covering mobile payments and, to some extent, e-money.

	financial transactions processed by banks between bank customers. Banks follow their own internally developed, screened, and legally vetted processes, which can be scrutinized during onsite inspections of banks conducted by SBP. Under BPD Circular No 3 of 2003 banks are required to publish and make available at their places of business and on their website schedules of all charges, including those related to Internet and m-banking. Banks are free to determine the rates of charges for various services they may provide to their customers. The regulatory instructions also require that the banks will levy service charges, which are commensurate with the scope of service they render to the customers. The Guidelines on Outsourcing Arrangements issued in BPRD Circular No. 9 dated July 13, 2007, outlines a number of relevant provisions, including on customer confidentiality, grievance redressal, and contingency planning. The Guidelines for Branchless Banking (draft dated November, 24, 2007) outline a number of consumer protection principles for m-banking and other types of branchless banking ("banks need to ensure that adequate measures for customer protection, awareness and dispute resolution are in place"). But it appears that these have been issued as a draft only, and many of the principles outlined are recommendations only, and would not appear to be binding on banks. In other instances, the guidelines are prescriptive and detailed, such as on complaint redressal and consumer awareness programs: "Financial Institutions must put in place a proper complaint redressal setup capable of efficiently and quickly redress complaints from customers. Complaint Redressal (CR), at minimum should be capable of: • Receiving and processing customers' complaints 24 hours through, text, IVR and e-mail, • Generate acknowledgement of complaint giving it a unique complaint number. • Communicate acknowledgement to customer giving either the redressal or the complaint number and estimated time to redressal. • Redirecting the complaint to appropriate function for redressal. • Keep track/log of all complaints and give status of every complaint." In any event, for all banking transactions and services there are guidelines for error resolution and fraudulent activities, mentioned in the relevant instructions or generally covered under Guidelines in dealing with Customers Complaints given in BPD Circular No. 17 dated June 7, 2004. SBP regularly engages in consumer awareness campaigns in collaboration with foreign and local partners. Banks also undertake such activities according to their own business plans and programs. In the case of branchless banking, the draft guidelines outline minimum requirements for consumer awareness to be

	conducted by banks.
Recommendation	The draft Guidelines for Branchless Banking should be finalized as soon as practicable in order to provide a sound framework for branchless banking, which is growing rapidly in Pakistan. SBP should review existing policies and guidelines to determine if they need to be strengthened to ensure compliance with C.6 b. and c. above.
Good Practice C.7	***Electronic Fund Transfers and Remittances*** **a. There should be clear rules on the rights, liabilities, and responsibilities of the parties involved in any electronic fund transfer.** **b. Banks should provide information to consumers on prices and service features of electronic fund transfers and remittances in easily accessible and understandable forms. As far as possible, this information should include** **(i) the total price (e.g., fees for the sender and the receiver, foreign exchange rates, and other costs);** **(ii) the time it will take the funds to reach the receiver;** **(iii)the locations of the access points for sender and receiver; and** **(iv)the terms and conditions of electronic fund transfer services that apply to the customer.** **c. To ensure transparency, it should be made clear to the sender if the price or other aspects of the service vary according to different circumstances, and the bank should disclose this information without imposing any requirements on the consumer.** **d. A bank that sends or receives an electronic fund transfer or remittance should document all essential information regarding the transfer and make this available to the customer who sends or receives the transfer or remittance without charge and on demand.** **e. There should be clear, publicly available, and easily applicable procedures in cases of error and fraud in respect of electronic fund transfers and remittances.** **f. A customer should be informed of the terms and condition of the use of credit/debit cards outside the country, including foreign transaction fees and foreign exchange rates that may be applicable.**
Description	The Payment Systems and Electronic Fund Transfer Act, 2007, provides standards to protect consumers and to determine respective rights and liabilities of the financial institutions and other service providers, their consumers, and participants. It provides clear rules on the rights, liabilities, and responsibilities of the parties involved in any electronic fund transfer. Section 29 of the act provides requirement of notice to consumers before levying any fee, though there is no requirement of providing the level of detail outlined above, nor is there a requirement regarding notification of the time it will take

	for funds to reach the receiver. Section 30 requires that the terms and conditions of EFTs shall be disclosed in English and in a manner clearly understood by the consumer, at the time the consumer contracts for an electronic fund transfer service. It further elaborates on the nature of the terms and conditions to be disclosed. As noted in C.6, banks are generally required to disclose their schedule of charges to their customers. A bank is required to document all essential information regarding the transfer and to make this information available to the customer (Section 32). There are clear procedures outlined for handling errors and frauds (e.g., Sections 36–39). The mission found no specific rules related to terms and conditions of the use of credit cards outside of Pakistan, but all provisions of the Payment Systems and Electronic Fund Transfer Act, 2007, that deal directly or indirectly with payments within Pakistan apply.
Recommendation	SBP may wish to consider greater specificity on pricing, notably of foreign transactions, and requiring banks to notify clients of the time it will take for an ETF to reach the receiver.
Good Practice C.8	***Debt Recovery*** **a. A bank, agent of a bank, and any third party should be prohibited from employing any abusive debt collection practice against any customer of the bank, including the use of any false statement, any unfair practice, or the giving of false credit information to others.** **b. The type of debt that can be collected on behalf of a bank, the person who can collect any such debt, and the manner in which that debt can be collected should be indicated to the customer of the bank when the credit agreement giving rise to the debt is entered into between the bank and the customer.** **c. A debt collector should not contact any third party about a bank customer's debt without informing the customer of the debt collector's right to do so; and the type of information that the debt collector is seeking.** **d. Where sale or transfer of debt without borrower consent is allowed by law, the borrower should be** **(i) notified of the sale or transfer within a reasonable number of days;** **(ii) informed that the borrower remains obligated on the debt; and** **(iii) provided with information as to where to make payment, as well as the purchaser's or transferee's contact information.**
Description	

	Banks are exposed to the risk of nonrecovery or late recovery of nonperforming loans because of a huge backlog of cases pending with the courts that intensifies this risk. The volume of the backlog of pending cases is much greater than the processing capacity of the concerned courts. According to the available records, more than 56,000 recovery suits were pending with courts and banking tribunals during the first quarter of 2011. More than 14,000 of these have been pending for more than 10 years. The relatively limited size and operational capacity of the judiciary compared with the huge backlog of pending cases slows down the litigation process and not only delays the recovery of the defaulted amount but also provides incentives to borrowers to default on their commitments. SBP, through BPRD Circular No. 13 dated November 3, 2008, has issued fair debt collection guidelines that set minimum standards to be observed by banks/DFIs in collection and recovery of debt from customers and borrowers. These guidelines are applicable to various types of consumer financing facilities, including credit cards and housing, auto, and personal loans. They include the following minimum guidelines: (i) Before proceeding for debt collection from a customer, the bank shall provide the customer all information relating to payments fallen due. A minimum of 14 days' notice will be served to the customer through letter or text advising him or her to make the overdue payment, before a visit to his or her residence or business is undertaken in a lawful manner to negotiate recovery of the outstanding amounts. Advance notice will be required to the customer when bank staff picks up the payment, and if done at the customer's request then it should be properly recorded. (ii) Banks/DFIs in their collection/recovery efforts shall ensure that (a) the customers/borrowers are not contacted at an inconvenient time; (b) proper disclosure of identity, name of the bank, and the purpose of call is provided; and (c) only lawful and acceptable business language and professional attitude are employed in such contact. (iii) Banks/DFIs shall also ensure that (a) collection calls are properly recorded; (b) customers/borrowers are contacted at the given address/phone numbers and if they cannot be contacted, at alternate address/phone number obtained through collection efforts; (c) "visit reports" shall be kept on record for at least six months; and (d) collection staff shall not harass customers' family members. However, necessary information could be obtained from family, friends, or a third party of the borrower if he or she is not in contact for 30 days after the first missed payment. (iv) Banks/DFIs shall give 14 days' written notice before repossessing a leased vehicle on breach of an agreement or default on repayment by the customers/borrowers; banks/DFIs and recovery agencies they employ are advised to allow the customer/borrower to take their possessions out of the vehicle.

	(v) Banks/DFIs are advised to ensure that (a) their collection/recovery staff do not transfer or misuse any personal data of customers/borrowers without their prior approval and (b) any information about the customer/borrower provided to the collections staff are properly documented. (vi) Banks/DFIs shall ensure that the collection/recovery agencies they employ must be enrolled with the Pakistan Banks' Association, in accordance with the Guidelines on Outsourcing Arrangements issued by State Bank of Pakistan. (vii) In order to effectively control the functions of collection and recovery and the human resources engaged in this process, banks/DFIs would ensure the following: (a) Frame a code of lawful conduct for recovery staff. (b) Introduce a well-defined mechanism for addressing complaints against the collection/recovery staff. (c) Undertake a periodic review of their recovery procedures. (d) Engage suitably qualified staff in collection/recovery and provide them necessary training. (e) Regularly monitor the activities of collection and recovery staff. There is no requirement the bank provide information on debt collection procedures at the time the credit agreement is entered into. The sale or transfer of debt without borrower consent is not practiced in Pakistan.
Recommendation	The written directives on debt recovery are comprehensive and in line with the Good Practice. However, the mission was informed that the guidelines are not always followed in practice. It is therefore recommended that customers be made more aware of these guidelines, and informed of their rights.
Good Practice C.9	***Foreclosure of mortgaged or charged property*** **a. In the event that a bank exercises its right to foreclose on a property that serves as collateral for a loan, the bank should inform the consumer in writing in advance of the procedures involved, and the process to be employed by the bank to foreclose on the property it holds as collateral, and the consequences thereof to the consumer.** **b. At the same time, the bank should inform the consumer of the legal remedies and options available to him or her regarding the foreclosure process.** **c. If applicable, the bank should draw the consumer's attention to the fact that the bank has a legal right to recover the balance of the debt due in the event the proceeds from the sale of the foreclosed property are not sufficient to fully discharge the outstanding amount.**

	d. In the event the mortgage contract or charge agreement permits the bank to enforce the contract without court assistance, the bank should ensure that it employs professional and legal means to enforce the contract, including regarding the sale of the property.
Description	Section 15 of the Financial Institutions (Recovery of Finances) Ordinance, 2001, elaborates on the information to be given to a customer regarding the foreclosure of his or her property along with the explicit notice periods. (Three written notices are required.) Under Section 15(4) of the ordinance, financial institutions may sell the mortgaged property without intervention of courts in the manner prescribed in the said law. Property under charge can be sold only with the court's assistance. There is nothing in the ordinance that stipulates explicitly that the bank must inform the customer of the procedure involved, of the legal remedies available, or that the bank has a legal right to recover any balance due if the proceeds of sale are insufficient to fully discharge the debt. It should be noted that the ordinance was enacted at a time when Pakistan was experiencing severe problems with debt recovery and willful defaults, and it was intended primarily to address this problem.
Recommendation	SBP may wish to consider issuing a circular addressing the issues noted above requiring banks/DFIs to inform the customer of the procedure involved, of the legal remedies available, and that the bank has a legal right to recover any balance due if the proceeds of sale are insufficient to fully discharge the debt.
Good Practice C.10	***Bankruptcy of Individuals*** **a. A bank should inform its individual customers in a timely manner and in writing on what basis the bank will seek to render a customer bankrupt, the steps it will take in this respect, and the consequences of any individual's bankruptcy.** **b. Every individual customer should be given adequate notice and information from his or her bank to enable the customer to avoid bankruptcy.** **c. Either directly or through its bank association, every bank should make counseling services available to customers who are bankrupt or likely to become bankrupt.** **d. The law should enable an individual to** **(i) declare his or her intention to present a debtor's petition for a declaration of bankruptcy;** **(ii) propose a debt agreement;** **(iii)propose a personal bankruptcy agreement; or** **(iv)enter into voluntary bankruptcy.** **e. Any institution acting as the bankruptcy office or trustee responsible for the administration and regulation of the personal**

	bankruptcy system should provide adequate information to consumers on their options to deal with their own debt and rehabilitation process in the event of bankruptcy.
Description	Personal insolvency is covered by the Provincial Insolvency Act, 1920. This is a very antiquated regime for personal bankruptcy, which is punitive rather than rehabilitative, and does not allow individuals to make a proposal to creditors. From discussions with banks and practitioners, it appears that personal bankruptcy is almost never invoked in Pakistan. The practices outlined above are therefore not respected.
Recommendation	There is first of all a need for a complete overhaul of both corporate and personal bankruptcy laws in Pakistan. If and when this is done, it would be important to apply the practices outlined above.
SECTION D	**PRIVACY AND DATA PROTECTION**
Good Practice D.1	***Confidentiality and Security of Customer Information*** **a. The banking transactions of any bank customer should be kept confidential by his or her bank.** **b. The law should require a bank to ensure that it protects the confidentiality and security of the personal data of its customers against any anticipated threats or hazards to the security or integrity of such information, as well as against unauthorized access.**
Description	Section 33A of the BCO and Section 70 of the Payment Systems and Electronic Fund Transfer Act, 2007 deal with secrecy, fidelity, and privacy of customer data and state that "Every bank and financial institution shall not, except as otherwise required by law or according to customary practices in the banking sector, divulge any information relating to the affairs of its customers." The Guidelines on Outsourcing Arrangements further require banks to ensure that outsourcing arrangements that involve the transfer of customer information to third parties comply with Section 33A of the BCO, as well as other relevant laws, regulations, and directives. The Payment Systems and Electronic Funds Transfer Act, 2007 Section 15, requires that providers use secure means for transfer, compliant with international standards or requirements that may be prescribed by SBP. Under the OGCC Section 2, credit card issuers are similarly required to ensure the confidentiality of customer information, and may not share it with or divulge it to any party except SBP's Credit Information Bureau or another approved credit information bureau. The Branchless Banking Guidelines, 2007, also require the protection of customer confidentiality.

	Finally, the Guideline on Information Technology Security (BSD Circular 15, 2004) makes specific reference to the need for banks to address risks such as unauthorized access to critical financial data, impersonating clients, and theft or alteration of information.
Recommendation	No recommendation.
Good Practice D.2	***Sharing Customer Information*** **a. A bank should inform its customers in writing** **(i) of any third-party dealing for which the bank is obliged to share information regarding any account of the customer, such as any legal inquiry by a credit bureau; and** **(ii) as to how it will use and share the customer's personal information.** **b. Without the customer's prior written consent, a bank should not sell or share account or personal information regarding a bank customer to or with any party not affiliated with the bank for the purpose of telemarketing or direct mail marketing.** **c. The law should allow a bank customer to stop or opt out of the bank's sharing of certain customer information and, prior to any such sharing of information for the first time, every bank should be required to inform each of its customers in writing of his or her rights in this respect.** **d. The law should prohibit the disclosure by a third party of any banking-specific information regarding a bank customer.**
Description	Sharing of personal information is not a customary banking practice in Pakistan except in response to a credit report sought by a bank from another bank on a particular customer. Bank secrecy laws and regulations as quoted above prevent the sharing of personal information. However, credit-related information and defaults are shared with SBP, which maintains a Credit Information Bureau accessible to all banks. Accordingly, under Section 25(A) of the BCO, all banks are required to furnish to the state bank credit information in such manner as the state bank may specify, and the state bank may, either on its own or at the request of any banking company, make such information available to any banking company. Accordingly, the borrower's consent is not required for reporting of credit data to state bank. It is relevant to highlight that a draft Credit Bureaus Act is in the process of promulgation, which covers this aspect. Under Section 93C of the BCO, banks may share general information/data among themselves, but the information cannot be used for marketing purposes. Section 70 of the Payment Systems and Electronic Fund Transfer Act2007 restricts financial institutions from divulging any information relating to electronic funds transfer, affairs, or accounts of its customers except where required by law or customary among bankers or if the client has given his consent.

Recommendation	No recommendation.
Good Practice D.3	***Permitted Disclosures*** **The law should provide for** **(i) the specific rules and procedures concerning the release to any government authority of the records of any customer of a bank;** **(ii) rules on what the government authority may and may not do with any such records;** **(iii) the exceptions, if any, that apply to these rules and procedures; and** **(iv) the penalties for the bank and any government authority for any breach of these rules and procedures.**
Description	Under Section 46A of SBP Act, 1956 (Production of unpublished record of Bank): (1) No court, tribunal, or other authority shall be entitled to compel the bank (State Bank of Pakistan) or any person in the service of the bank to produce, or as the case may be, give any evidence derived from, any unpublished record of the bank. (2) No court, tribunal, or other authority shall permit anyone to produce or give evidence derived from any unpublished record of the bank, except with the prior permission in writing of the governor who may give or withhold such permission as he thinks fit. Law enforcement agencies (LEAs) may access individual customer information to aid in their investigation under a court order, which generally entails stringent criteria as determined by the courts in each case on merit. Authenticated copies of such bank records may be used as evidence by LEAs. Banks are otherwise not under compulsion as per Section 33A (fidelity and secrecy) of the BCO, bank shall not divulge any information relating to the affairs of its customers except as otherwise required by law. Under Section 33A (4) of the BCO, the State Bank of Pakistan may, if satisfied that it is necessary so to do at the time of holding general elections under any law relating thereto, publish a list of persons to whom any loans, advances, or credits were extended by a bank or financial institution, either in their own name or in the name of their spouses or dependents or of their business concerns (if mainly owned and managed by them) that were due and payable and had not been paid back for more than one year from the due date, or whose loans were unjustifiably written off in violation of banking practices, rules, or regulations on or after such date as may be determined by the government: Provided that before publishing the name of any person in any such list, the person shall be given prior notice and, if he or she so requests, an opportunity of hearing.
Recommendation	Pakistan is generally in compliance with the good practices related to permitted disclosures; however, there is no stipulation of the penalties that apply to banks or other agencies for failure to comply with the law. The government may wish to consider whether such penalties should be specified.
Good Practice D.4	***Credit Reporting***

	a. Credit reporting should be subject to appropriate oversight, with sufficient enforcement authority. **b. The credit reporting system should have accurate, timely, and sufficient data. The system should also maintain rigorous standards of security and reliability.** **c. The overall legal and regulatory framework for the credit reporting system should be** **(i) clear, predictable, non-discriminatory, proportionate, and supportive of consumer rights; and** **(ii) supported by effective judicial or extrajudicial dispute-resolution mechanisms.** **d. In facilitating cross-border transfer of credit data, the credit reporting system should provide appropriate levels of protection.** **e. Proportionate and supportive consumer rights should include the right of the consumer** **(i) to consent to information-sharing based on the knowledge of the institution's information-sharing practices;** **(ii) to access his or her credit report free of charge (at least once a year), subject to proper identification;** **(iii) to know about adverse action in credit decisions or less-than-optimal conditions or prices due to credit report information;** **(iv) to be informed about all inquiries within a period of time, such as six months;** **(v) to correct factually incorrect information or to have it deleted and to mark (flag) information that is in dispute;** **(vi) to reasonable retention periods of credit history, for instance two years for positive information and five to seven years for negative information; and** **(vii) to have information kept confidential and with sufficient security measures in place to prevent unauthorized access, misuse of data, or loss or destruction of data.** **f. The credit registries, regulators, and bank associations should undertake campaigns to inform and educate the public on the rights of consumers in the above respects, as well as the consequences of a negative personal credit history.**
Description	SBP currently operates and manages the Electronic Credit Information Bureau (eCIB), further to Section 25 (a) of the BCO. The eCIB gathers and reports credit information on all bank borrowers, irrespective of the size of the loan. Banks are required to obtain a credit report on borrowers before extending credit facilities. No regulatory or supervisory regime is currently available for incorporation and functioning of private credit bureaus in Pakistan. The proposed draft Credit

	Bureaus Act will cover the licensing requirements for existing and newly established credit bureaus. A few financial institutions are sharing consumer credit information confidentially and voluntarily through a private company owned by the participating banks, Datacheck. SBP conducts consumer awareness campaigns regarding the importance of credit databases and the implications of negative reporting for financial consumers. All banks and member financial institutions are required to ensure the integrity and reliability of credit data reporting as per CPD Circular Letter No. 1 dated May 27, 2011. SBP takes severe punitive actions against defaulting banks and financial institutions under the provisions of the BCO. SBP ensures that rights of consumers are not jeopardized and consumers' complaints are dealt with effectively. BSD Circular No. 16 of 2004 requires reporting institutions to send a letter to the borrower about the implications of reporting to the eCIB, and to allow a reasonable time period (at least 15 days) for reconciliation or settlement of overdue liabilities. Under the OGCC, Section 6.8, the card issuer is responsible for correcting erroneous information provided to the eCIB, or any other approved credit bureau, within a reasonable time. SBP does not make corrections to the system at the request of a borrower: Banks are solely responsible for data accuracy, and only the reporting institution is able to alter information about a borrower. Updates in the borrower's record are made every 10 days, although overdue amounts that have been settled are cleared the following month. Neither corporations nor individuals are able to obtain their own credit reports. A comprehensive law called the Credit Bureaus Act is in the process of promulgation. The proposed law further elaborates all issues in the area of consumers' rights.
Recommendation	SBP should enable companies and individuals to obtain their own credit reports and to dispute inaccurate information. It will be important to ensure that the good practices outlined above are incorporated into the new Credit Bureaus Act.
SECTION E	**DISPUTE RESOLUTION MECHANISMS**[3]
Good Practice E.1	***Internal Complaints Procedure***

[3] This section is based on the state of affairs at the time of the mission. Subsequently, a new Federal Ombudsmen Institutional Reforms Act, 2013, was promulgated that may have repercussions on the Banking Ombudsman of Pakistan. See box 1 and volume I for further details.

	a. Every bank should have in place a written complaints procedure and a designated contact point for the proper handling of any complaint from a customer, with a summary of this procedure forming part of the bank's terms and conditions referred to in B.7 above and an indication in the same terms and conditions of how a consumer can easily obtain the complete statement of the procedure. **b. Within a short period of time following the date a bank receives a complaint, it should** **(i) acknowledge in writing to the customer/complainant the fact of its receipt of the complaint; and** **(ii) provide the complainant with the name of one or more individuals appointed by the bank to deal with the complaint until the complaint either is resolved or cannot be processed further within the bank.** **c. The bank should provide the complainant with a regular written update on the progress of the investigation of the complaint at reasonable intervals of time.** **d. Within a few business days of completing the investigation of the complaint, the bank should inform the customer/complainant in writing of the outcome of the investigation and, where applicable, explain the terms of any offer or settlement being made to the customer/complainant.** **e. The bank should also inform the customer/complainant of the availability of a financial ombudsman services or other form of alternative dispute resolution.** **f. When a bank receives a verbal complaint, it should offer the customer/complainant the opportunity to have the complaint treated by the bank as a written complaint in accordance with the above. A bank should not require, however, that a complaint be in writing.** **g. A bank should maintain an up-to-date record of all complaints it has received and the action it has taken in dealing with them.** **h. The record should contain the details of the complainant, the nature of the complaint, a copy of the bank's response(s), a copy of all other relevant correspondence or records, the action taken to resolve the complaint, and whether resolution was achieved and, if so, on what basis.** **i. The bank should make these records available for review by the banking supervisor or regulator when requested.**
Description	Under BPD Circular No. 17 dated June 7, 2004, detailed "Guidelines in dealing with Customers Complaints" were issued. Under the guidelines, banks are required to put in place a comprehensive complaint redressal mechanism and are required to designate an appropriate senior person to deal with complaints. Banks must display in all branches and on their websites the complaints process, and provide leaflets to customers on request. In addition to requiring the appointment of a designated officer responsible for complaint handling, banks are required to set up a complaint redressal system for identification and classification of complaints, to ensure proper investigation and an expeditious resolution within a specified timeline. Complaints must be responded to within 10 working days. Where a complaint requires further investigation, an interim reply must be sent, indicating the reasons for the time to be taken and expected

	date of action/response. In any case, the final reply may be sent within 45 working days, barring cases where reasonable grounds exist for not complying with the 45-day limit. Banks are required to maintain statistics on complaints, including volume, types, and settlement, and should analyze the data and prepare periodic reports. Complaint data as prescribed under the guidelines is reviewed by internal audit and onsite inspection teams of SBP. SBP inspection teams evaluate related mechanisms and efficient handling, but a general reporting requirement is not in vogue, except that BPRD Circular Letter No. 25 dated August 26, 2009, requires banks to report utility bill complaint data on a monthly basis to the state bank. Banks must also report incidents of fraud and forgeries to SBP. SBP maintains its own database of complaints received from bank customers and scrutinizes the data from an operational risk perspective for internal analysis and also to formulate policy initiatives for consumer protection. SBP policies are in conformity with all aspects of E.1 above, with the exception of E.1 f. There appears to be no requirement that banks treat verbal complaints on the same basis as written complaints. However, discussions with banks during the mission indicated that they generally did so.
Recommendation	SBP may wish to consider clarifying that banks should treat verbal complaints on the same basis that they treat written complaints.
Good Practice E.2	***Formal Dispute Settlement Mechanisms*** **a. A system should be in place that allows customers of a bank to seek affordable and efficient recourse to a third-party banking ombudsman or equivalent institution, in the event the complaint of one or more of customers is not resolved in accordance with the procedures outlined in E.1.** **b. The existence of the banking ombudsman or equivalent institution and basic information relating to the process and procedures should be made known in every bank's terms and conditions referred to in B.7.** **c. At the request of any bank customer, the bank should make available to the customer the details of the banking ombudsman or equivalent institution, and its applicable processes and procedures, including the binding nature of decisions and the mechanisms to ensure the enforcement of decisions.** **d. The banking ombudsman or equivalent institution should be appropriately resourced and discharge its function impartially.** **e. The decision of the banking ombudsman or equivalent institution should be binding upon the bank against which the complaint has been lodged.**

Description	In addition to the Consumer Protection Department at SBP, the Office of the Banking Mohtasib Pakistan (ombudsman) operates under Section 82 of the BCO. The recently created Karachi Center for Dispute Resolution can also act as a mediator in bank disputes. Section 71 of the Payment Systems and Electronic Fund Transfer Act, 2007 provides that consumers may address complaints to State Bank of Pakistan. If a client does not obtain resolution of his or her grievance from his or her bank within 45 days, he or she may refer the matter to the ombudsman (OBM). Decisions of the OBM may be appealed by consumers to SBP governor (Section 82 of the BCO) or ultimately to the courts, but are binding on banks. Timelines are specified for resolution. Most disputes that go to the ombudsman are settled through an amicable resolution process, but roughly 20 percent are settled at a hearing held by the OBM. The OBM handled 20,322 complaints between its founding in 2005 and 2011. The position of the ombudsman, which is appointed by the president on the recommendation of SBP governor, remained vacant for approximately eight months - creating a serious backlog at OBM – before an appointment was made in March, 2013. Under BPRD Circular Letter 18 dated August 10, 2010, banks are directed to inform customers about the OBM—in English and Urdu—on all bank statements. In addition, public service messages have been published in widely circulated newspapers across Pakistan to increase consumer awareness. In spite of these efforts, awareness of the OMB and its procedures, although improving, appears to be inadequate. Roughly two-thirds of those using the service do not comply with the formal procedure and have to be guided through the process by the OBM. Furthermore, a large number of complaints are directed to the CPD of SBP, which then redirects the complaints to the concerned financial institution or the OBM for follow-up. This indicates that consumers are not fully aware of the process to be followed. The OMB is funded by levies charged to banks, and is adequately staffed and funded. Services are provided free of charge to consumers.
Recommendation	A new ombudsman needs to be appointed as soon as possible. If allowed by law, the authorities should put in place a system to ensure that there will always be an acting ombudsman in the event of a vacancy in the office, through either delegated powers or the automatic appointment of an interim ombudsman. Consideration should be given to proactively increasing awareness of the OBM, and streamlining procedures to make them more user-friendly. SBP, the OBM, and/or the PBA should consider conducting a more proactive campaign through the media and other channels to increase awareness.
Good Practice E.3	***Publication of Information on Consumer Complaints*** **a. Statistics and data of customer complaints, including those related to a breach of any code of conduct of the banking industry, should be periodically compiled and published by the ombudsman, financial supervisory authority, or consumer protection agency.**

	b. Regulatory agencies should publish statistics and data and analyses related to their activities in respect of consumer protection regarding banking products and services so as to, among other things, reduce the sources of systemic consumer complaints and disputes. **c. Banking industry associations should also analyze the complaint statistics and data and propose measures to avoid the recurrence of systemic consumer complaints.**
Description	The OBM publishes an annual review of complaints it handles. Further, under Section 82 G of the BCO, the Office of Banking Mohtasib shall send a report to the State Bank of Pakistan on or before March 31 in every succeeding year, setting out a review of the activities of its office during the preceding year. The Banking Mohtasib shall also submit a report or reports to the State Bank of Pakistan containing the results of such inquiries as it may be directed to conduct by the state bank from time to time. All reports submitted by the Banking Mohtasib shall be published and released to the public unless it directs otherwise (in such cases, the reasons are to be recorded). The Consumer Protection Department of SBP annually reviews the data related to complaints and proposes policy measures to enhance the level of consumer protection. However, they do not publish any data or analysis. Individual banks also maintain statistics, analyze the data, and produce reports for bank senior management. However, the PBA does not do so.
Recommendation	There is a need to centralize, analyze, and publish data on consumer complaints. There is a wealth of data available on consumer complaints, but the data are dispersed among individual banks, SBP, the OBM, and provincial councils. The OBM publishes statistics and analyzes complaints it receives to determine if there are issues that require policy attention. The CPD also analyzes data on consumer complaints it receives and prepares an annual review. Findings are used for internal analysis, and the CPD has taken several policy initiatives on the basis of conclusions drawn from the findings. This annual review is not made public, however, and the data analyzed are not comprehensive. A comprehensive and public analysis of all financial consumer complaints would allow regulators and banks to better identify and address recurring problems and areas of weakness in banking practices. This may be an appropriate role for the CPD of SBP.
SECTION F	**GUARANTEE SCHEMES AND INSOLVENCY**
Good Practice F.1	***Depositor Protection*** **a. The law should ensure that the regulator or supervisor can take**

	necessary measures to protect depositors when a bank is unable to meet its obligations including the return of deposits. **b. If there is a law on deposit insurance, it should state clearly** **(i) the insurer;** **(ii) the classes of those depositors that are insured;** **(iii) the extent of insurance coverage;** **(iv) the holder of all funds for payout purposes;** **(v) the contributor(s) to this fund;** **(vi) each event that will trigger a payout from this fund to any class of those insured; and** **(vii) the mechanisms to ensure timely payout to depositors who are insured.** **c. On an ongoing basis, the deposit insurer should directly or through insured banks or the association of insured commercial banks, if any, promote public awareness of the deposit insurance system, as well as how the system works, including its benefits and limitations.** **d. Public awareness should educate the public on, among other things, the financial instruments and institutions covered by deposit insurance, the coverage and limits of deposit insurance, and the reimbursement process.** **e. The deposit insurer should work closely with member banks and other safety-net participants to ensure consistency in the information provided to consumers and to maximize public awareness on an ongoing basis.** **f. The deposit insurer should receive or conduct a regular evaluation of the effectiveness of its public awareness program or activities.**
Description	The State Bank of Pakistan Act provides SBP a wide range of corrective measures in the event a bank conducts operations without due regard to safety and soundness or fails to comply with the BCO and SBP's Prudential Regulations. Such measures include, depending on the circumstances: (i) imposition of a directive; (ii) replacement of the board of directors and senior managers; (iii) imposition of a moratorium on a bank's operations pending its restructuring; (iv) removal of a bank's license to conduct banking business; and (v) effecting the exit of bank from the industry through the seeking of a winding-up order. In recent years, SBP has acted to resolve a number of smaller distressed banks using a variety of the methods available. If offsite surveillance or onsite inspection indicate signs of widespread weaknesses and the affairs of any banking company being conducted in a manner detrimental to the interests of the depositors or in a manner prejudicial to the interests of the banking company, the state bank, under the terms of Section 41 of the BCO, can remove and supersede the board of directors. The state bank publishes reports on the performance and stability of financial sector on a half-yearly basis. Further, banks are required to have themselves rated by credit rating agencies on the approved panel of the State Bank of Pakistan and disclose their credit rating prominently in their published annual and quarterly financial statements. Banks are required to have their financial

	statements audited by external auditors on the panel maintained by the state bank for the purposes of auditing banking companies under Section 35 of the BCO and submit them to the state bank. Submission of wrong or misleading information leads to action against banks and auditors under the provisions of the BCO. Under the Banks (Nationalization) Act, 1974, all bank deposits are protected by the government. This provision was introduced at the time when the banks were nationalized, and is no longer appropriate in a system that is largely privately owned. It is also not clear that the GOP would be in a position to honor this guarantee in a timely and orderly manner in the event of a failure of one or more large banks. The mission understands that a draft law establishing an explicit deposit protection scheme (DPS) to provide protection to small depositors was drafted some time ago, but has not been submitted to parliament.
Recommendation	There is a need to clarify the position on depositor protection through appropriate legislation. The proposal outlined in SBP's "10-Year Strategy Paper" for creating a DPS would appear to be an appropriate solution for Pakistan. A deposit insurance system should limit the scope for discretionary decisions, promote public confidence, help to contain the costs of resolving failed banks, and provide for an orderly process for dealing with bank failures. The law should specify how the system is to be funded on a sustainable basis, as well as its obligations to depositors, and needs to be part of a well-constructed financial system safety net. It would need to be supported by a high level of public awareness about its existence, benefits, and limitations.
Good Practice F.2	***Insolvency*** **a. Depositors should enjoy higher priority than other unsecured creditors in the liquidation process of a bank.** **b. The law dealing with the insolvency of banks should provide for expeditious, cost-effective, and equitable provisions to enable the maximum timely refund of deposits to depositors.**
Description	Depositors enjoy higher priority than other creditors, under Section 58 of the BCO, at the time of suspension of business and winding up of a banking company. The BCO, Section 58, deals with bank insolvency. In addition, SBP has prepared a Problem Bank Manual that explicitly lays down a hierarchy of actions to be taken in cases of problem banks. These measures range from informal to strict formal actions (cancellation of license and liquidation of the bank). In practice, there have been no instances of the latter, so the insolvency framework remains untested. In the past, problem banks have typically been resolved through recapitalization or amalgamation. As noted above, under the law (Bank Nationalization Act, 1974) all bank deposits remain under government guarantee.
Recommendation	The new Deposit Protection Act should provide for expeditious, cost-effective,

	and equitable refund to depositors in the event of insolvency. If the Deposit Protection Act is enacted, the BCO and Bank Nationalization Act would need to be amended accordingly.
SECTION G	**CONSUMER EMPOWERMENT (SEE VOLUME I, FINANCIAL EDUCATION)**
Good Practice G.3	***Unbiased Information for Investors*** **a. Financial regulators should provide, via the Internet and printed publications, independent information on the key features, benefits, and risks—and where practicable the costs—of the main types of financial products and services.** **b. Nongovernmental organizations should be encouraged to provide consumer awareness programs to the public regarding financial products and services.**
Description	a) SBP does not provide, either via the Internet or through printed publications, independent information on the key features, benefits, risks, or costs of financial products and services. It is the view of SBP that this is a role for the media, consumer organizations, or the bankers' association rather than the regulator. However, in Pakistan, none of these organizations currently fulfill this role. b) Pakistan does not currently have a system of consumer NGOs that are actively engaged in consumer protection in financial services, although one or two consumer protection NGOs look into financial services from time to time. One such NGO conducted and published a study on banking industry competition in 2010.
Recommendation	To the extent feasible, SBP should encourage NGOs to become more actively engaged in financial services, by, among other things, engaging with them on consumer protection issues and consulting with them when considering new guidelines, rules, and regulations in this area. A new system of consumer nongovernmental organizations is needed in particular to serve heavily indebted households. Consideration should be given to the role of nonprofit financial advisors (such as the credit counseling center in operation in Malaysia), which can help indebted people sort out their debts and provide them with necessary counseling. These organizations should also be encouraged to keep records of the cases they receive, conduct trend analysis of this data, and propose changes in legislation where appropriate.
SECTION H	**COMPETITION AND CONSUMER PROTECTION**
Good Practice H.1	***Regulatory Policy and Competition Policy***

	Regulators and competition authorities should be required to consult one another for the purpose of ensuring the establishment, application, and enforcement of consistent policies regarding the regulation of financial services.
Description	The Competition Commission of Pakistan (CCP) works under Competition Act, 2010. The act sets out the principles and norms of sound competitive behavior as well as the manner in which these norms are to be enforced. The CCP has across-the-board sanction powers including over the financial sector, as provided under Competition Act, 2010. In practice, the CCP may consult and seek clarifications from SBP as the major regulator of financial sector.
Recommendation	The CCP and SBP should consider establishing an MOU that outlines the respective roles and outlines a consultative process to be followed.
Good Practice H.2	***Review of Competition*** **Given the significance of retail banking to the economy as a whole and to the welfare of consumers, competition authorities should** **(i) monitor competition in retail banking;** **(ii) conduct, and publish for general consumption, periodic assessments of competition in retail banking (such as the range of interest rates across banks for specific products); and** **(iii) make recommendations publicly available on enhancing competition in retail banking.**
Description	The CCP does not systematically monitor competition in retail banking, but it has analyzed specific aspects and taken action. The CCP may undertake such an initiative under its broader mandate.
Recommendation	The CCP may wish to consider undertaking and publishing periodic assessments and comparative information about retail banking products.
Good Practice H.3	***Impact of Competition Policy on Consumer Protection*** **The competition authority and the regulator should evaluate the impact of competition policies on consumer welfare, especially regarding any limitations on customer choice and collusion regarding interest and other charges and fees.**
Description	At SBP, it is an ongoing process to ensure fair trade practices and a level playing field for all stakeholders, so that no class of consumers is put in a disadvantageous position due to particular circumstances or practices. Although the broader context of such evaluations is based on consumer welfare, it is assessed on a qualitative basis for negative or positive impact rather than on a quantifiable level.
Recommendation	The evaluation of the impact of competition policies could be incorporated into the MOU between SBP and CCP, with respective roles and responsibilities.

2. Microfinance providers: Good Practices

SECTION A	CONSUMER PROTECTION INSTITUTIONS
Good Practice A.1	***Consumer Protection Regime*** **The law should provide clear consumer protection rules regarding microfinance providers,[4] and there should be adequate institutional arrangements to ensure the thorough, objective, timely, and fair implementation and enforcement of all such rules, as well as of sanctions that effectively deter violations of these rules.** **a. There should be specific statutory provisions that create an effective regime for the protection of consumers of microfinance providers.** **b. There should be a government authority responsible for implementing, overseeing, and enforcing consumer protection in the area of microfinance providers.** **c. The supervisory authority for microfinance providers should have a register that lists the names of microfinance providers.** **d. There should be coordination and cooperation among the various institutions mandated to implement, oversee, and enforce consumer protection and financial sector regulation and supervision.** **e. The law should provide for, or at least not prohibit, a role for the private sector, including voluntary consumer associations and self-regulatory organizations, in respect of consumer protection in the area of microfinance providers.**
Description	General assessment: The consumer protection regime for microfinance providers is in many respects ineffective because of its fragmentation and incompleteness, which leave a significant portion of the microfinance clients uncovered and another portion only partially protected. A large part of the microfinance sector is not under the purview of any financial authority with regulatory and enforcement powers and does not need to follow minimum standards. There is a lack of coordination among authorities and other bodies with regard to the desirable protection regime for microfinance clients. Microfinance clients are less protected than bank clients and have fewer options to resolve grievances. Microfinance service providers (MSPs) adopt a variety of legal forms: microfinance banks (MFBs), microfinance institutions (MFIs), and rural support programs (RSPs). MSPs operate under separate laws implemented by different federal agencies and provincial governments. The non-regulated sector is comprised of nonprofit organizations (MFIs and RSPs) and cannot mobilize deposits. MFIs and RSPs are not regulated and supervised by any financial authority. There are nine MFBs, but the exact number of MFIs and RSPs is not known.[5] While MFBs must comply with consumer protection regulations issued by the State Bank of Pakistan (SBP), MFIs and RSPs fall exclusively under the general

[4] Throughout this assessment, we use the term "microfinance providers" to refer generically to providers of microfinance, both banks and nonbanks.

[5] Among the members of the Pakistan Microfinance Network (PMN), there are 15 MFIs and 5 RSPs.

consumer protection laws implemented by the provincial governments (see description of the provincial consumer protection laws in volume I), the Competition Ordinance, and voluntary codes of conduct. This leaves MFI/RSP clients less protected than clients of MFBs, and bank clients more protected than all microfinance clients.

The primary laws relevant to microfinance and consumer protection of microfinance consumers are listed in the table below.

Law	Relevance to microfinance
Microfinance Institutions Ordinance, 2001 (hereafter MFB Ordinance[6])	Defines MFBs and MFIs, but applies only to MFBs. It contains a few rules relevant to consumer protection. The MFB Ordinance is implemented by SBP.
Societies Registration Act, 1860, and related provincial regulations	Governs MFIs constituted as charitable societies and implemented by provincial governments. There are no provisions directly related to consumer protection.
Companies Ordinance, 1984	Governs MFPs constituted as limited liability companies and registered with the Securities & Exchange Commission of Pakistan (SECP). There are no provisions directly related to consumer protection. SECP is responsible for implementing the ordinance and has regulatory powers defined in the ordinance.
Voluntary Social Welfare Agencies (Registration and Control) Ordinance, 1961, and related provincial regulations (e.g., Voluntary Social Welfare Agencies [Registration and Control] Rules 1962, Government of Punjab)	Governs MFPs constituted as welfare agencies and registered by the provincial governments (e.g., Directorate General of Social Welfare of Punjab). Has a few provisions related to consumer protection, but it is not directly relevant for this diagnostic.
Trust Act, 1882	Governs MFPs constituted as trusts. There are no directly relevant provisions for protection of microfinance clients.
Provincial consumer protection laws (see full description of such laws in volume I) (e.g., Punjab Consumer Protection Act, 2005, and Punjab Consumer Protection Rule, 2009. Other provincial laws such as usury	The provincial consumer protection laws apply to all MFPs. For instance, the Punjab Consumer Protection Act, 2005, sets liability of the service provider, duty of disclosure, and prohibition on exclusions from

[6] Although the ordinance is called "the Microfinance Institutions Ordinance," this document will use the term "MFB Ordinance," to avoid confusion, because the ordinance is not applicable to MFIs, but only to MFBs.

	laws (e.g., the Punjab Usurious Loans Ordinance, 1959, and the Punjab Relief of Indebtedness Act, 1934)	liability; it defines unfair practices and establishes the Consumer Protection Council and the Consumer Courts of Punjab.
	Competition Act, 2010	Prohibits anticompetitive practices and creates the Competition Commission of Pakistan (CCP), which is responsible for its implementation. This law applies to all financial institutions, including MFPs. It has provisions relevant to consumer protection, such as prohibition of discriminatory pricing and deceptive marketing.
	Banking Companies Ordinance (BCO) and related regulations	The BCO (or any other law relating to banking companies or financial institutions) does not apply to MFBs or MFIs, unless otherwise stated. An MFB shall not be deemed to be a banking company for the purposes of the BCO, SBP Act, or any other law or regulation relating to banking companies. However, some provisions of the BCO, such as those related to bank secrecy and the winding up of institutions, apply to MFBs and are relevant for consumers.
	Payments and Electronic Fund Transfers Act, 2007	Sets some protection provisions for payment instruments and payments and electronic fund transfers. Applies to any entity providing such services.

The provincial consumer protection acts apply to all financial service providers, including MFBs and MFIs/RSPs. However, they lose relevance in practice, as they do not have provisions specific for financial services, being clearly focused on manufactured goods and other services. Moreover, only Punjab has passed regulations (Punjab Consumer Protection Rule, 2009) to implement the consumer protection act through the establishment of the Consumer Protection Council and Consumer Protection Courts.

The legal framework for MFIs/RSPs is fragmented, which might affect the achievement of policy goals for microfinance. MFPs other than MFBs are believed to have more than 50 percent of the total number of clients of the microfinance sector. The laws under which MFIs and RSPs are incorporated set different frameworks for the company's statutory organization (i.e., ownership structure, governance, reporting requirements, accountability, and profit-sharing arrangements), creating a fragmented framework in which microfinance services are offered to Pakistani consumers, leaving a good part of the sector without the obligation to follow common consumer protection and conduct standards. For

	instance, there are no standards for microcredit operations undertaken by MFIs and RSPs, similar to those applicable to MFBs. There are no minimum disclosure and transparency standards for them either. There is some concern, by some stakeholders, that the lack of common standards might drive the industry to a crisis such as the delinquency crisis of 2008–09 faced by one of Pakistan's largest MFIs. In addition, this fragmentation may have long-term implications, such as on MFPs' ability to attract investors and access infrastructure such as the banking courts. Ultimately, it results in a good portion of the sector being outside the scope of any financial policy or supervisory authority, which can limit the country's ability to achieve the stated policy goals for the microfinance sector and for an inclusive financial system. The most important policy document for the microfinance sector in Pakistan, the Strategic Framework for Sustainable Microfinance in Pakistan, was issued by SBP in January 2011, setting a vision to transform microfinance into a "dynamic industry, integrated with the overall financial system, which provides inclusive financial services to the underserved economic and geographic segments through self-sustaining business models and demand driven products, while maintaining high standards of governance and service delivery, supported by agile regulatory environment."[7] To achieve such goals, common standards for protecting consumers will need to be established across currently regulated and unregulated providers. Only MFIs and RSPs incorporated under the Companies Ordinance are registered with SECP. SECP does not regulate or supervise MFIs/RSPs registered under Section 42 of the Companies Ordinance. Although MFIs and RSPs are not regulated or supervised by SBP, they are defined in the MFB Ordinance as institutions that extend microcredit and allied services to the poor through sources other than public savings and deposits. The MFB Ordinance prohibits MFIs from using the expressions "microfinance bank" and "MFB" on their names and from taking deposits without an MFB license. Contraventions are punishable with imprisonment and fines. Where it appears to SBP that a person is carrying on the business of an MFB, SBP may give directions, conduct inspections, retrieve books and information, and exercise other powers such as removing directors. Only MFBs are regulated and supervised by SBP, under a dedicated regulatory framework. Microfinance banks (MFBs), which account for nearly 50 percent of borrowers and 60 percent of total outstanding microcredit,[8] are regulated and supervised by SBP. MFBs hold only a small portion of total bank deposits. All MFBs must be licensed by SBP under the MFB Ordinance.[9] The ordinance uses the term "microfinance institution" in its title and several articles. However, it is clear that the legislators' intent was to refer to MFBs, not to MFIs, in nearly all provisions. The current text of the ordinance could be interpreted to mean that

[7] Strategic Framework for Sustainable Microfinance in Pakistan, January 2011, available at www.sbp.org.pk/MFD/Strategic-Framework-SM-24-Jan-2011.pdf. This framework supersedes the 2007 national microfinance strategy and is based on a diagnostic of the state of the industry*, compared with the milestones set in the 2007 document, which were only partially achieved.*

[8] Pakistan Microfinance Review, 2011, Pakistan Microfinance Network.

[9] The Khushali Microfinance Bank was initially created and governed by its own 2000 ordinance, until that was revoked. Khushali MFB is now operating under the MFB Ordinance.

MFIs are subject to the provisions of the ordinance, including the need to obtain a license from SBP and to follow the standards imposed on MFBs.

An MFB is defined in the MFB Ordinance as an institution licensed by SBP that must render assistance to microenterprises and provide microfinance services in a sustainable manner to low-income persons, preferably women, with a view to alleviating poverty. Low-income persons are defined as those with an annual household income less than PRs 600,000. In an attempt to keep MFBs targeted on poor segments of the population, SBP has limited loan sizes in accordance with the table below.

Type of loans	Type of borrower	Maximum loan size
Housing loan	With household annual income up to PRs 600,000	PRs 500,000 (at least 60 percent of the portfolio must be of loans below PRs 250,000)
General loan	With household annual income up to PRs 300,000	PRs 300,000
Microenterprise loan (only MFBs that meet minimum capital requirements are authorized to extend this type of loan)	Microenterprise is defined as a project or business in trading, manufacturing, services, and agriculture that leads to livelihood improvement and income generation, undertaken by self-employed individuals, or those that employ up to 10 individuals (excluding seasonal labor)	PRs 500,000 (at least 60 percent of the portfolio must be loans below PRs 150,000)

The MFB Ordinance is complemented primarily by the Prudential Regulations for Microfinance Banks, 2007 (PRMFB). In addition, some circulars and other regulatory or legal instruments apply to MFBs, which are mostly focused on matters other than consumer protection.

The main SBP regulations applicable to MFBs or to microfinance undertaken by other regulated institutions are listed in the table below.

Regulatory Instrument	Topics covered
PRMFB (updated March 2012)	Focuses on prudential and operational requirements for MFBs, and has a few consumer protection provisions.
Microfinance Credit Guarantee Facility (MCGF) Guidelines (Circular 03, 2012)	Establishes the MCGF, administered by SBP. The MCGF is available to MFBs and MFIs seeking financing from banks and development finance institutions (DFIs).

Licensing Requirements and Guidelines for Setting up MFBs	Explains minimum requirements for MFIs or others applying for an MFB license.
Branch Licensing Policy and BPRD Circular No. 15, 2007	Sets minimum physical, security, and other requirements for branches of MFBs. SBP assesses, before approving branch expansion plans of MFBs, the convenience and needs of the population of the area to be served. There are a few provisions related to consumer protection.
Guidelines for Islamic Microfinance Business by Financial Institutions	Establishes rules for Islamic microfinance business by financial institutions.
Guidelines for Commercial Banks to Undertake Microfinance Business	Establishes rules for microfinance business undertaken by commercial banks.
NGO Guidelines	Guidance for NGOs considering applying for an MFB license.
BPRD Circular No. 9, 2007	Guidelines on outsourcing for banks and DFIs. Outsourcing arrangements must ensure they do not reduce the protection afforded to depositors or investors, and must not be used to avoid regulatory compliance.
Branchless Banking Guidelines, 2007	Sets guidelines for the use of branchless banking channels and basic provisions to protect customers using these channels.

The Competition Commission of Pakistan has jurisdiction over all businesses in Pakistan, including MFPs. It deals with some issues directly related to consumer protection. The CCP was created by the Competition Ordinance, 2007, but it does not conduct prudential or consumer protection supervision. However, it has legal authority to

- initiate proceedings and make orders in cases of contravention of the provisions of the Competition Ordinance;
- conduct studies for promoting competition;
- conduct inquiries into the affairs of any undertaking (including financial service providers) in Pakistan;
- to give advice to undertakings so that their businesses are conducted according to the Competition Ordinance;
- to engage in competition advocacy; and
- take any other action necessary for carrying out the purposes of the Competition Ordinance, including giving orders, entering and searching premises, imposing penalties in case of noncompliance with the ordinance or orders, and requesting information.

The CCP's advocacy mandate allows it to, among other things, review policy frameworks for fostering competition and making recommendations for

amendments to the Competition Ordinance and any other law that affects competition in Pakistan (Competition Ordinance, Section 29). Financial institutions aggrieved by the CCP's decisions can appeal to the Appellate Bench of the Commission. With such a broad mandate, the CCP may have an increasing role in the overall framework for protection of microfinance consumers, and has expressed interest in doing so, particularly with regard to deceptive marketing (it has launched a nationwide campaign to increase consumer awareness against deceptive marketing) and consumer agreements.

SBP has constituted the Microfinance Consultative Group (MFCG), with representation from the Ministry of Finance, the Pakistan Poverty Alleviation Fund (PPAF), and microfinance investors active in Pakistan, with the intent to discuss the industry's long-term goals and related policy strategy. The MFCG has, for instance, ratified SBP's Strategy for Sustainable Microfinance in Pakistan. There are no stated goals in the strategy specific to consumer protection, and the issue of legal and institutional fragmentation has not been addressed by the MFCG.

1. **Assessment: There is institutional and legal fragmentation with regard to MFIs and RSPs.**

MFIs and RSPs do not follow a common legal framework and are not under the supervision and regulation of any financial authority. Part of the sector is registered by SECP, but that body acts solely as a registrar, not as a financial regulator and supervisor. According to the Companies Ordinance, SECP would have investigative and regulatory powers in some limited circumstances, and it has broad investigative powers and power to revoke licenses in some circumstances (when the business of the MFI/RSP is conducted with the intent to defraud any person or is not in accordance with sound business principles or prudent commercial practices, and when the financial position of the company endangers its solvency). SECP has power to initiate action against managers in many situations. The licenses of nonprofit organizations, in particular, are granted subject to regulations SECP may issue, although this has not been done in practice.

The interviews conducted for this diagnostic indicate that SECP has been considering using such prerogatives to regulate and supervise MFIs/RSPs registered under Section 42 of the Companies Ordinance. So far, no concrete action has been taken. It is not clear whether bringing MFIs and RSPs under SECP is the best alternative to improve protection of microfinance consumers in Pakistan. Extending SECP's mandate to regulating and supervising consumer protection in MFIs/RSPs would require supervisory and regulatory capacity (knowledge, expertise, staff, budget) that SECP may not have and may not be able to gain at least in the medium term, despite its regulatory and supervisory mandate regarding insurance and securities markets. Moreover, SECP has historically considered MFPs as charity or welfare concerns with supervision regimes similar to those for nonprofits working in nonfinancial sectors and may not be familiar with financial or market conduct supervision of these institutions.

	The CCP has expressed interest in influencing the microfinance sector as well, and even issuing regulations under its broad mandate to foster competition in the markets (e.g., rules against deceptive marketing and sales practices). Although regulated MFBs are expected to account for a significant proportion of the microfinance industry going forward, in terms of loan portfolio, in terms of client outreach, MFIs and RSPs are expected to remain relevant.[10] Hence, there is some urgency in setting a clear path for the industry to follow minimum conduct and consumer protection standards based on long-term goals, with the objective of protecting borrowers and the overall health of the industry. **2. <u>Assessment: The regulation of MFBs is fragmented, incomplete, and sometimes unclear with regard to consumer protection. The regime for MFIs and RSPs is inadequate.</u>** The laws covering MFIs and RSPs are not sufficient to provide protection to MFI clients. The provincial consumer protection laws are not enforced in practice and are focused on nonfinancial sectors; the interviews suggest that microfinance consumers, as in other countries, are largely unaware of such laws and their impact on their relationship with microfinance providers. Such laws also do not establish an effective institutional framework in which MFIs/RSPs would be subject to regulation and supervision, and an effective framework for resolving grievances of clients. With regard to MFBs, the regulation pertaining to consumer protection is fragmented and incomplete. Consumer protection topics are dealt with in different regulations dedicated to varied topics, such as credit cards, branch licensing, branchless banking, and payments. Also, the framework lacks depth and breadth to be more effective and provide a greater level of protection to MFB clients, while catering to financial inclusion goals. For instance, there are areas, such as disclosure standards, that have been regulated for the bank sector but not for MFBs. Overall, the framework issued by SBP to protect payment services users is more developed than the framework for basic credit and deposit services. The framework for branchless banking is also more developed (e.g., with regard to complaints resolution), although it is particular to such alternative means of service delivery. There is no consensus within either SBP or the market with respect to the applicability, to MFBs, of some regulations issued for scheduled banks. Some believe circulars and guidelines apply equally to MFBs, others are certain they do not apply. Some interviews suggest that even when regulations are not applicable, compliance is checked in practice by SBP's inspectors, revealing inconsistency between policy and supervisory decisions inside SBP. Some of the regulations issued by SBP for banks with potential relevance to microfinance consumer protection include: • BPD Guidelines 17, 2004, on Dealing with Customer Complaints • BPRD Circular 01, 2012, on Minimum Return on Savings Deposits • CPD Circular 02, 2012, on Sale of Third-Party Products by Banks

[10] Regulating Pakistan's Non-bank Microfinance Institutions. December 2011. Pakistan Microfinance Network.

- BPRD Circular No. 23, 2003, on service charges on deposit accounts
- BPD Circular No. 30, 2005, on basic bank account
- BPRD Circular No. 7, 2011, on Service Charges on PLS Deposit Accounts
- BPRD Circular No. 12, 2011, which prohibits charging for cash handling/deposit services at counters
- BPD Circular Letter No. 21, 2004, and NPD Circular No. 7, 2006, on unclaimed deposits
- BPD Circular No. 7, 2006, on statement of accounts to PLS/current account holders and basic bank account holders
- Prudential Regulations for Consumer Financing, which, among other things:
  - Sets limits and rules for consumer loans, including the need to limit client exposure according to the client's income
  - Sets rules for credit card financing, including rules for unauthorized or wrong transactions
  - Sets rules for auto loans, housing loans, and personal loans
- Operational Guidelines for Credit Card Business in Pakistan

3. <u>Assessment: There is no central registry of microfinance providers (MFIs, RSPs, and MFBs)</u>

At present, it is difficult to find a precise number of existing microfinance providers other than MFBs and outside the members of the Pakistan Microfinance Network. There is no central registry of microfinance providers or a common source of information that compiles updated lists from different bodies for the benefit of the general public. Some interviews suggest there are hundreds of unregistered MFIs/RSPs serving low-income populations in Pakistan, but information about them is scarce and their total number is unknown. The size and relevance of the financial cooperative sector is also unknown. The most accessible source of information for the industry are PMN's reports and website. Although high-quality and relevant, the information is limited to PMN's membership. SBP publishes some information about MFBs in its quarterly *Development Finance Review*.

The Securities & Exchange Commission of Pakistan does not publish an updated list of MFIs/RSPs registered under the Companies Ordinance. Likewise, SBP does not publish online a list of all licensed MFBs. Although the State Bank of Pakistan Act 1956 (SBP Act) requires SBP to maintain in all its offices and branches an up-to-date list of licensed banks, there is no such requirement for MFBs in the MFB Ordinance. According to the interviews conducted for this diagnostic, SBP maintains a list of licensed MFBs in its offices and any person may obtain access to it upon request. It would be useful if an up-to-date list was readily available online for any person, company, or investor.

4. <u>Assessment: SBP's authority to regulate consumer protection in MFBs does not emanate from a specific mandate and may be questioned.</u>

The MFB Ordinance empowers SBP to "systematically monitor and evaluate the

	performance of a MFB to ensure that it is complying with the applicable criteria and prudential rules and regulations." With approval of the federal government, SBP may make rules for carrying out the purposes and provisions of the MFB Ordinance. SBP is authorized to make regulations to provide for all matters for which provision is necessary or expedient, for the purpose of giving effect to the ordinance and for efficient conduct of the affairs of an MFB. Any person who contravenes any provision of the MFB Ordinance or any rule, regulation, order, instruction, or condition made, given, or imposed under the ordinance shall be liable to fines (MFB Ordinance, Section 23.3). Some of the fines are determined in the ordinance and some are left to SBP's discretion. SBP may cause inspections and evaluations based on receipt of complaints (MFB Ordinance, Section 21). Finally, where SBP is satisfied that • in the interest of the public; • to prevent the affairs of an MFB being conducted in a manner detrimental to the of the depositors or in a manner prejudicial to the interest of the MFB; • in furtherance of monetary or financial sector policy; or • to secure the proper management of the MFB; it is necessary to issue directions to MFBs generally or to any MFB in particular, it may issue such directions and MFBs shall comply with them. SBP may also remove directors or other managers and make them ineligible for managerial positions in any MFB for up to three years, and supersede the board of directors of an MFB for up to three years. Based on its broad mandate, SBP is regarded as competent to issue consumer protection rules. However, because such powers with regard to consumer protection in MFBs are not explicit, they could conceivably be questioned and therefore would benefit from greater clarity. **5. <u>Assessment: There is insufficient interdepartmental coordination inside SBP with regard to consumer protection in microfinance.</u>** The incomplete and fragmented consumer protection framework for MFBs, as well as the lack of clarity with regard to applicability of existing regulations, is related to insufficient coordination among departments of SBP involved in microfinance: the Banking Policy and Regulations Department (BPRD), the Agricultural Credit and Microfinance Department (ACMFD), the Banking Surveillance Department (BSP), the Banking Inspection Department (BID), and the Consumer Protection Department (CPD). This deficiency is intensified by the lack of clarity regarding the responsibility (among the CPD, BPRD, and ACMFD) for issuing consumer protection regulations for MFBs specifically. The ACMFD is responsible for some aspects of microfinance regulation, but is more focused on agricultural finance and advocacy of financial inclusion, and has not been dealing with consumer protection more specifically (except financial literacy). The ACMFD does not conduct supervision, which is done by the BSD and BID. The BSD, BID, and CPD do not generate new regulatory proposals specifically for MFBs, let alone for consumer protection in MFBs. The information generated by the CPD and BID does not seem to be used by the BPRD or ACMFD on an ongoing basis to set regulatory priorities. All departments, including the ACMFD and CPD, participate in regulatory changes

proposed by the BPRD or any other department, but there seems to be limited awareness of or emphasis on consumer protection in microfinance, and a need to increase consistency between supervision and policy in this area, as well as the need to have a cohesive, comprehensive framework for consumer protection. The ACMFD believes that the current regulation provides an adequate level of protection and that more regulatory action could result in excessive costs for MFBs, frustrating financial inclusion goals. Striking a balance between regulatory protection and compliance costs to spur financial inclusion is a laudable goal, but the current protection framework is not adequate for the particularities of microfinance clients and operations and may negatively impact inclusion goals in the medium and long term.

6. <u>Assessment: There are no self-regulatory bodies with regulatory and enforcement powers.</u>

PMN is the industry association and the main source of information on microfinance in Pakistan. PMN has 27 members[11] among MFBs, MFIs, and RSPs. All MFBs (with the exception of the recently licensed Waseela MFB) and all large MFIs/RSPs are members of PMN. PMN has done a remarkable job in providing reliable information on its membership, including periodic sector performance and trend analyses. It also launched its Consumer Protection Initiative in 2009, with important measures in this regard, including an initiative to assess compliance with PMN's Code of Conduct.

To become a member of PMN, an MFP needs to be in operation for at least a year, have at least 5,000 clients, comply with PMN Code of Conduct, and render information to PMN on a regular basis. PMN reserves the right to, based on a performance review, request members to surrender PMN membership. PMN plays an important advocacy role and has also engaged in projects that benefit both the industry and its clients, such as the national rollout of a credit information bureau dedicated to microfinance (MF-CIB) in 2013.

PPAFPPAF is the leading poverty alleviation agency in Pakistan, operating under the public-private partnership model sponsored by the government of Pakistan and international development organizations. PPAF is by far the largest provider of funding to MFPs, covering institutions approximately 50 percent of the total gross loan portfolio in Pakistan and reaching nearly 900,000 borrowers.[12] PPAF also provides grants for human and institutional development of MFPs. MFP funding constitutes 57 percent of overall PPAF disbursements. In 2011, PPAFPPAF funded 41 MFPs[13] and has maintained a focus on loans to women, who account for 64 percent of all borrowers; 79 percent of PPAF's portfolio is in rural areas.

PPAFPPAF funding to MFPs is concretized through partnership agreements. MFPs applying for funds from PPAF must have a track record of at least two

[11] Pakistan Microfinance Network. www.microfinanceconnect.info/. Accessed January 14, 2013.

[12] Pakistan Poverty Alleviation Fund Annual Report 2011 and information provided by PPAF (it is not clear how the total loan portfolio in Pakistan was calculated, as not all existing MFIs report their financial data).

[13] Pakistan Poverty Alleviation Fund Annual Report 2011.

	years, prove their capacity to grow and expand, have transparent funding structures and proper accounting systems, show bank statements, have internal controls and external audits, and be financially sustainable or on the path of sustainability. They must also have good governance and strong management, and must not be political, discriminatory, ethnic, sectarian, or exclusionary in nature. PPAFPPAF also helps MFPs to access commercial funds through its Program for Increasing Sustainable Microfinance. Today, there are about 50 MFIs funded by PPAF. PPAF plays an important role in imposing and monitoring conduct and financial performance standards of its partners, through its grant and loan arrangements. It has created a code of conduct based on the Client Protection Principles of the Smart Campaign[14] as part of its partnership agreements and the Seal of Excellence for Poverty Outreach and Transformation in Microfinance and has been working to increase awareness of social performance standards in the industry. According to information provided, compliance with this and other terms and conditions is checked annually by PPAF during monitoring activities, which include onsite inspections and reviews of financial information. PPAF has not identified, in the course of such reviews, important consumer issues in MFIs or deviations from its client protection code. In addition to PPAF and PMN, there are a few consumer associations in operation in Pakistan, but they do not focus on financial services and are largely unaware of consumer protection issues in microfinance. Both PMN and PPAF have been playing relevant roles, but neither can be considered a self-regulatory body with a formal mandate. PMN's Code of Conduct is voluntary as long as PMN membership is also voluntary. Besides, there is no enforcement mechanism to make sure the code is being implemented in practice and there are no means to sanction noncompliance. PMN management has recently announced a plan to increase its role in consumer protection, including undertaking monitoring activities to assess compliance with the code of conduct and implementing an ombudsman mechanism for microfinance clients.[15] However, these activities have stalled due to lack of agreement among market participants and relevant regulators, regarding whether an industry association should play such a role, because it could conflict with the interests of PMN members. As the apex institution for the microfinance industry, PPAF has some powers to push for better practices. However, its monitoring actions, although highly relevant, are unlikely to drive long-term adherence to good business practices and a desirable level of consumer protection. PPAF's influence lasts only as long as the financing instrument. Moreover, PPAF does not cover all unregulated MFPs and does not have a formal regulatory and enforcement mandate. **7. <u>Assessment: There is limited coordination among relevant bodies on</u>**

[14]The Smart Campaign is a global effort to unite microfinance leaders around the common goal to keep clients as the driving force of the industry. See http://www.smartcampaign.org.

[15] The PPAF has also been involved in the formulation of the grievance redressal mechanism.

	consumer protection in microfinance. There is a good level of interaction among SBP, PMN, and PPAF on the development goals and vision for the microfinance sector in Pakistan. For instance, these institutions participate and exchange ideas in regular conferences and other forums (such as the Microfinance Consultative Group – MFCG) about microfinance, and have come to a consensus that the industry should work toward reaching financial and social sustainability. There seems to be much less coordination, however, with respect to consumer protection. For instance, no action has been agreed on by the various players to address the important gaps of the current framework, and no solutions or even palliative arrangements have come out of a coordinated effort. They have not been able to, for example, implement a pragmatic solution, even if temporary, to set common standards for consumer protection in MFPs under SBP, PMN, or PPAF. They have also failed to set up a redress mechanism that covers the majority of microfinance clients. Similarly, they have failed to produce and maintain a list of all (or at least the large majority) of MFPs operating in Pakistan. Finally, there is a surprising lack of awareness by relevant stakeholders about consumer issues in microfinance, which might be related to the lack of information sharing and research on this topic. Some undesirable practices are known to exist (e.g., discrimination against women, pass-on of loans from female borrowers to men, unfair collection practices, overlending, and lack of price disclosure), but there is no concrete coordinated action to conduct an assessment of consumer issues in microfinance or take measures to improve business practices across all types of MFPs. Indeed, some interviews suggested that some bad practices, particularly those related to gender and the lack of recourse mechanisms for microfinance clients, are considered acceptable. Also, there is limited coordination on this subject among SBP, PMN, PPAF, SECP, and CCP. Based on various interviews, SECP and CCP seem to be increasing or planning to increase their roles in microfinance. There are discussions (involving other government agencies) about SECP's potential role in regulation and supervision of microfinance. Also, the CCP has expressed interest in issuing specific regulations on deceptive marketing and pricing practices.[16] Without a coordinated effort, such endeavors can end in a less than optimal arrangement, and inconsistent or overlapping initiatives.
Recommendation	1. SBP, SECP, PMN, PPAF, and other relevant authorities should coordinate to conduct an assessment and implement the most suitable and pragmatic institutional arrangements and related coordination mechanisms to address gaps resulting from the fragmentation in microfinance consumer protection.[17] The reforms should not only work to extend rights and protections to unregulated markets, but also lay the ground for the most effective oversight and enforcement mechanism, and a range of nonregulatory measures, including consumer awareness. This will take a good level of coordination among the concerned

[16] See, for instance, the CCP's ruling over ATM and switching charges/fees.
http://www.cc.gov.pk/index.php?option=com_content&view=article&id=249&Itemid=151

[17] The SECP formed a Steering Committee on MFIs in November 2012, consisting of the SECP, SBP, PPAF, and relevant MFIs to consider the development of a viable regulatory framework for MFIs.

	stakeholders. This will require an adequate forum for discussion. This forum could be the existing Microfinance Consultative Group, or a new body to discuss specifically consumer protection in microfinance. PMN and PPAF should continue to play an important role in setting and implementing minimum standards for microfinance, because they have influence over the large majority of the MFI/RSP market. Addressing the institutional and regulatory gaps is the most important challenge to improve consumer protection in microfinance in Pakistan and sustain the healthy growth of this nascent industry. It will affect all the specific regulatory and nonregulatory recommendations of this report, which are made without specifying under which institutional arrangement such recommendations should be implemented. 2. Consideration should be given to clarifying SBP's authority in consumer protection in MFBs in the next amendment of the MFB Ordinance. It would also be useful to provide consistency in the use of the terms "microfinance institution" versus "microfinance bank," which are sometimes used interchangeably in the ordinance. 3. In consultation with the industry and coordination with PMN and PPAF, SBP should strengthen the regulatory framework for MFBs, with regard to consumer risks. It should consider reviewing the existing regulations according to the specific recommendations in this report, and disclose to the market the entire list of regulations issued by the BPRD and other departments that are applicable to MFBs. SBP should more clearly embrace consumer protection in microfinance as a supervisory matter, and increase interdepartmental coordination and information exchange to set supervisory and regulatory priorities as well. The roles of each department involved in consumer protection and microfinance advocacy, regulation, and supervision should be fully clarified. The mechanisms through which such departments exchange information on a regular basis, particularly for the purposes of setting supervisory priorities in consumer protection issues, should be improved and formalized. 4. SBP should publish an up-to-date list of licensed MFBs on its website, to facilitate access to this information and increase awareness of MFBs by the general public and microfinance clients who have access to the Internet. 5. A central registry of all MFIs and RSPs in operation in Pakistan, regardless of their legal status, should be created and an updated list should be kept and be available to the general public, at least online. 6. MFIs and RSPs should be encouraged or required to register with SECP, under Section 42 of the Companies Ordinance.[18]
Good Practice A.2	***Code of Conduct for Microfinance Providers***

[18] According to our consultations, the PPAF has been encouraging their partners to register under the Companies Ordinance, Section 42.

	a. There should be a principles-based code of conduct for microfinance providers devised in consultation with the nonbank microfinance industry and with relevant consumer associations and monitored by a statutory agency or an effective self-regulatory agency. **b. If a principles-based code of conduct exists, it should be publicized and disseminated to the general public.** **c. The principles-based code should be augmented by voluntary codes on matters specific to the industry (credit unions, credit cooperatives, other microfinance providers).** **d. Every such voluntary code should likewise be publicized and disseminated.**
Description	There are no mandatory codes that are monitored by a statutory agency or a self-regulatory body with enforcement powers. Both PMN members and PPAF partners have subscribed to the Client Protection Principles, a principles-based model code adopted by microfinance providers globally.[19] The principles are: (i) appropriate product design and delivery; (ii) prevention of overindebtedness; (iii) transparency; (iv) responsible pricing; (v) fair and respectful treatment of clients; (vi) privacy of client data; and (vii) mechanisms for complaints resolution. All MFBs, being PMN members, have subscribed to the code, but SBP does not have power to enforce voluntary industry codes. There are weaknesses in industry practices related to failures to observe these principles, including those pertaining to breaches of privacy of client data. This indicates that neither PMN, PPAF, nor SBP have effectively monitored adherence to the principles and the voluntary codes. PMN has neither the authority nor the resources to closely monitor each member for compliance with its code of conduct. PMN has made public[20] an upcoming exercise to assess adherence to the Client Protection Principles through member self-evaluations, using a questionnaire based on Smart Campaign's Getting Started Questionnaire. The data from the self-assessments (which is to be carried out by the members' own internal and external auditors) would be compiled by PMN to identify weak client protection practices in the industry, track member compliance, and refine the code over time. A first assessment of the industry, based on these self-assessments, is expected by mid-2014. There is no legal basis for addressing or sanctioning noncompliance. The CCP has a Voluntary Competition Compliance Code that provides guidance to businesses operating in Pakistan. It requires them to establish an internal compliance mechanism to observe the provisions of the Competition Act, 2010. In addition to providing a basic framework for compliance, the CCP's code establishes that the CCP might apply more lenient treatment and reduce penalties to businesses that, though found in breach of the act, show that they have sought compliance with the code in good faith. Businesses interested in adopting the code may do so by registering with the CCP, which has pledged to publish a list

[19] The Client Protection Principles that have been incorporated by the PPAF and PMN were developed by the Smart Campaign. http://www.smartcampaign.org/about-the-campaign/smart-microfinance-and-the-client-protection-principles.

[20] Implementing an Industry Code of Conduct at Pakistan Microfinance Network. 2010. Smart Notes No. 5. October 2010. Pakistan Microfinance Network.

	of participants in its website.
Recommendation	1. The adoption of voluntary codes that are not enforced by a regulatory or self-regulatory body with power to impose sanctions and penalties in case of noncompliance has had limited impact in market practices. SBP should consider checking an MFB's compliance with industry codes to which they have subscribed, in the course of its supervision, and supporting PMN and PPAF in dissemination efforts to increase consumer awareness of the code. It should, at a minimum, require MFBs' internal auditors to include this theme in their evaluations, and review the auditors' reports on a regular basis. 2. Initiatives (like PMN's) that publicize assessments of compliance with industry codes have the potential to spur improvements in market practices, by pinpointing widespread weaknesses or exposing noncompliant entities. SBP should consider undertaking a similar exercise, taking into consideration the existing industry codes to which MFBs subscribe. 3. The SPB, PPAF, and PMN should consider coordinating in order to adopt similar assessment methodologies to check compliance with industry codes. The assessment tool developed by PMN could be a starting point for such coordination.
Good Practice A.3	***Other Institutional Arrangements*** **a. Whether microfinance providers are supervised by a financial supervisory agency, the allocation of resources between financial supervision and consumer protection should be adequate to enable their effective implementation.** **b. The judicial system should ensure that the ultimate resolution of any dispute regarding a consumer protection matter with a microfinance provider is affordable, timely, and professionally delivered.** **c. The supervisory authority for microfinance providers should encourage media and consumer associations to play an active role in promoting consumer protection regarding microfinance providers.**
Description	In the case of MFBs, which are regulated and supervised by SBP, there is no indication that the allocation of resources between financial supervision and consumer protection supervision is inadequate. However, as stated in Good Practice A.1, there is limited awareness about consumer protection issues in microfinance, the need to set specific minimum standards for protecting microfinance consumers, and the need to devise a pragmatic and effective solution to the fragmented institutional and legal framework for microfinance. There is also limited coordination among different departments dealing directly or indirectly with microfinance at SBP, as stated earlier, and there is room for improving clarity with regard to the role of each department. Courts are not commonly used by microfinance clients in Pakistan or other developing countries. They generally have lengthy, expensive, and sometimes complicated processes, making formal dispute resolution through courts too burdensome given the amounts involved in microfinance loans, deposits, and services. However, the law has created a potentially workable solution for formal

	redress mechanisms in Pakistan, the provincial Consumer Courts. The problem is that such courts exist only in Punjab. Moreover, there seems to be little awareness about them in Punjab. There is also little awareness by authorities of the deterrents for microfinance clients seeking redress in general, and formal redress in particular. Such deterrents require further investigation and will need to be addressed in a coordinated effort involving not only the courts in an awareness campaign, but other empowerment measures. SBP has not systematically engaged with consumer associations and the media with regard to consumer protection in microfinance. In the case of microfinance clients, there would be limited value in involving consumer protection associations at this time, given their focus on goods and other nonfinancial services.
Recommendation	1. Following the example of Punjab, the other provinces that have consumer protection acts should consider implementing their own consumer courts to provide affordable, speedy, professional resolution mechanisms to microfinance consumers (see Good Practice E in this chapter). 2. Beyond consumer associations, the concerned stakeholders (SBP, PPAF, SECP, and PMN) should consider engaging with other supporting organizations, such as community groups, mobile network operators, and radio stations, that could help increase awareness of consumer rights when dealing with MFPs, including the right to file complaints with the intent to improve the services received from MFPs.
Good Practice A.4	***Licensing of Microfinance Providers*** **All financial institutions that extend any type of credit to households should be registered with a financial supervisory authority.**
Description	The MFB Ordinance requires MFBs to register with SECP as companies under Section 42 of the Companies Ordinance, 1984, and be licensed by SBP. MFBs must operate in accordance with the regulations issued by SBP and the terms and conditions of the license granted by SBP. For instance, SBP shall satisfy itself, by an inspection, that the affairs of the MFB are not being, and are not likely to be, conducted in a manner detrimental to the interests of its members and present or future customers. SBP has full supervisory powers over MFBs, based on each license granted. In addition, all MFBs need to comply, on an ongoing basis, with prudential requirements such as liquidity levels, capital adequacy ratios, reserves, and other requirements established from time to time by SBP. All MFBs must meet minimum entry requirements. During licensing, SBP reviews the MFB's business plan, financial projections, and description of the products, services, and delivery channels, which should all be based on market surveys. There is no specific requirement with regard to policies to comply with consumer protection regulations or codes of conduct. In addition, sponsors, board members, and MFB managers are all subject to fit and proper tests. For instance, members of a political party or government officials do not qualify to own an MFB. SBP has provided additional guidance and requirements for MFIs/RSPs applying

	for an MFB license (NGO Guidelines). Usually, only an institution that has demonstrated experience as MFI/RSPs for at least three years can apply for an MFB license. However, SBP states that in exceptional circumstances, it may consider applications from other persons with extensive exposure to or experience with micro, agriculture, or small and medium enterprise lending, or another related area. No person or group will be granted permission to operate more than one MFB. All MFBs shall start operations within six months of the granting of the license. SBP may cancel or suspend an MFB license under certain circumstances. MFIs and RSPs are not subject to licensing or a common registering authority. Only MFIs and RSPs constituted as limited liability companies must register with SECP under Section 42 of the Companies Ordinance ("Associations not for profit").[21] MFPs registered with SECP are subject to all requirements applicable to other limited liability companies, with the exception that they do not need to use the word "limited" in their names. For example, MFIs are required to file changes to their memorandum/articles of association with SECP within 90 days of the change (Sections 24 and 25). According to Section 42(1), the license is granted on such conditions and subject to such regulations as SECP thinks fit, and those conditions and regulations shall be binding on the association and shall, if SECP so directs, be inserted in the memorandum/articles of the MFI. Although this provides seemingly broad regulatory power, SECP in practice acts exclusively as a registrar, and the conditions and regulations are primarily related to the formalities of the company's memorandum/articles of association and procedures intended to protect a company's members and creditors. They do not set financial performance or business conduct standards. The license may at any time be revoked by SECP, if it decides the company is not conducting its business appropriately for a not for profit company. Other MFPs operating under a variety of legal forms under different laws are not required to be licensed or registered by any financial supervisory authority. They are registered by different provincial registry authorities and do not follow common registration, operational, or reporting standards.
Recommendation	All MFPs in Pakistan should be required to at least register with a financial supervisory authority, which has the power to set requirements for registration, such as for minimum disclosure and financial reporting. Registration does not necessarily mean subjecting all registered entities to the same supervisory intensity, scope, and depth. Most likely, not all MFPs will require prudential supervision, and some will be subject only to monitoring but not to supervision. This approach is adopted, for instance, by the National Bank of Cambodia, as well as by the Bank of Mozambique, which divide the supervision of microfinance providers according to their size, scope, and market relevance.
SECTION B	**DISCLOSURE AND SALES PRACTICES**

[21] The Companies Ordinance Section 14(1) requires all partnerships or companies consisting of more than 20 persons, formed for the purpose of carrying on any business in Pakistan, to be registered as a company under the ordinance. This obligation does not apply to joint family businesses (Section 14(2)[b]).

Good Practice B.1	***Information on Customers*** **a. When making a recommendation to a consumer, a microfinance provider should gather, file, and record sufficient information from the consumer to enable the institution to render an appropriate product or service to that consumer.** **b. The extent of information the microfinance provider gathers regarding a consumer should** **(i) be commensurate with the nature and complexity of the product or service either being proposed to or sought by the consumer; and** **(ii) enable the institution to provide a professional service to the consumer in accordance with that consumer's capacity.**
Description	Disclosure regulation for MFBs is highly fragmented and at times unclear. There is not a single regulation dealing with disclosure, or a regulation dealing with consumer protection or transparency issues. Disclosure rules are spread across different regulations dealing with varied topics, such as the Prudential Regulations for Microfinance Banks, the Branch Licensing Guidelines, the Operational Guidelines for Credit Cards (OGCC), and the Branchless Banking Guidelines. These regulations focus on products, channels, or services, not on a topic such as disclosure. MFBs are subject to a few regulations setting minimum information that needs to be gathered and recorded. First, PRMFB, Section 17, sets documentation requirements for anti-money-laundering and combating the financing of terrorism (AML/CFT) purposes. There is no specific requirement that such information be commensurate with the nature and complexity of the product or service, although SBP has implemented a risk-based approach to AML/CFT requirements according to the risk of each account or transaction. The PRMFB determines that MFBs need to obtain copies of a client's national identity card, passport, or driver's license, and certify, by stamping the copy, that it was verified against the original document. In remote areas and for microfinance clients who lack identity documents, particularly women, the MFB may establish other appropriate means to verify the identity of the client. This diagnostic is not able to conclude whether such alternative methods are being used in practice and there is some indication that, at least in the case of women, they are not. The Operational Guidelines for Credit Cards (OGCC (Section 2.4), when applicable to MFBs, requires collection of a written application and verification of the client's identity through reference such as the NADRA database. The client's needs assessment in a loan operation is usually done by all types of MFPs, through an analysis of the household economy and financial flows, and the economic activity that is in need of financing. Traditionally, an MFP applies a labor-intensive process of visiting the household and the family business, and sometimes conducting interviews with community leaders or acquaintances, to assess the client's payment capacity and willingness, and financing needs. The depth or even the adoption of all phases of this procedure depends on each MFP, but in all cases less formal documentation is gathered about the client, when compared with traditional banking loan documentation. The documentation and

	background information produced by the microfinance methodology is expected to give the MFP a thorough understanding of the client's needs and capacity, but the adherence to the principle of suitability and affordability depends on the policies of each MFP. PRMFB Regulation 15 requires MFBs to implement appropriate pricing to ensure access to affordable financial services by the poor as well as the operational and financial sustainability of MFBs. PRMFB Regulation 11 requires MFBs to monitor the level of indebtedness of their clients, including by obtaining a written declaration from the client detailing the credit facilities he or she has, before extending a loan. MFBs must ensure a client's exposure does not exceed her or his repayment capacity. MFBs shall obtain a credit report from SBP's Credit Information Bureau (CIB) or any other appropriate bureau of which they are members. Put together, these provisions create a good framework for MFBs to assess the client's payment capacity, without imposing burdensome and inflexible procedures on the MFB. It is common knowledge in Pakistan that there is multiple borrowing by microfinance clients, particularly in urban areas. MFPs tend to concentrate on the same areas and focus on the same clients. There is less information available, though, as to whether such multiple borrowing is generating overindebtedness. Specific research in this field is lacking. The advent of the credit bureau for the microfinance sector (see Good Practice D.2 in this chapter) should help shed some light on this topic. Many stakeholders interviewed believe that multiple borrowing exists because MFPs fail to design adequate, suitable products that cater to the specific needs of each client. Instead, they tend to offer standardized products and limit themselves to assessing the clients' payment capacity rather than trying to meet their financing needs. Even in individual lending (as opposed to group lending), the options of products are limited and the terms and conditions are highly standardized (including payment schedules). These practices are common in Pakistan and elsewhere and are the core of commercial microfinance. However, lack of product flexibility and innovation may be causing clients to use multiple borrowing sources which, in addition to increasing transaction costs for clients, may facilitate over-indebtedness. SBP has introduced some flexibility by permitting MFBs to offer larger loans to microenterprises. In addition to weak product design, there are some worrisome practices in Pakistan that go against the suitability and fair treatment principles. MFIs and RSPs (more often) and MFBs (less often) lend primarily to women, for reasons such as pressure from donors and set gender-related targets. However, this policy faces challenges in cultures where women's access to finance can be exploited by close male relatives or husbands. The client assessment is based on the woman's creditworthiness and the household financial situation, as is usual in microfinance. The problem is that the loan is often used in another activity, by a

	male related to the female borrower, such as the husband. The pass-on of loans in Pakistan was documented in 2012 World Bank research.[22] The report shows evidence that microfinance loans do not always benefit women borrowers, who are given the loans only to comply with gender targets set by international funders or the provider itself. Men, who need loans, including those who have defaulted in the past, use women to access credit. Between 50 percent and 70 percent of microloans to women in Pakistan may actually be used by their male relatives, and a good part may be used in businesses in which the female borrower has no participation or from which she does not benefit indirectly. According to our interviews, all stakeholders acknowledge this practice, which seems to be widely accepted. MFBs, which are under the prudential supervision of SBP, are less prone to follow this practice, given its potential negative impact on the credit risk of the microcredit portfolio, and because the practice infringes the PRMFB requirement for loans to be extended in the name of the entrepreneur, to ensure traceability and reduce multiple borrowing (PRMFB Regulation 10). Indeed, if the beneficiary of the loan is not the registered borrower, the assessment of the borrower's creditworthiness becomes less relevant. This has consequences for the institution's risk profile. According to information gathered in this diagnostic, SBP onsite inspectors may be discouraging the pass-on of loans. The PRMFB also subjects borrowers who use their loans for any purpose other than that for which the loan is granted to penalties of fine and imprisonment. The combination of this provision with the prevalent practice puts women MFB borrowers in a very vulnerable position where they bear the risk (and its legal consequences), while not having control over the use of the loan. As a result, MFBs tend to lend more to men, reflecting more closely the reality of Pakistan's cultural gender bias and the fact that men tend lead family businesses. There are no regulations for MFIs and RSPs besides the broad goal of suitability embedded in the client protection principles. The practice of passing on loans raises important issues not only on suitability of microfinance products and services, but also on the quality of MFPs' loan and client monitoring systems, and therefore the quality of their financial management and internal controls. And, if the creditworthiness of the real beneficiary of the loan is not being rightly assessed, this practice also contradicts the efforts by PMN to implement a credit bureau for the microfinance sector. This scenario has deep implications for the achievement of the policy goals defined by both SBP and PMN of constructing a fair, healthy, consumer-oriented microfinance sector. In addition to the pass-on of loans, another gender-related practice in Pakistan goes against consumer protection principles advocated by PMN and PPAF. It is not uncommon to find discriminatory loan approval processes and requirements adopted by all types of microfinance providers, including MFBs. It is usually much more difficult for women entrepreneurs, and single and widowed women, to access microfinance loans on an individual basis. One of the discriminatory requirements is for women to present one or two male guarantors, while female

[22] The research, titled "Are Pakistan's Women Entrepreneurs Being Served by the Microfinance Sector?" can be found at http://siteresources.worldbank.org/EXTFINANCIALSECTOR/Resources/282884-1339624653091/8703882-1339624678024/Format_Pakistan_women_entrepreneurs_10-16-12.pdf.

	guarantors are not accepted in most cases. This might be one of the explanations for the relatively low percentage of women microentrepreneurs who are microfinance borrowers in Pakistan (less than 25 percent according to the World Bank study). According to the study, such discriminatory lending practices force Pakistan's women entrepreneurs to seek informal funding sources such as informal savings, personal assets, and family loans. Another deterrent for women to access and use loans and file complaints with the MFP is the low number of female MFP personnel interacting with the overwhelming majority of female borrowers. Female personnel could listen to and understand women borrowers more easily, helping the MFP to provide more suitable products, avoid discriminatory practices, and monitor the use of the loan to avoid pass-ons. Some interviews suggest that it might be dangerous for female staff to work in some areas, but this is not believed to be a widespread problem.
Recommendation	1. SBP should consider consolidating existing disclosure rules into a comprehensive regulation, to ensure clarity and cohesiveness. It should also consider evaluating whether it is necessary to amend the Branchless Banking Guidelines or other regulations to ensure that disclosure standards apply when branchless banking is use for service delivery. 2. The regulation issued by SBP should be more specific on the need for MFBs to design and implement their own internal policies to ensure product suitability and fair treatment, in addition to affordability. This should cover client documentation, loan approval processes, and client monitoring after the loan is granted. The regulation should prohibit discriminatory practices against women and other groups. Adherence to such policies should be checked by SBP in the course of its supervisory review, which needs to be strengthened to reduce or eliminate practices such as the passing on of loans from women borrowers to men. Ideally, MFIs and RSPs should follow similar rules. They should have policies that are consistent with the client protection principles to which they subscribe, particularly the principle of product suitability. They should be subject to some form of monitoring for adherence to such rules and principles, by a financial supervisory authority or other body with formal enforcement powers. 3. Resolving the gender issues in microfinance in Pakistan will take more than regulatory measures and will demand a continuous, long-term commitment, including awareness efforts to empower women and discourage men from using loans taken by women. The relevant stakeholders should consider forming a working group to deal with gender and protection issues in microfinance, involving the industry, regulators, policymakers, and representatives of civil society. 4. Additional research on the reasons, forms, and consequences of multiple borrowing should be conducted, to help SBP, PMN, PPAF, and MFPs in their efforts to avoid over-indebtedness. A definition of over-indebtedness could also be explored, to serve as a reference.

	5. MFPs should exercise greater flexibility to offer differentiated products that fit the financing needs of clients, without jeopardizing the business case of each offer and the company's financial sustainability. MFPs should also, to the extent possible, hire, train, and support more female staff, because a large share of clients are women and the interaction between staff and customers could run more smoothly. Clients may feel more comfortable with female staff.
Good Practice B.2	***Affordability*** **a. When a microfinance provider makes a recommendation regarding a product or service to a consumer, the product or service it offers to that consumer should be in line with the need of the consumer.** **b. Sufficient information on the product or service should be provided to the consumer to enable him or her to select the most suitable and affordable product or service.** **c. When a microfinance provider offers a new credit product or service that significantly increases the amount of debt assumed by the consumer, the consumer's creditworthiness should be properly assessed.**
Description	In microfinance, financial advice about products and services is not common, particularly in markets dominated by group lending methodology. MFPs usually limit themselves to guiding the client on how to use the loan, the client's rights and obligations, the payment schedule, the payment method, and the consequences of defaulting. This is consistent with the lower level of sophistication of the microfinance clientele and the simplicity and inflexibility of microfinance products and services. Although MFIs and RSPs are not subject to any enforceable regulation, the PRMFB Regulation 30 requires MFBs to help the public make informed decisions. MFBs shall make adequate efforts to educate their clients on important terms and conditions of all their products, including loans and savings, while fully disclosing the lending and deposit rates in annualized percentage terms in signed contracts and documents. The MFB staff should also read these terms in front of their clients. MFBs must display important terms and conditions prominently at their branches. In addition, MFBs shall educate customers about the charges as well as customer's obligations in respect of other services such as ATMs and microinsurance (PRMFB Regulation 30). MFPs in Pakistan present varied levels of transparency and effectiveness in their disclosure practices. Some MFPs post prices, terms, and conditions visibly in their offices and in their marketing materials, whereas others do not. Some use interest rates over the declining loan balance, whereas others use flat interest rates. Some MFPs use an effective interest rate containing all charges and costs incurred by the borrower in a loan operation (e.g., loan application fee, monthly account handling fees, and the insurance premium). Others disclose rates that include only a few items and disclose other items separately or do not disclose them at all. Some do not disclose to the customer that the loan is covered by an insurance policy whose premium is being charged directly to the client.

	There are no standardized formats and formulas for all MFPs to follow, and no specific standard formulas to calculate and disclose costs and returns of microfinance products and services. The lack of industry standards makes it difficult for microfinance clients to compare prices and conditions across different providers. PMN is coordinating with PPAF to conduct a review of product pricing practices in Pakistan, with MFTransparency.[23] The exercise aims to provide important information on how and how much MFPs charge their clients. This could support additional guidance, regulatory, and supervisory efforts toward improved transparency and disclosure. For instance, based on the findings of MFTransparency, PMN plans to implement standard formulas and a standard format for price disclosure within its membership. SBP has not created a specific regulatory measure to institute standard disclosure formats, and believes the existing regulation is sufficient to provide an adequate level of protection to consumers. PPAF also does not require any standardized disclosure formats by its partners. Similarly, there are no standard formats for loan agreements and other consumer contracts, with the exception of rules for credit card contracts, set out in the OGCC, and the standards for payment services set out in the Payment Systems and Electronic Funds Transfer Act, 2007 Sections 26 and 29. Loan agreements and account opening agreements are often long documents, with small print and complex language, making it very difficult for the average microfinance customer to understand. Whether contracts need to be long will depend on legal traditions, but in Pakistan, there are no common standards for highlighting important terms and conditions in long contracts. This is done, for instance, in Mexico, where the most relevant terms of the usually extremely long contracts need to be bolded and in much bigger font, so the consumer can easily identify the key terms of the operation.[24] Lastly, there are no regulations or standards with regard to minimum and prohibited clauses in the consumer agreements. Standards for consumer contracts for payment services are set in the Payment and Electronic Funds Transfer Act, Section 30. This states that the language must be clearly understood by the consumer and must include the consumer's liability for unauthorized transactions, the phone number for the fraud department, what types of transactions the consumer is allowed to conduct and related charges, the consumer's right to stop payment of preauthorized transfers and to receive information, and the liabilities of the service provider. The CCP is interested in regulating consumer contracts in the financial sector, defined as those standardized contracts over which the consumer usually has little influence. This has already been done in other sectors. Regulators and industry bodies will need to coordinate to set common and appropriate standards

[23] MicroFinance Transparency is an international nongovernmental organization that promotes transparency by facilitating microfinance pricing disclosure, offering policy advisory services, and developing training and education materials for all market stakeholders. http://www.mftransparency.org.

[24] In Mexico, these standards are set by the financial consumer protection agency, Condusef. http://www.condusef.gob.mx.

	in the whole microfinance industry, to avoid issuing conflicting guidance. The microfinance methodology traditionally relies on the promise of future larger loans as an incentive for loan repayment. It is expected that, when offering a bigger loan to a client, all MFPs will reassess the client's payment capacity. In practice, this varies from MFP to MFP; some may decide not to conduct the assessment again, particularly when the next bigger loan is within the indebtedness capacity originally set for that client. As a result, MFPs may overlook new loans and other financing that the client may have contracted in the meantime. MFIs and RSPs do not need to follow any regulation, but are supposed to abide by the broad client protection principles related to affordability and suitability embedded in the codes of conduct to which they subscribe. There is no specific rule for MFBs offering new bigger loans to existing clients, but the regulation requires them to assess the client's capacity in all cases. The intensity and depth of such assessment will depend on the MFB's own internal policies, but all MFBs are subject to the same minimum requirements and to SBP's supervisory review. Also, MFBs must develop policies, to be approved by their board of directors, for rescheduled and restructured loans (PRMFB Regulation 13).
Recommendation	1. The concerned authorities (at minimum, SBP, SECP, and CCP), in coordination with PMN and PPAF, should develop minimum common standards disclosing price and other terms and conditions, including the need to post relevant information in places of business, consumer contracts, and marketing materials. SBP may wish to evaluate whether it is necessary to amend the Branchless Banking Guidelines or other regulations to ensure disclosure standards are also applicable when branchless banking channels are used. The standards should be common for all MFPs, regardless of whether they are regulated by a financial authority or not, to allow consumers to compare across different providers. There should be some level of standardization of terms and expressions used by MFPs in marketing materials and in their consumer agreements. There should be common methods and formulas to calculate effective interest rates and rates of return. It is preferable that MFPs use the declining balance method to charge interest from their borrowers, which is a much fairer method than the flat rate. There should be explicit guidance with regard to prohibited contractual clauses, including in accessory products such as credit life insurance, and minimum clauses that should be in all contracts. 2. All MFPs should be required to reassess the payment capacity of the borrower when offering a new larger loan, at least by consulting a credit bureau, to make a sound judgment regarding the borrower's indebtedness level and any change since the client's creditworthiness was last assessed. 3. Authorities should devise an oversight scheme to effectively monitor MFPs' compliance with the recommended minimum standards, including by MFIs and

	RSPs.
Good Practice B.3	***Cooling-off Period*** **a. For financial products or services with a long-term savings component, or those subject to high-pressure sales contracts (unless explicitly waived by the consumer in writing), a microfinance provider should provide the consumer a cooling-off period of a reasonable number of days (at least three to five business days) immediately following the signing of an agreement between the institution and the consumer.** **b. On his or her written notice to the microfinance provider during the cooling-off period, the consumer should be permitted to cancel or treat the agreement as null and void without penalty to the consumer of any kind.**
Description	The practice of allowing a cooling-off period is not as common in microfinance as in banking and insurance services. This is a reality not only in Pakistan, but globally, including in more developed markets, such as Bolivia and Peru. This is related to the more usual short-term, inflexible nature of microfinance loans and other financing instruments offered by microfinance providers. It is also related to the prevalence, in some markets including Pakistan, of group lending methodologies, which make cooling-off periods more difficult to implement without increasing the costs and the uncertainty considerably, or at least breaking the logic of the group lending methodology. The interviews conducted for this diagnostic indicate that some MSPs offer a cooling-off period of up to two weeks, allowing the client to cancel a loan agreement without incurring additional penalties other than losing the loan application fee and any other upfront fee charged by the MSP. However, this practice seems ad hoc and informal, adopted in case the client seeks cancellation, rather than being part of the disclosed terms and conditions of the loan agreements. This subject has not found consensus in publications about microfinance consumer protection regulation globally, but there are strong arguments in favor of establishing cooling-off periods and procedures—at least for individual lending, and for other types of services provided by MSPs, such as deposit accounts, insurance, mobile money accounts, and investment products, if any. For cooling-off periods to be effective in microfinance, they need to be longer than three to five days, given the longer distances microfinance clients typically need to travel to get to the microfinance provider should that be necessary, and also the relatively higher opportunity costs in spending partial or full working days in dealing with financial services providers to cancel a transaction. Also, the procedures for customers to cancel their operations during the cooling-off period should not be unduly burdensome or complex. Clients should be able to easily request cancellation, without being dragged into unnecessary bureaucratic procedures (e.g., writing a signed letter to the head office to explain the reasons for desisting) and should be in consonance with the methods and channels used by the MFP to sell the product (e.g., if clients are able to buy a product through a retail or mobile money agent and sign electronic contracts, they should also be able to cancel their operations using the same channels and electronic means).

Recommendation	The concerned authorities and stakeholders may wish to consider requiring MFPs to offer a cooling-off period on their loan, insurance, and savings services, during which clients can cancel the operation without any penalty or additional fee. The period should allow enough time for the microfinance client to benefit from it in practice, taking into consideration the context in which the products are offered and in which the clients operate. The establishment of a common cooling-off period and guidance for its implementation could be agreed to among SBP, PMN, PPAF, and industry. An oversight arrangement for monitoring compliance could be developed. The existence and terms of cooling-off periods should be effectively disclosed to clients in a timely manner.
Good Practice B.4	***Bundling and Tying Clauses*** **a. As much as possible, microfinance providers should avoid the use of tying clauses in contracts that restrict the choice of consumers.** **b. In particular, whenever a borrower is required by a microfinance provider to purchase any product, including an insurance policy, as a precondition for receiving a loan, the borrower should be free to choose the provider of the product and this information should be made known to the borrower.** **c. Also, whenever a microfinance provider contracts with a merchant as a distribution channel for its credit contracts, no exclusionary dealings should be permitted.**
Description	Section 3 of the Competition Act, 2007, prohibits tie-ins—where sales of the service are made conditional on the purchase of another service—when it prevents, restricts, reduces, or distorts competition. There are no specific requirements by SBP, besides Regulation 30 of the PRMFB, which states that MFBs are required to educate their customers about the charges as well as a customer's obligations in respect of services like microinsurance. Likewise, PPAF does not set common standards for the disclosure of compulsory credit life insurance and there is no specific guidance from PMN. Requiring microfinance borrowers to acquire an insurance policy to cover the debt amount in case of the borrower's death (and other situations, depending on the insurance policy) is a widely adopted practice in Pakistan and other countries. The credit life insurance premium is typically 1 to 2 percent of the loan value, paid once with the payment of the loan application fee and other upfront costs imposed on the client. In Pakistan, there is little transparency of the items included in the upfront costs, including bundled insurance. Some MFPs do not even disclose to their client that they are paying an insurance premium. There is also lack of transparency, in some instances, with regard to the terms and condition of the insurance coverage, which vary depending on the insurance provider. Moreover, the diversity of types of insurance coverage used by different providers, in a context where disclosure is not standardized to facilitate comparison, makes it hard for microfinance clients to shop around or refuse insurance coverage if she or he has another policy covering the same events (not very common, but possible), or to decline to enter into the loan agreement altogether, because of the insurance cost.

	Lastly, the insurance coverage is often tied to an exclusive arrangement with a particular insurance provider, and the client is not free to choose the insurer. In some cases, the MFP does not even hire an insurance company; instead, it builds up a fund to self-insure and requires the client to accept the coverage in order to get the loan. This is also a common practice in microfinance in other countries, although less common than making an arrangement with an insurer. However, there are a very few cases where, in a more competitive microinsurance market, the microfinance provider is able to offer options with regard to the insurer, or at least the coverage type. The use of retailers for the distribution of microfinance services is an emerging market in Pakistan. MFBs are more actively involved in different types of branchless banking, including the use of agent networks. There are no regulatory obstacles for MFBs to share their agents with other MFBs or even other financial institutions, but the current practice is to have exclusivity arrangements between agent networks and MFBs, due to agreements between the MFB and the agent network manager (often a mobile network operator). Given the initial stage of development of agent networks in Pakistan, it is premature to take any regulatory action to encourage the sharing of retail networks by several MFPs. Prohibiting exclusive arrangements could jeopardize the initial investment in and further development of such networks.
Recommendation	1. SBP should establish and implement a standardized disclosure format (see Good Practice B.5) that includes and increases transparency of all upfront fees, including bundled insurance. MFBs should be required to disclose the basic terms and conditions of mandatory credit life insurance. MFBs should also be required to check whether the client has any other insurance policy with similar coverage, to avoid unnecessary double coverage and related costs. SBP should consider working with SECP's insurance department to (i) conduct an assessment of the microinsurance industry (credit life insurance and others) to decide whether it is feasible to require MFBs to provide more than one option for insurance coverage when signing microcredit agreements; and (ii) to review other relevant practices in microinsurance to protect the client, such as prohibiting or at least minimizing exclusions in policies and simplifying policies.[25] 2. Similar standards and practices should be adopted by MFIs and RSPs, and an effective monitoring scheme to ensure compliance with the standards should be developed.
Good Practice B.5	***Key Facts Statement*** **a. Microfinance providers should have a Key Facts Statement for each**

[25] The SECP issued draft microinsurance regulations that touch on this and many other relevant points for protecting microinsurance clients. Subsequently, SECP has issued Microinsurance Rules in February 2014. See Microinsurance Rules at http://www.secp.gov.pk/notification/pdf/2014/SRO_116_Microinsurance_Rules_20140219.pdf and the consultation paper at http://secp.gov.pk/corporatelaws/doc/MI_Consultation_09102012.docx

	type of account, loan, or other products or services. **b. The Key Facts Statement should be written in plain language, summarizing in a page or two the key terms and conditions of the specific financial product or service, and allowing consumers the possibility of easily comparing products offered by different institutions.**
Description	MFBs are subject to a few disclosure and sales practice requirements, whereas MFIs and RSPs are not subject to any regulation outside the very broad principles of the provincial consumer protection laws. For instance, the Punjab Consumer Protection Act creates the Duty of Disclosure for service providers (Section 16), but it is not specific enough to be relevant for this analysis. MFBs are required by the PRMFB to assist the public in making informed decisions and educate clients on the terms and conditions of products, including loans and savings. Lending rates must be disclosed as an annualized percentage rate. MFBs must also display important terms and conditions of the products on the entrance or window of their branches and educate consumers on the charges as well as obligations regarding services like ATM and microinsurance. The Payment Systems and Electronic Funds Transfer Act, 2007 Section 29, sets requirements for disclosure of fees and charges in electronic payment channels, such as ATMs. There is no specific guidance on the type and format (beyond being an annualized percentage rate) of the disclosures required by regulation. There is no mention of other types of disclosure, such as the contact number for complaints (except for credit cards in the OGCC), the ability of the client to repay a loan before maturity, the existence of a cooling-off period, or information about compulsory microinsurance. In practice, the quality of the information provided to consumers and the materials used by MFIs, RSPs, and MFBs vary widely across the industry, making it difficult for clients to have a full understanding of the cost, terms, and conditions of products, and to compare different options. Disclosure of effective rates or total cost of loans is rare, as is the full disclosure of upfront costs and other important terms and conditions, such as mandatory insurance coverage. Key Facts Statements are not used in Pakistan. There are no requirement by SBP for MFBs to use a common, standardized statement, to allow the client easy access to the key characteristics of microfinance products. Likewise, there are no standards set by PPAF or PMN. There appears to be inadequate awareness, by SBP, SECP, and PPAF of the weaknesses in disclosure practices in microfinance, how they affect clients, and what could be done to improve the level of client protection. As mentioned previously, the MFTransparency pricing study being coordinated by PMN will shed some light about disclosure practices in Pakistan and will provide valuable information for future minimum disclosure standards. So far there has been no concerted effort by relevant authorities and industry representatives to develop common disclosure formats such as Key Facts Statements (KFSs).
Recommendation	1. All MFPs should strengthen disclosure by developing and adopting common KFSs for the most relevant microfinance products. SBP should develop regulations requiring a standardized KFS for MFBs. All other MFPs should

	adopt KFSs, with support and pressure from PMN and PPAF. KFSs should have plain language and highlight the key characteristics of the main microfinance products, using standard methodologies to calculate and disclose total costs and returns. KFSs should be handed or made available through other forms (e.g., electronically) to the client at the appropriate moment, before contract signing. Clients should be able request additional guidance from MFP personnel to fully understand the KFSs. It is important to note that a KFS model that works for commercial banking customers will not necessarily work for microfinance clients. Ideally, the KFS for microfinance will be developed in consultation with the industry, and will also be consumer-tested, through field surveys. There should be an effective monitoring scheme to check whether KFSs are being used and in the right manner. 2. SBP should evaluate whether it is necessary to amend the Branchless Banking Guidelines or other regulations to ensure that Key Facts Statements are properly used when branchless banking schemes and other third parties (such as sales agents) are used for service delivery.
Good Practice B.6	***Advertising and Sales Materials*** **a. Microfinance providers should ensure that their advertising and sales materials and procedures do not mislead customers.** **b. All advertising and sales materials should be easily readable and understandable by the general public.** **c. Microfinance providers should be legally responsible for all statements made in advertising and sales materials (i.e., be subject to the penalties under the law for making any false or misleading statements).**
Description	With regard to MFBs, the only specific applicable regulation on marketing and sales material is in the Operational Guidelines for Credit Cards, Section 1 (see description in Good Practice C.4). The Competition Ordinance, 2007, Section 10, prohibits deceptive marketing, defined as including the following: • Distribution of false or misleading information to consumers, including the distribution of information lacking a reasonable basis or related to the price, character, method or place of production, property, suitability for use, or quality of goods; and • False or misleading comparison of goods in the process of advertising. The Punjab Consumer Protection Act describes some prohibited unfair practices, such as false, deceptive, or misleading representation (Section 21 and 22). There are no regulations from SBP setting minimum standards for advertising and sales materials used by MFBs, and no guidance from PMN and PPAF, other than the general client protection principles to which MFIs and RSPs subscribe. The above framework provides only principles-based guidance, but there are no

	specific regulatory requirements such as the calculations and type of price disclosure, and disclosures about cooling-off periods, important contact numbers (e.g., the complaints handling unit at the MFP), and so forth.
Recommendation	1. SBP should issue specific regulations dealing with advertising and sales materials to prohibit misleading statements and require full disclosure of key product characteristics and costs, to the extent possible, using standardized formulas and formats consistent with those used in Key Facts Statements and consumer contracts. SBP should consider incorporating some useful provisions from the Operational Guidelines for Credit Cards. 2. MFIs and RSPs should be subject to similar standards to those applicable to MFBs. 3. All sectors should be subject to a monitoring scheme that ensures effective enforcement of the standards.
Good Practice B.7	***General Practices*** **Specific rules on disclosure and sales practices should be included in the microfinance providers' code of conduct and monitored by the relevant supervisory authority.**
Description	There are no specific rules in the Client Protection Code of Conduct adopted by PMN members and the code adopted by PPAF partners. A principles-based code is limited to encourage transparency, without being specific on desirable or prohibited market and sales practices. Moreover, neither PMN nor PPAF have statutory power to enforce their codes.
Recommendation	1. When specific common standards for disclosure in microfinance are developed, as recommended in Good Practices 1-6, the principles-based codes adopted by PMN and PPAF should be updated and complemented to require completeness, accuracy, and fairness of marketing and sales materials. 2. SBP should consider monitoring compliance with industry codes, by MFBs. 3. All MFPs, including MFBs, should be subject to an effective and formal monitoring scheme that ensures compliance with such codes.
Good Practice B.8	***Disclosure of Financial Situation*** **a. The relevant supervisory authority should publish annual public reports on the development, health, strength, and penetration of the microfinance providers, either as a special report or as part of the disclosure and accountability requirements under the law that governs these.** **b. Microfinance providers should be required to disclose their financial information to enable the general public to form an opinion regarding the financial viability of the institution.**
Description	The MFB Ordinance requires MFBs to have their accounts audited annually by auditors approved by SBP according to the Chartered Accountants Ordinance,

	1961. Within three months of the end of the financial year, the audited accounts shall be published in a daily newspaper of wide circulation in the area of operation of the MFBs, and be submitted to SBP. SBP does not publish financial reports of MFBs, but publishes consolidated financial and performance analysis of the microfinance sector in its *Development Finance Newsletter*. MFBs do not appear as a separate segment in SBP's *Financial Stability Report*, which focuses on banks and development financial institutions. In addition to these public disclosures, MFBs are subject to regulatory reporting requirements set in the PRMFB (Regulation 27), such as biweekly cash reserve requirements and statutory liquidity requirement statements, along with a statement of affairs, and quarterly financial data. MFIs and RSPs registered under Section 42 of the Companies Ordinance are required to submit financial reports on an annual basis to SECP. They are not required to publish this information and SECP does not publish it and does not produce any analytical report about these markets. MFIs constituted under other laws, and therefore not registered with SECP, do not follow any regulatory or legal disclosure requirement. PPAF partners are required to report their financials to PPAF, but this information is not made public. MFIs registered under the Voluntary Social Welfare Agencies Ordinance, 1961, must file their financial statements and annual report with the Registration Authority at the close of each financial year. They should also publish such documents. The annual report should include information on the following: • General management • Nature and extent of services rendered in the year • Program for next year • Audited accounts The largest MFIs operating in Pakistan report their financial information to the Mix Market, but this reporting is voluntary and not based on any legal requirement. Finally, PMN requires its members, regardless of being MFBs, RSPs, or MFIs, to report their financial and social performance information on a yearly basis. Based on this material, PMN provides the richest source of information on the microfinance sector in Pakistan.
Recommendation	All MFPs should be required to report to a financial authority at least once every year, and such information should be made available to the general public through easily accessible platforms such as the Internet, and through analytical reports and studies conducted or commissioned by a designated financial authority.
SECTION C	**CUSTOMER ACCOUNT HANDLING AND MAINTENANCE**
Good Practice C.1	***Statements*** **a. Unless a microfinance provider receives a customer's prior signed**

	authorization to the contrary, the microfinance provider should issue, and provide the customer with, a monthly statement regarding every account the microfinance provider operates for the customer. **b. Each such statement should (i) set out all transactions concerning the account during the period covered by the statement; and (ii) provide details of the interest rate(s) applied to the account during the period covered by the statement.** **c. Each credit card statement should set out the minimum payment required and the total interest cost that will accrue if the cardholder makes only the required minimum payment.** **d. Each mortgage or other loan account statement should clearly indicate the amount paid during the period covered by the statement, the total outstanding amount still owed, the allocation of payment to the principal and interest, and, if applicable, the up-to-date accrual of taxes paid.** **e. A microfinance provider should notify a customer of long periods of inactivity of any account of the customer and provide reasonable final notice in writing to the customer if the funds are to be transferred to the government.** **f. When a customer signs up for paperless statements, such statements should be in an easy-to-read and readily understandable format.**
Description	MFBs are not required to provide monthly statements to clients on their deposit or loan accounts. The PRMFB is silent with regard to statement of accounts. The Branch Licensing Guidelines, Section 9.4, requires MFBs to provide a statement of accounts to their clients at regular intervals, even if the services are rendered through mobile branches. There is no specific requirement for statements to be paper-based, and their frequency is also up to each MFB. The Payment and Electronic Funds Transfer Act, Section 33, requires institutions to provide a monthly statement of payment accounts, which can be electronic. Such statements should clearly set forth the balances and the account at the beginning and the close of the period, and the amount of any fee charged. However, this requirement does not seem to apply to deposit and loan accounts handled by MFBs. Although it is not clear whether BPD Circular No. 8, 2006, applies to MFBs, in practice most MFBs follow the requirement for banks to provide a statement of accounts every six months. MFBs offering mobile phone–based services usually offer more frequent statements in electronic form. There are no specific requirements with regard to the items that need to be in the statements or to the language that is used (e.g., language that is easily understood, and if/how abbreviations are permitted). MFIs and RSPs are not allowed to issue credit cards, but MFBs are. They seem to be subject to the OGCC.[26] The OGCC, Section 4, requires issuers to send a monthly statement of account to credit card holders at least 15 days before the due date. It is allowed to use electronic formats, if they have appropriate security

[26] According to interviews, the Operational Guidelines for Credit Card Business in Pakistan, issued by SBP's Payment System Department, apply to MFBs, despite the fact that the guidelines do not mention MFBs at all.

	measures. In case the client lodges a complaint that the statement has not been sent, the issuer is required to send a statement in no more than two days. In addition to statements, credit card issuers need to send monthly bills, even in cases of zero billing. The monthly statement must have, at a minimum • a breakdown of total amount due and the minimum amount payable; • annualized rate of interest and interest amount along with the method of calculation; • acceptable modes of payment, expected number of days each mode takes to clear, and handling charges, if any; and • due date for payment. In practice, there seem to be many problems in using the postal services in Pakistan, which are considered highly unreliable. Alternatively, banks and MFBs have been using expensive courier services to mail statements to clients. This justifies in part the choice of biannual statements rather than monthly. However, to compensate for this low frequency, MFBs should offer free monthly statements in some electronic format, if such means are already being used by the customers to repay their loans or conduct other transactions. There are no common standards being followed by MFIs and RSPs for account statements. Because they do not offer deposit accounts and long-term products, they usually do not offer any statements to their clients, and in a group lending methodology this type of information is handled at the group level, with support from the loan agents. It is common for MFPs offering only loans to substitute account statements for informal methods such as "passbooks" in which the client or group writes down the quantity being paid and the quantity being kept as savings (if any). According to the microfinance technology, these informal instruments serve the purpose of educating borrowers on financial management and control.
Recommendation	1. SBP should issue a specific regulation to set some standards for the language, content, frequency, and format of account statements, to ensure they are frequent enough, readable, complete, and easily understood by microfinance clients. Such standards are likely to be different from those applicable to banks, given the nature of the microfinance business and the level of sophistication of microfinance clients. MFBs should be encouraged to provide account statements more frequently than every six months. However, given the practical challenges and the costs of dealing with postal and courier services in Pakistan, there should be flexibility for MFBs to use electronic channels. 2. MFIs and RSPs should be subject to common minimum standards similar to those applicable to MFBs. SBP, PMN, and PPAF should coordinate to develop such standards whenever they are relevant. An effective monitoring scheme should be created to ensure compliance with the standards.
Good Practice C.2	***Notification of Changes in Interest Rates and Noninterest Charges***

	a. A customer of a microfinance provider should be notified in writing by the microfinance provider of any change in **(i) the interest rate to be paid or charged on any account of the customer as soon as possible; and** **(ii) a noninterest charge on any account of the customer a reasonable period in advance of the effective date of the change.** **b. If the revised terms are not acceptable to the customer, he or she should have the right to exit the contract without penalty, provided such right is exercised within a reasonable period.** **c. The microfinance provider should inform the customer of the foregoing right whenever a notice of change under paragraph a. is made by the institution.**
Description	As mentioned in previous items, disclosure regulation is fragmented, spread across regulations dealing with services, channels, and other topics. These regulations have some provisions related to notifications of price and cost and changes in them. For instance, the Branch Licensing Guidelines prohibit MFBs using mobile ATMs to impose extra charges for transactions in this channel, other than the existing charges for ATM transactions. Also, MFBs, with relation to customers from other banks using their ATMs, cannot charge more than the agreed fee for interswitch transactions (about PRs 15). The Payment and Electronic Funds Act also protects the consumer's right to be notified of relevant changes at least 21 days prior to the effective date of any material change in any term or condition of the consumer's account. Also, the Operational Guidelines for Credit Cards requires revisions in the agreed terms and conditions or removal or withdrawal of an incentive to be communicated to the customer at least 30 days before the actual effective date. There are no provisions regarding the customer's foregoing right. There are no specific provisions related to rates paid or charged to deposit accounts at MFBs. There is no consensus in the market on whether the existing rules for scheduled banks related to interest paid on customer accounts apply equally to MFBs (e.g., a minimum rate of return on savings accounts). The Operational Guidelines for Credit Cards, Section 3, require that changes in schedule of charges, revision in the agreed terms and conditions, or removal or withdrawal of an incentive be communicated to the customer at least 30 days before the actual effective date.
Recommendation	1. SBP should consider issuing a specific regulation dealing with notifications that MFBs need to give in case of changes in prices and costs. Such notifications should be done in due time, and through means that are consistent with the services being provided to the client (e.g., electronic means could be used for such alerts). Customers should have the right to cancel the service if they are not in agreement with the change. SBP may consider incorporating some of the rules from the Operational Guidelines for Credit Cards in this regard.

	2. MFIs and RSPs should be subject to similar minimum requirements on notifications to clients, and their compliance with such requirements should be effectively monitored by an authority with enforcement powers.
Good Practice C.3	***Customer Records*** **a. A microfinance provider should maintain up-to-date records in respect of each customer of the microfinance provider that contain the following:** **(i) a copy of all documents required to identify the customer and provide the customer's profile;** **(ii) the customer's address, telephone number, and all other customer contact details;** **(iii) any information or document in connection with the customer that has been prepared in compliance with any statute, regulation, or code of conduct;** **(iv) details of all products and services provided by the microfinance provider to the customer;** **(v) a copy of all correspondence from the customer to the microfinance provider and vice-versa and details of any other information provided to the customer in relation to any product or service offered or provided to the customer;** **(vi) all documents and applications of the microfinance provider completed, signed, and submitted to the microfinance provider by the customer;** **(vii) a copy of all original documents submitted by the customer in support of an application by the customer for the provision of a product or service by the microfinance provider; and** **(viii) any other relevant information concerning the customer.** **b. A law or regulation should provide the minimum permissible period for retaining all such records and, throughout this period, the customer should be provided ready free access to all such records.**
Description	The PRMFB, Section 17, requires MFBs to maintain records of transactions and client identification data, for at least five years following the termination of the business relationship. This includes account files and business correspondence. Transaction records must be sufficient for reconstruction of individual transactions for the purposes of investigations on criminal activities. The Guidelines on Outsourcing Arrangements (BPRD Circular No. 9, 2007), Section 30, requires MFBs to satisfy SBP that outsourcing activities do not violate statutory or prudential requirements on anti-money-laundering or record-keeping procedures. The Payments and Electronic Transfers Act, 2007, Section 7, requires institutions providing funds transfer facilities to retain complete records of electronic transactions in electronic form in the same manner as provided in Section 6 of the Electronic Transactions Ordinance, 2002, for a period as determined by SBP. Moreover, the Branchless Banking Guidelines, Section 5.4, requires agents to ensure safekeeping of all relevant documents and files for at least five years, or such information may be kept by the MFB itself for the same minimum period.

	MFIs and the RSP fall into the definition of financial institutions established in the Anti-Money Laundering Act, 2010. Hence, they are subject to client due diligence and record-keeping rules, which seem to be adequate for the purposes of this Good Practice. In this regard, they report to and are monitored by the Financial Monitoring Unit only.
Recommendation	None
Good Practice C.4	*Credit Cards* **a. There should be clear rules on the issuance of credit cards and related customer disclosure requirements.** **b. Microfinance providers, as credit card issuers, should ensure that personalized disclosure requirements are made in all credit card offers, including fees and charges (including finance charges), credit limit, penalty interest rates, and method of calculating the minimum monthly payment.** **c. Microfinance providers should not be permitted to impose charges or fees on pre-approved credit cards that have not been accepted by the customer.** **d. Consumers should be given personalized minimum payment warnings on each monthly statement and the total interest costs that will accrue if the cardholder makes only the requested minimum payment.** **e. Among other things, the rules should also** **(i) restrict or impose conditions on the issuance and marketing of credit cards to young adults (below age 21) who have no independent means of income;** **(ii) require reasonable notice of changes in fees and interest rate increases;** **(iii) prevent the application of new higher-penalty interest rates to the entire existing balance, including past purchases made at a lower interest rate;** **(iv) limit fees that can be imposed, such as those charged when consumers exceed their credit limits;** **(v) prohibit a practice called double-cycle billing by which card issuers charge interest over two billing cycles rather than one;** **(vi) prevent credit card issuers from allocating monthly payments in ways that maximize interest charges to consumers; and** **(vii) limit upfront fees charged on subprime credit cards issued to individuals with bad credit.** **f. There should be clear rules on error resolution and reporting of unauthorized transactions and of stolen cards, with the ensuing liability of the customer being made clear to them prior to their acceptance of the credit card.** **g. Microfinance providers and issuers should conduct consumer awareness programs on the misuse of credit cards, credit card overindebtedness, and prevention of fraud.**

Description	It is not entirely clear whether the Operational Guidelines for Credit Cards (OGCC) applies to MFBs, as it makes reference to only banks and development financial institutions. However, because MFBs are allowed to issue credit cards, this section assumes they apply to MFBs. The OGCC establishes many consumer protection standards that are relevant for this Good Practice. For instance, MFBs shall quote interest rates on an annual basis, and inform such rates to customers through advertising or mailing (OGCC, Section 3). MFBs shall not levy any charge that was not explicitly mentioned in the user guide, application form, or schedule of charges provided to the customer at the moment of sale. Changes in the schedule of charges, revision of the agreed terms and conditions, or removal or withdrawal of an incentive must be communicated to the customer at least 30 days before the actual effective date. The OGCC, Section 1, states that issuers should follow the code of conduct for marketing of credit cards that would be issued by the Pakistan Banks' Association (PBA) in consultation with SBP. They should discourage aggressive selling and marketing during work hours, except with a prior appointment. If a prospective client is called during office hours, she should be asked first if she would like to continue the call. Providers must first seek authorization from clients to inform them about new products and services by phone. Providers must maintain a "don't call" list comprised of customers who have opted out. Marketing personnel must disclose their official identity before or while meeting with prospective customers. Marketing and sales personnel should be trained regularly, provide complete information on credit cards to prospective customers, and not make false claims on the card features. Institutions are required to do "surprise checks" to verify the marketing approach and to take immediate remedial steps and disciplinary actions against staff who do not comply with these guidelines. There are no rules limiting upfront fees charged on subprime cards issued to individuals with bad credit. There is a clear regulatory framework for error resolution in credit cards, which is in partly set by the OGCC (see description of internal complaint-handling mechanisms in Good Practice E.1), and partly set by the rules imposed by card brands such as Visa, MasterCard, and American Express. In addition, the OGCC, Section 2.3, prohibits stipulations, caveats, clauses, or provisions in the terms and conditions of the contract, which may result in curtailment of customer rights. There are no regulations requiring MFBs to undertake consumer awareness campaigns with regard to the misuse of credit cards, overindebtedness, and prevention of fraud. The OGCC simply requires issuers to describe, in the application form to be provided to cardholders in English and Urdu, the liabilities of all parties in case of credit card loss or fraud. Also, in order to mitigate fraudulent use of cards, issuers must have functionality built into their systems to monitor the usage of the card, and promptly identify unusual

	transactions. Lastly, issuers are required to maintain a track record of merchants' performance and categorize them, based on risks and involvement in fraud and disputed transactions, and develop a database of merchants involved in fraudulent activities, to minimize the occurrence of frauds.
Recommendation	1. SBP should clarify whether the Operational Guidelines for Credit Cards apply equally to MFBs. 2. SBP should consider reviewing the OGCC to align them with the items listed in this Good Practice.
Good Practice C.5	***Debt Recovery*** **a. All microfinance providers, agents of a microfinance provider, and third parties should be prohibited from employing any abusive debt collection practice against any customer of the microfinance provider, including the use of any false statement, any unfair practice, or the giving of false credit information to others.** **b. The type of debt that can be collected on behalf of a microfinance provider, the person who can collect any such debt, and the manner in which that debt can be collected should be indicated to the customer of the microfinance provider when the credit agreement giving rise to the debt is entered into between the microfinance provider and the customer.** **c. A debt collector should not contact any third party about a microfinance customer's debt without informing that party of the debt collector's right to do so and the type of information the debt collector is seeking.** **d. Where sale or transfer of debt without borrower consent is allowed by law, the borrower should be** **(i) notified of the sale or transfer within a reasonable number of days;** **(ii) informed that the borrower remains obligated on the debt; and** **(iii) provided with information as to where to make payment, as well as the purchaser's or transferee's contact information.**
Description	There are no regulations setting accepted and unaccepted lending and collection practices for microfinance loans, including for MFBs. There is also no mention to the incentive structure offered by MFPs to avoid abuses, such as compensation of loan officers. There are no rules with regard to sales or transfers of debts. MFIs and RSPs are not subject to any regulation with regard to collection practices. PPAF partners and PMN members subscribe to the Client Protection Principles, including treating their clients fairly and respectfully and ensuring adequate safeguards to detect and correct corruption and aggressive or abusive treatment by their staff and agents, particularly during the loan sale and debt-collection processes. These institutions are not subject to statutory supervision to ensure compliance with the principle. As stated earlier, PPAF conducts yearly monitoring of its partners, and one of the topics reviewed is adherence to the client protection principles. However, it lacks legal enforcement powers. There are reports of abusive collection practices, such as physically intimidating

	delinquent borrowers (particularly female borrowers), threatening clients with imprisonment based on the issuance of bounced checks, and other types of harassment. It is common for MFIs and MFBs to require, from clients with an account (MFB borrowers are usually required to open a current account), a series of post-dated checks as backup for each loan installment. The checks are returned to the client at the end of the loan contract, if all installments were made. In the case of a delay in payment, the MFB reportedly notifies the client that the check will be deposited. This is an effective pressure on the borrower, because issuing checks without funds is a criminal offense in Pakistan. Hence, the borrower can end up in jail for delaying a payment for more than 60 days. MFBs clarify that very rarely they need to involve the police; in most cases, borrowers pay their installments after the first warning that the checks will be deposited. Although this practice would be considered unacceptable in many markets, it is widely accepted in Pakistan, because of the difficulties and costs of applying other collection and enforcement practices. With regard to credit cards, the OGCC requires the issuer to ensure that recovery letters issued to cardholders bear the designation, contact number, and office address of the collection official. They should respond to queries arising out of the recovery letters within a reasonable time period, which must be specified in the issuer's public policy and properly communicated to the customer. Issuers must ensure that their recovery/collection officers do not resort to any verbal or physical harassment of the delinquent cardholder, their family members, referees, and friends. Officers shall not humiliate publicly or in private or intrude the privacy of the cardholder's family members, referees, and friends. Telephone calls and visits to cardholders for recovery should be restricted to a convenient time and it must be defined in the issuer's public policy and properly communicated to customers when the card is issued. Recovery should be made only from the principal cardholder and in no case shall supplementary cardholders be subject to any sort of pressure to pay the unpaid amount. Supplementary cardholders may be contacted only to inquire about the whereabouts of the principal cardholder. Transactions that are being disputed (at either the issuer, the ombudsman, or SBP) shall not be subject to the recovery process.
Recommendation	1. SBP should improve the regulation for MFBs, to include more specific rules for debt collection practices, highlighting prohibited practices and some minimum standards such as the ones listed in this Good Practice. It should consider incorporating some of the provisions from the OGCC. 2. The practice of using post-dated checks signed by borrowers should be monitored to ensure it does not involve abusive behavior by agents or staff responsible for collecting the loans. 3. MFIs and RSPs should be subject to standards similar to those issued for MFBs and should also be subject to a monitoring scheme to ensure compliance

	with such standards and other broad principles embedded in codes to which they subscribe.
SECTION D	**PRIVACY AND DATA PROTECTION**
Good Practice D.1	***Confidentiality and Security of Customers' Information*** **a. The financial transactions of any customer of a microfinance provider should be kept confidential by the institution.** **b. The law should require microfinance providers to ensure that they protect the confidentiality and security of personal data of their customers against any anticipated threats or hazards to the security or integrity of such information, and against unauthorized access.**
Description	There are no specific regulations requiring MFBs to put in place procedures to ensure the confidentiality, security, and integrity of consumer's personal information. There is a fragmented framework with rules spread across different regulations dealing with varied topics, such as outsourcing and branchless banking. The Guidelines on Outsourcing Arrangements (BPRD Circular No. 9, 2007) require MFBs, when entering outsourcing arrangements that involve the transfer of customer data to third parties, to ensure that the outsourcing arrangements comply with the relevant statutory requirements related to confidentiality of its customers, specifically the provision of the BCO on fidelity and secrecy (Section 33A[27]), relevant local laws, regulations, and instructions issued by SBP. MFBs must establish proper safeguards to protect the integrity and confidentiality of customer information, including obtaining prior consent to data sharing. In case the outsourcing arrangement involves sharing confidential information to service providers abroad, it will be subject to prior approval from SBP. The OGCC, Section 2, requires issuers to ensure confidentiality of their customers' information and to not divulge, share, or sell customers' information to any other body or institute, except SBP's Electronic Credit Information Bureau (eCIB) and any other approved credit bureau to which the issuer belongs. The limitation also does not apply to the companies who have an agreement with the issuer for data sharing because of outsourcing arrangements. However, outsourcing arrangements must enforce the confidentiality requirement for the third party. The Payment and Electronic Fund Transfers Act, Section 15, requires service providers to ensure that secure means are used for transfer, compliant with current international standards and as may be prescribed by SBP from time to time. MFIs and RSPs are not subject to any regulation. They subscribe to the Client Protection Principles, which include ensuring privacy of client data: "the privacy of individual client data will be respected in accordance with the laws and regulations of individual jurisdictions. Such data will only be used for the purposes specified at the time the information is collected or as permitted by law,

[27] Every bank and financial institution shall not, except as otherwise required by law or according to customary practices in the banking sector, divulge any information relating to the affairs of its customers.

	unless otherwise agreed with the client." However, the principles are not subject to enforcement by a statutory entity with enforcement powers. PPAF conducts annual reviews of its partners, including with regard to compliance with the Client Protection Principles, and it has not highlighted data privacy as a consumer issue with its partners. Branchless banking (defined according to the Branchless Banking Guidelines, 2007) has become an important instrument for financial inclusion and a policy priority of SBP, which has been encouraging its adoption. The regulatory framework for branchless banking is relatively robust for consumer risks, providing protections such as data confidentiality. Compliance officers and internal auditors at MFBs are required to ensure compliance with all applicable regulations when branchless banking is used. Moreover, MFBs must implement agent due diligence policies and procedures. MFBs are responsible for data and network security to ensure authenticity, confidentiality, and integrity of data, and assign responsibility to each involved actor to mitigate risks. The Branchless Banking Guidelines also recommend standards for end-to-end secure communication in electronic channels, such as authentication, user personal identification number (PIN), and other techniques. In addition to keeping MFBs responsible for protecting customer data, the Branchless Banking Guidelines also require MFBs to orient customers of their roles and responsibilities which, at a minimum, include (i) securing password or PIN; (ii) keeping personal information private; (iii) keeping records of wireless transactions; (iv) being vigilant while initiating or authorizing transactions; (v) taking special care of the mobile device; and (vi) other measures related to ATMs and cards. However, MFI clients remain less protected. Only banks and MFBs can operate branchless banking platforms and agent networks, but MFIs use their services without having to follow any consumer protection standard such as data privacy. There have been instances of agent fraud and abuse (e.g., overcharging of fees and fraudulent transactions using client information) and other problems with electronic and agent transactions, but the industry is in its infancy, and the lack of information on consumer complaints makes it difficult to assess the performance of branchless banking at the consumer level. With branchless banking taking off in Pakistan, it is important to monitor consumer issues in all types of MFPs.
Recommendation	1. It is recommended that SBP review existing rules pertaining to confidentiality, security, and integrity of consumer's personal information, and compile relevant rules in a cohesive regulation extending such principles to all operations undertaken by MFBs (i.e., not only for credit cards or for outsourcing arrangements). A complete and cohesive regulation would have specific requirements for MFBs to develop and implement data security policies and procedures, which are enforced by SBP through its supervisory review.

	2. MFIs and RSPs should follow similar standards, and compliance should be checked by an authority with effective enforcement powers. 3. SBP should introduce a consumer protection perspective to the oversight of branchless banking models in MFBs, in accordance with the general principles stated in the Branchless Banking Guidelines, 10.1 and 10.3. For instance, SBP may wish to design and review standard complaint reports to identify and address any industry-wide problems in branchless banking channels. 4. With regard to MFIs and RSPs using branchless banking schemes provided by authorized financial institutions, consumer protection risks should be addressed by setting and monitoring compliance with standards similar to those applicable to MFBs.
Good Practice D.2	***Credit Reporting*** **a. Credit reporting should be subject to appropriate oversight, with sufficient enforcement authority.** **b. The credit reporting system should have accurate, timely, and sufficient data. The system should also maintain rigorous standards of security and reliability.** **c. The overall legal and regulatory framework for the credit reporting system should be (i) clear, predictable, nondiscriminatory, proportionate, and supportive of consumer rights; and (ii) supported by effective judicial or extrajudicial dispute resolution mechanisms.** **d. Proportionate and supportive consumer rights should include the right of the consumer** **(i) to consent to information sharing based on the knowledge of the institution's information-sharing practices;** **(ii) to access his or her credit report free of charge (at least once a year), subject to proper identification;** **(iii) to know about adverse action in credit decisions or less-than-optimal conditions or prices due to credit report information;** **(iv) to be informed about all inquiries within a set period of time, such as six months;** **(v) to correct factually incorrect information or to have it deleted and to mark (flag) information that is in dispute;** **(vi) to reasonable retention periods of credit history; and** **(vii) to have information kept confidential and with sufficient security measures in place to prevent unauthorized access, misuse of data, or loss or destruction of data.** **e. The credit registers, regulator, and associations of microfinance providers should undertake campaigns to inform and educate the public on the rights of consumers in the above respects, as well as the consequences of a negative personal credit history.**
Description	SBP manages and operates the eCIB, created in 1992, based on Section 25(a) of

	the Banking Companies Ordinance. See a full description of the eCIB and its general compliance with this Good Practice, in volume I. The eCIB collects data on all borrowers irrespective of any limit (there was a data reporting minimum amount of PRs 500,000, which was eliminated in 2006[28]) and it provides credit reports including the client's exposure as of a certain date. While banks need to obtain a credit report on borrowers before extending facilities of PRs 500,000 and above, MFBs are required to get such reports before extending loans of any size.[29] The eCIB maintains records for 12 months. The eCIB information is not sufficient for MFBs to assess the aggregate credit exposure of a microfinance client, as it is accessed and populated only by entities regulated by SECP or SBP. This leaves out MFIs and RSPs. Also, it does not contain other useful information, such as positive payment history of utilities and other bills, which helps first-time microfinance borrowers without a credit history get credit. MSPs, including MFBs, need to rely on informal procedures to assess the existence of other loans extended to a loan applicant, such as requiring a declaration from the client herself, and calling other providers, one by one, to check on individual clients, and getting credit reports from other bureaus.[30] This increases costs for providers and clients, and is less effective than an accessible and effective bureau. Microfinance clients in Pakistan end up being more vulnerable to high levels of indebtedness than bank clients, as has already been proved by the delinquency crisis in Punjab in 2008/2009. Also, the lack of positive payment information on first-time borrowers makes it more difficult for them to get approved. There are not many rules pertaining to the specific rights of consumers included in the eCIB. BSD Circular No. 16, 2004, requires reporting institutions to send a letter to the borrower about the implications of reporting to the eCIB, and allow a reasonable time period (at least 15 days) for reconciliation or settlement of overdue liabilities. The Operational Guidelines for Credit Cards, Section 6.8, makes the card issuer responsible for correcting erroneous information provided to eCIB, or any other approved credit bureau, within a reasonable time. Also, SBP does not make any correction in the system at the request of a borrower. Accuracy is the responsibility of financial institutions and only the reporting institution is able to alter data about a borrower. Updates in the borrower's record are made every 10 days, although overdue amounts that were paid are only cleared in the next month's reporting by the concerned financial institution. Lastly, the right for privacy is taken to the extreme by SBP, and not even corporations and individuals are able to obtain their own credit information reports.

[28] BSD Circular No. 6, 2006.

[29] MFBs can get credit reports from other bureaus for loans up to PRs 30,000. Above that value, accessing the eCIB is mandatory, regardless of whether another bureau is also accessed.

[30] Besides the eCIB, there are other privately owned credit bureaus operating in Pakistan: Datacheck (Pvt.) Limited, News-VIS Credit Information Systems, ICIL/PakBizInfo, and Credit Chex (Pvt.) Limited.

	The microfinance industry, through a joint initiative by SBP, PMN, and PPAF (with funding from the Department for International Development), has piloted its own credit bureau in Lahore, separate from SBP's eCIB, which is now being expanded to the rest of the country. This is to address the lack of credit information on MFI and RSP clients. It is called MF-CIB and will be regulated and supervised by SBP. A separate bureau has been established because of resistance by banks to share their clients' information deposited in the eCIB, and because, as an SBP-hosted bureau, the eCIB is not an adequate system to host other types of information that can be useful for microfinance lending, such as utility bill payment history. It is not clear yet whether nonmembers of PMN will be able to use this new bureau. The interviews suggest that some MFIs are resistant to being required to access any bureau, because this could reduce their lending capability in areas where several MSPs overlap. Overall, MFIs in the same region tend to target the same customers, exposing them to higher risk of overindebtedness in the absence (or lack of usage) of credit information. SBP has a consumer awareness campaign specifically to increase knowledge about and trust in the CIB. SBP has also implemented the eCIB helpdesk to assist individuals and members of the eCIB with their queries and complaints about the system.
Recommendation	1. The MF-CIB is expected to provide many benefits to the industry and microfinance borrowers, including the potential to reduce risk of over-indebtedness. However, it will only achieve such benefits if the majority of microfinance providers become members. At least PMN members and PPAF partners should be required to become members of the MF-CIB. Also, PMN and PPAF should consider incorporating positive credit history and alternative payment information, such as utility bill payment history, to encourage lending to first-time borrowers. 2. Borrowers should be able to request their own credit reports from the eCIB, MF-CIB, or any other credit bureau for that matter. SBP should consider introducing regulatory changes to allow this.
SECTION E	**DISPUTE RESOLUTION MECHANISM**
Good Practice E.1	***Internal Complaints Procedure*** **Complaint resolution procedures should be included in the microfinance providers' code(s) of conduct and monitored by the supervisory authority.**
Description	There is no clear legal or regulatory requirement for MFBs, MFIs, or RSPs to have an internal structure to deal with customer complaints referent to any type of operation in which these institutions engage. The Client Protection Principles adopted by PMN and PPAF establish that MFPs will have in place timely and responsive mechanisms for complaints and problem resolution for their clients and will use these mechanisms both to resolve individual problems and to improve their products and services. However, most MFPs do not have a formal

	internal complaint-handling mechanism and adherence to the code is not monitored by a supervisory authority. PPAF does conduct monitoring of their partners, but it has no legal enforcement power, nor does it have specific standards aside from what is in the code. In practice, most MFBs, but only a few MFIs or RSPs have instituted redress channels. The availability, structure, and quality of this service vary widely across providers, due to the lack of common standards. With some exceptions, microfinance clients served by MFIs and RSPs are left with no complaints channel other than the courts, because they do not have access to third-party redress as well (see Good Practice E.2 below). The fact that MFBs have instituted complaint-resolution mechanisms more often than RSPs and MFIs is due to the existence of some regulations mentioning the need for MFBs to have complaint mechanisms. For instance, MFBs providing branchless banking facilities are required to put in place proper complaint redressal mechanisms (Branchless Banking Guidelines, 10.1 and 10.3) capable of (i) receiving and processing costumer's complaints within 24 hours through text messages, automated phone service, and e-mail; (ii) general acknowledgment of complaints through a unique complaint identification number; (iii) communicating the acknowledgement to the client with estimated time for redressal; (iv) redirecting the complaint to the appropriate section; and (v) keeping track of all complaints and giving the status of every complaint. Regardless, the framework for MFBs remains unclear and fragmented, with existing rules included in specific product-, channel-, or service-related regulations, rather than in an instrument that clearly applies to all products and providers regardless of their scope of operation. There should be minimum standards harmonized across the industry. For instance, the quality of customer service (which arguably includes complaint resolution) is used as criteria for approving annual branch expansion plans of MFBs (Branch Licensing Guidelines, Section 55), but the regulation does not spell out any minimum standards such as those found in the Branchless Banking Guidelines. Also, SBP requires MFBs to, before extending the facility of cash and check deposits through ATMs, develop and put in place a well-defined procedure for dispute resolution related to ATM transactions. When using third-party ATM networks, the MFB must be responsible for resolving disputes (Branch Licensing Guidelines, Sections 30 and 32). MFBs are allowed to have sales and service centers, which can work as a channel for clients to lodge their complaints and other requests (Branch Licensing Guidelines, Section 19). These centers must have clear and proper signage. Also, the Guidelines on Outsourcing Arrangements (BPRD Circular No. 9, 2007), Section 31, requires MFBs to give a well-defined mechanism for redressal of complaints regarding outsourced services, and the service provider will make sure they facilitate the redressal mechanism. Lastly, the Payment Systems and Electronic Funds Transfer Act 2007 requires institutions, when investigating a possible error such an unauthorized transaction, to deliver or mail to the consumer an explanation of its findings within three business days from the conclusion of the investigations. This fragmented framework creates some confusion in the market as to whether MFBs are required to have complaint mechanisms and follow the same standards imposed on banks in this regard. It also seems that SBP inspectors review

	complaint-handling mechanisms put in place by MFBs, following the supervisory practices used to evaluate banks, which is based on BPRD Circular No. 17, 2004.[31] Specifically with regard to MFBs' credit card operations (MFIs and RSPs are not allowed to offer credit cards), the Operational Guidelines for Credit Cards (which seems to apply to them on the same basis as to banks) requires, in Section 6, that the card issuer have an appropriate complaint resolution structure in place commensurate with the volume of complaints and better service considerations. The mechanism should be prominently disclosed on the official website, and online complaint filing should be provided. A unique number should be created for each new complaint. The complaints should be solved promptly and as per the franchise rules of Visa, MasterCard, American Express, or another, not to exceed 45 days total. Authorities have not demonstrated a strong interest in investigating the availability and quality of internal complaint resolution mechanisms in microfinance. Despite covering this topic in the course of its supervisory review of MFBs, SBP does not require reporting of and does not use complaint statistics on a regular basis. PPAF also has not pointed out complaint resolution as an area of concern. The lack of apparent concern with improving redress mechanisms in microfinance might be related to some prevalent views and prejudices. Some think that microfinance clients have no reason to complain because they benefit from access to finance. Others think that clients might be afraid of losing access to credit if they file complaints against the institution. Furthermore, because many microfinance clients are women, they would feel intimidated to make a complaint, particularly because most staff are men. Others seem to believe that microfinance in Pakistan has developed with a charity mindset, and hence it does not give rise to consumer complaints.
Recommendation	1. SBP should address the regulatory fragmentation and specifically require MFBs to have internal complaint resolution mechanisms to deal with all types of problems and queries, not only in particular areas as is the case today (e.g., credit cards). It should set minimum standards for complaint handling, such as establishing the maximum period within which the MFBs should respond to a complaint, and require MFBs to appoint an official to be in charge of managing, monitoring, and improving the complaint-handling function. MFBs should also be required to disclose the phone number and other means of communication for clients to reach the complaints unit, including in sales and marketing materials, communications, receipts, marketing materials, and, to the extent possible, during electronic transactions (e.g., during a cash withdrawal). 2. SBP should review the effectiveness of complaint-handling systems, and use complaint data (collected through regulatory returns) for regulatory and supervisory planning purposes. Improving complaint handling and using

[31] According to this circular, banks and development financial institutions have to handle complaints in an efficient and effective manner. Every bank is required under the guidelines to have a complaint resolution unit or department, and devise a system for redress of complaints in an appropriate and courteous manner, and the reply to the complainant must be clear and indicate the rationale of the decision. The banks and DFIs are also required to respond to the complaints within a period of 10 working days. The final reply should be sent to the customer in no more than 45 working days.

	complaint data will become increasingly important as the microfinance sector grows in number and complexity, and adopts electronic and other indirect means of service delivery (branchless banking). These developments can spur the number of complaints and reveal failures not only in consumer protection systems, but also in internal controls that could create other risks in MFBs. Analyzing complaint data is also useful to shape financial literacy and awareness campaigns. Complaint statistics should be reported to SBP on a regular basis, using a standard complaint report template defining the types and status of complaints. SBP should also use such statistics to publish data on consumer complaints in the MFB sector. 3. Complaint handling by MFBs, MFIs, and RSPs should have clear, affordable, and accessible procedures that work for microfinance clients. MFIs and RSPs should be subject to similar rules and conditions imposed on MFBs, and there should be an effective monitoring scheme to ensure compliance with the principles and regulations. 4. Lastly, as there is some belief that microfinance clients are not expected to file complaints and may feel intimidated from doing so out of fear of losing access to their loans or because of cultural biases, there should be a concerted effort by at least SBP, PMN, and PPAF, to make microfinance clients aware of internal complaint resolution channels, and empower clients, particularly women, to use these channels as a manner to influence the quality of the service provided by MPFs.
Good Practice E.2	***Formal Dispute Settlement Mechanisms*** **a. A system should be in place that allows consumers to seek affordable and efficient third-party recourse, such as an ombudsman, in the event the complaint with the microfinance provider is not resolved to the consumer's satisfaction in accordance with internal procedures.** **b. The role of an ombudsman or equivalent institution in dealing with consumer disputes should be made known to the public.** **c. The ombudsman or equivalent institution should be impartial and act independently from the appointing authority, the industry, and the parties to the dispute.** **d. The decisions of the ombudsman or equivalent institution should be binding on microfinance providers. The mechanisms to ensure the enforcement of these decisions should be established and publicized.**
Description	Although commercial bank clients have access to the banking ombudsman (the Office of the Banking Mohtasib), microfinance clients and MFB clients do not. This is because the ombudsman was created by the BCO (Section 82A), and applies only to institutions covered in the ordinance. The procedures imposed by the Mohtasib seem accessible enough, even for microfinance clients, and the decisions of the Mohtasib are binding on the provider. Also, clients unsatisfied with the Mohtasib's decision may appeal to the SPB Governor. MFB clients can seek third-party redress using the Consumer Protection

	Department at SBP, which offers a free and simplified procedure to deal with complaints against financial institutions in general. After receiving a response (or not) from the MFB about a complaint, the customer who feels dissatisfied may write to the CPD or send an e-mail with all the necessary information about the case. Cases pending at legal forum cannot be addressed by the CPD. Cases by MFI and RSP clients cannot be processed by the CPD, as it only covers institutions related to and supervised by SBP. All that is left for MFI and RSP clients are the courts, including the District Consumer Courts of Punjab, which can be accessed by any financial consumer dealing with any type of financial institution. However, only Punjab has a consumer court, whereas in the other provinces microfinance clients need to go through the nonspecialized courts. The Punjab Consumer Courts require clients to first seek redress with financial institutions, by written notice (signed on solemn affirmation or oath). The provider is required to reply to the consumer within 15 days. The courts will not accept any case where the consumer does not prove that he has contacted the service provider first. Claims can be filed at the court only within 30 days of the cause of the action (the court may allow an extension to up 60 days, which might help in microfinance cases). The court shall decide the claim within six months. If the court concludes that any or all of the allegations contained in the claim are true, it shall issue an order to the provider for the adoption of a range of corrective measures described in the Punjab Consumer Protection Act, Section 31. If the provider fails to perform such actions, it shall be punished with imprisonment up to three years or fine up to PRs 20,000. Consumers aggrieved by the court's final order may file an appeal with the Lahore High Court within 30 days. The Punjab Consumer Courts received approximately 700 cases against banks and insurance companies in 2013, but not many (the number is not available) from microfinance consumers. The consumer court system could be a workable third-party solution for microfinance clients, if it were implemented in other provinces. There are five provincial consumer protection laws in Pakistan, and they all create a framework for formal dispute settlement for small claims with the same powers as are vested in civil court under the Code of Civil Procedure, 1908. However, the other provinces need to pass regulations to implement the consumer protection acts in practice, and establish the consumer protection council, as well as the consumer courts in the provinces. The Punjab Consumer Protection Act, 2005, and the Punjab Consumer Protection Rules, 2009, create the system for dealing with consumer claims in an expedited manner, in cases where the consumer believes the service provider is in contravention of the Consumer Protection Act. There was a plan, by PMN, to implement a complaint-handling structure to attend cases from clients of all its members, as part of PMN's Consumer Protection Initiative. Although it was supposed to be a short-term solution until another third-party mechanism (e.g., an ombudsman) could be offered to microfinance clients, the project did not move forward because of resistance of concerned stakeholders, based on the belief that there is an inherent conflict of interest when a member-based industry association deals with consumer complaints.

	There seems to be a very low level of awareness or understanding of all these channels, including the CPD and the consumer courts. Only a few complaints from MFB clients have been registered at the CPD and at the consumer courts in Punjab. There is no research on the underlying reasons for microfinance clients not to seek third-party redress, and their perceptions about these channels and their processes. Some relevant stakeholders believe that microfinance clients would not have reasons to complain against MFPs, because they have access to services that are otherwise inaccessible, or that problems between providers and customers are less common in microfinance, given the charitable origin of MFPs in Pakistan. With regard to courts, they are usually considered to impose complex, lengthy procedures that might intimidate a typically unsophisticated microfinance client. There is also a belief that because most microfinance clients are women, they would not feel that they should present a case against an MFP, or feel intimidated by the procedures, particularly since MFP personnel and court personnel are mostly males. Also, awareness about the Punjab Consumer Courts may be low because the other provinces do not have these courts. Finally, microfinance clients may fear losing access to microfinance services in cases where they complain about the provider.
Recommendation	1. As soon as possible, the concerned stakeholders (at least SBP, PMN, PPAF, OBM, and SECP) should coordinate and find the most pragmatic solution to provide effective, speedy, and low-cost third-party alternative dispute resolution to microfinance clients, and devise plans to increase awareness of microfinance clients about redress channels and procedures, and their right to file complaints without losing rights to access financial services. Complaint mechanisms in microfinance need to be as simple and straightforward as possible, and improving awareness about such mechanisms should be a policy priority. There should also be specific measures to deal with gender-related issues in complaint handling and filing, to empower women to exercise their rights (e.g., by employing women to deal with customer complaints, or having female loan officers to help clients file their complaints). It will also be necessary to increase awareness and knowledge among authorities that consumer issues and complaints can happen in microfinance, and that microfinance clients may want and have the right to present complaints and resolve grievances with their providers, similarly to bank and insurance clients. 2. The OMB has powers, expertise, capacity, and resources to also deal with grievances from microfinance clients. Its procedures may be accessible to most microfinance clients with few adaptations to allow clients in rural areas to present claims in a cost-effective manner (e.g., by presenting claims by mail or mobile phone), and some procedures might be streamlined to accommodate microfinance clients' lower level of sophistication. Stakeholders should consider expanding the Mohtasib's mandate to include all MFPs, regardless if they are regulated by SBP or not. Because expanding the mandate of the OMB involves legal reforms, palliative or short-term solutions may be required in the interim, such as the one once proposed by PMN. 3. In addition to alternative conflict resolution channels, it would be useful if consumer courts were operational in provinces other than Punjab, to offer

	speedy, specialized judicial procedures to all microfinance clients. Authorities might want to consider implementing the necessary legal and regulatory changes to establish such courts, and increase awareness efforts so consumers, particularly female consumers, know how to use the courts to solve their grievances and feel comfortable doing so.
SECTION F	**CONSUMER EMPOWERMENT** (See Volume I, Financial Education)

3. Insurance Sector: Comparison with Good Practices

SECTION A	CONSUMER PROTECTION INSTITUTIONS
Good Practice A.1	***Consumer Protection Regime*** **The law should provide for clear rules on consumer protection in all matters of insurance and there should be adequate institutional arrangements for implementation and enforcement of consumer protection rules.** **a. There should be specific provisions in the law that create an effective regime for the protection of retail consumers of insurance.** **b. The rules should prioritize a role for the private sector, including voluntary consumer organizations and self-regulatory organizations.**
Description	The Securities and Exchange Commission of Pakistan (SECP), through its Insurance Division, has supervisory responsibility for all aspects of insurance activities in Pakistan. The primary piece of legislation governing the insurance industry is the Insurance Ordinance, 2000 (the Insurance Ordinance). Further regulations, rules, and guidelines can be (and have been) issued by SECP. The importance of consumers of insurance is highlighted at the beginning of the Insurance Ordinance: "An Ordinance to regulate the business of the insurance industry to ensure the protection of the interests of insurance policyholders and to promote sound development of the insurance industry and for matters connected therewith and incidental thereto." In practice, many links in the chain that leads from the purchase through to a conclusion (claim or termination) of insurance policies can be strengthened. In some cases, this requires legal changes or the prescription of further rules by SECP, but in many cases the legal framework already exists and simply needs to be implemented and enforced. However, there is a lack of capacity both at SECP and in the industry, even though SECP has commenced enhancing its regulatory and supervisory capacity regarding insurance. The problems of consumer protection outcomes for retail insurance consumers are exacerbated by the general lack of awareness and understanding of insurance, and a lack of awareness of consumer rights in insurance (which is part of a wider issue in financial services and more generally). The situation is also aggravated by the poor implementation of mandated third-party motor vehicle insurance and some reputational issues. With the laudable efforts being made to develop microinsurance in Pakistan, the importance of consumer protection and developing financial literacy is heightened. Within SECP, to date, the regulatory and supervisory focus appears to have been more on prudential supervision of insurers than on consumer protection of holders and potential holders of insurance policies. An increased emphasis on consumer

	protection matters would benefit both consumers and the industry in the long run. As discussed in the overview, the legislation mandating third-party motor vehicle insurance is separate from the Insurance Ordinance, and the supervision of those providing such insurance needs to be addressed. The Competition Act, 2010, provides another channel for consumer protection via the Competition Commission of Pakistan. Some financial services entities, including an insurer, have been prosecuted under this act. There are also provincial Consumer Protection Acts in place.[32] These have general coverage, but they cover services, which suggest that they cover insurance. Insurance-related matters have been dealt with through the consumer courts established by these acts. a. There are some high-level requirements included in Part XI of the Insurance Ordinance. As noted above, the issue may lie more with implementation and enforcement than the legal framework. (see Section 12(4) of the Insurance Ordinance). b. This requirement is not met.
Recommendation	**A.1-1.** SECP should consider increasing its emphasis on consumer protection–related matters and establishing a section focused on addressing all aspects of consumer protection including, but not limited to, marketing practices, sales practices (including illustrations), disclosure (including policy documents), policyholder management processes (including statements), complaint management and resolution, awareness of insurance, and consumer education. This may be particularly relevant in the area of microinsurance. Consumer protection–related issues should be given increased priority in SECP onsite and offsite inspection processes. **A.1-2.** As part of wider initiatives, awareness of insurance and consumer rights should be published, made accessible, and promoted. These activities would best be undertaken by a broad-based partnership involving SECP and the insurance industry (potentially through the Insurance Association of Pakistan, or IAP) as well as other parties interested in consumer protection in the financial services. This may also include establishing relationships with media and other interested organizations to promote insurance and policyholder consumer rights. In particular, it may be appropriate to use work being undertaken in the banking sector, especially with regard to microinsurance. **A.1-3.** Greater clarity and coordination with respect to the various avenues available for consumer redress should be sought. This may lead to closer links between SECP and other agencies, and the courts.

[32] See, for example, the Punjab Consumer Protection Act, 2005.

Good Practice A.2	***Contracts*** **There should be a specialized insurance contracts section in the general insurance or contracts law, or ideally a separate Insurance Contracts Act. This should specify the information exchange and disclosure requirements specific to the insurance sector and the basic rights and obligations of the insurer and the retail policyholder and allow for any asymmetries of negotiating power or access to information.**
Description	There is no separate Insurance Contracts Act in Pakistan. Part XI of the Insurance Ordinance deals with market conduct. At a high level it specifies a number of requirements, including (i) a duty of utmost good faith on all parties to insurance contracts, (ii) prohibition on insurers engaging in misleading or deceptive conduct, and (iii) some further policyholder protections. Some further clarifications are provided in the rules. Although some policyholder protections are provided, it is not clear how carefully these protections, and their intent, are abided by or how strongly breaches (if and when identified) are dealt with. SECP intends to include requirements with regard to contracts and disclosure for microinsurance in the microinsurance regulations and guidelines currently being developed.
Recommendation	**A.2-1.** SECP's ongoing efforts to establish specific disclosure requirements for microinsurance provide an opportunity to review and improve disclosure requirements for insurance products more generally. **A.2-2.** See Recommendation A.1-1.
Good Practice A.3	***Codes of Conduct for Insurers*** **a. There should be a principles-based code of conduct for insurers devised in consultation with the insurance industry and with relevant consumer associations, and that is monitored and enforced by a statutory agency or an effective self-regulatory agency.** **b. If a principles-based code of conduct exists, insurers should publicize and disseminate it to the general public through appropriate means.** **c. The principles-based code should be augmented by voluntary codes for insurers on such matters specific to insurance products or channels.** **d. Every such voluntary code should likewise be publicized and disseminated.**
Description	a. There is no statutory code of conduct for either life or nonlife insurers in

	Pakistan. There was broad support from the life insurers for the establishment of an industry-wide code of conduct. There was also support for SECP being involved and giving such a code (or codes) their official endorsement. Sections 83 and 84 of the Insurance Ordinance appear to provide a basis by which SECP can achieve this. SECP intends to include requirements with regard to compliance with a code of conduct for microinsurance in the microinsurance regulations and guidelines currently being developed (see Section F3). SECP Consultation Paper covers both life and nonlife insurance. This provides the opportunity to establish a coordinated and consistent set of codes of conduct applicable to all types of insurance. b. Not applicable. c. The IAP has a code of conduct that is applicable to its nonlife insurer members. The extent to which the IAP enforces this code of conduct among its members is not clear. As of October 2012, the membership of the IAP does not include any Takfaul insurers (although it was reported that this may change in the near future), but does include all other life insurers in Pakistan and most nonlife insurers. It was reported to the mission that most insurers, life and nonlife, have internal codes of conduct (all those interviewed, with the exception of Postal Life Insurance, reported they had a code of conduct), although the extent to which these codes are enforced by insurers is not clear. None of the major (top three life and nonlife) insurers had a code of conduct available on their websites (as of October 2012). d. The IAP Code of Conduct is available on its website.[33]
Recommendations	**A.3-1.** SECP should establish appropriate codes of conduct for insurance, life and nonlife, in Pakistan. This should be done with industry participation. The IAP Code of Conduct for nonlife insurers provides a good starting point. **A.3-2.** SECP should follow through on its intention of establishing a specific code of conduct for microinsurance. **A.3-3.** SECP should include in its supervisory activities assessments of compliance with all codes of conduct and put in place processes (including penalties and redress to adversely impacted consumers) to remedy breaches of codes of conduct. **A.3-4.** As part of wider initiatives to promote awareness of insurance and consumer rights, codes of conduct should be published, made accessible, and

[33] See http://www.iap.net.pk.

	promoted. These activities would best be undertaken by a broad-based partnership involving SECP, the insurance industry (potentially through the IAP), and other parties.
Good Practice A.4	***Other Institutional Arrangements*** **a. Prudential supervision and consumer protection can be placed in separate agencies or lodged in a single institution, but allocation of resources between prudential supervision and consumer protection should be adequate to enable the effective implementation of consumer protection rules.** **b. The judicial system should provide credibility to the enforcement of the rules on financial consumer protection.** **c. The media and consumer associations should play an active role in promoting consumer protection in the area of insurance.**
Description	a. SECP is a unified regulator and supervisor for insurance, so all regulation and supervision of insurers is done by SECP. The prime focus of SECP is on prudential supervision of insurers. Although SECP has capacity limitations affecting its supervision of insurance matters, the emphasis on consumer protection–related issues is low. This is aggravated, particularly in the context of retail consumers, by SECP only indirectly supervising agents (through insurers). b. The judicial system in general in Pakistan is reported to be slow and costly to use. Thus, while in theory aggrieved consumers have the right to use the judicial system to seek redress, in practice this would only very rarely be a viable route. See also Section E.2. c. This does not occur. There appears to be little interest by either the media or consumer associations in insurance matters. Such lack of interest does not help raise awareness of the industry or support improving financial literacy or consumer protection.
Recommendations	**A.4-1.** See Recommendation A.1-1. **A.4-2.** SECP and the industry should consider developing an ongoing campaign to raise the profile and awareness of insurance education and related matters with the media and consumer protection bodies.
Good Practice A.5	***Bundling and Tying Clauses*** **Whenever an insurer contracts with a merchant or credit grantor (including banks and leasing companies) as a distribution channel for its contracts, no bundling (including enforcing adhesion to what is legally a single contract),**

	tying, or other exclusionary dealings should take place without the consumer being advised and able to opt out.
Description	It appears that Section 86 of the Insurance Ordinance may address this issue, but it also appears that this section is not enforced.[34]
Recommendation	**A.5-1:** SECP should consider applying Section 86 of the Insurance Ordinance as part of its assessment of insurance products and contracts. This may be particularly relevant to corporate leasing, bancassurance, and microinsurance products.
SECTION B	**DISCLOSURE & SALES PRACTICES**
Good Practice B.1	*Sales Practices* **a. Insurers should be held responsible for product-related information provided to consumers by their agents (i.e., intermediaries acting for the insurer).** **b. Consumers should be informed whether the intermediary selling them an insurance contract (known as a policy) is acting for them or for the insurer (in the latter case, the intermediary has an agency agreement with the insurer).** **c. If the intermediary is a broker (i.e., acting on behalf of the consumer) then the consumer should be advised at the time of initial contact with the intermediary if a commission will be paid to the intermediary by the underwriting insurer. The consumer should have the right to require disclosure of the commission and other costs paid to an intermediary for long-term savings contracts. The consumer should always be advised of the amount of any commission and other expenses paid on any single premium investment contract.** **d. An intermediary should be prohibited from filling both brokering and agency roles for a given general class of insurance (i.e., life and disability, health, general insurance, credit insurance).** **e. When a bank is the intermediary, the sales process should ensure that the consumer understands at all times that he or she is not purchasing a bank product or a product guaranteed by the bank.** **f. Sanctions, including meaningful fines and, in the case of intermediaries, loss of license, should apply for breach of any of the above provisions.**
Description	a. Insurers are responsible for all materials and information provided to policyholder and potential policyholders by their agents (Section 95 of Insurance Ordinance). The extent to which this obligation is enforced by SECP is not clear. b. Agents are required to disclose their status as an agent for an insurer (Section

[34] A specific instance of this is reported in "Consumer Financing in Pakistan: Issues, Challenges and Way Forward," published by the Consumer Rights Commission of Pakistan, 2008, in its section 7.10. Because banks are not regulated by the SECP, SBP should enforce the provisions of Section 86.

	100 of the Insurance Ordinance). The extent to which this obligation is enforced by SECP is not clear. c. All insurance brokers are required to be licensed by SECP. Only companies may be so licensed. There is no explicit requirement for a broker to disclose information regarding commission payment to policyholders or prospective policyholders. It is possible that such a requirement could be implied under the general requirement for brokers to disclose their relationship with insurer(s) (Section 105 of Insurance Ordinance). However, in practice, it appears commission disclosure is not required, or made. d. A broker may hold agency agreements with insurer(s) but an agent may not be a broker. A broker is presumed to be an agent for an insurer if a contract of agency is in place. Beyond disclosure requirements, there is no prohibition on a broker acting for one insurer as a broker and as an agent for another insurer for the same class of insurance business. e. The definition of "bancassurance" in SECP's Bancassurance Guidelines of 2010 includes insurance products that are (i) bundled with banking products, (ii) actively sold as independent products through the branch banking network, (iii) actively sold through other channels, or (iv) sold through any other channel that is recognized as an acceptable sales channel for banks by the State Bank of Pakistan. Section 4 of the guidelines includes requirements regarding marketing brochures and sales materials, claims handling, and the code of conduct for the bank (as agent for the insurer). The understanding that a purchase is not a bank product or guaranteed by the bank is not explicitly stated, but follows from the specified required disclosures. The extent to which such requirements are enforced by the insurer the bank is acting as agent for is not clear. f. SECP does not directly supervise the behavior of agents, banks or otherwise, hence does not apply sanctions for breaches of behavior by agents. SECP does license brokers and surveyors. It is unclear to what extent there is active supervision of them or what steps may be taken in the case of breaches of obligations.
Recommendation	**B.1-1.** While much of the regulatory framework to manage and supervise sales practices is in place (or can be put in place), SECP should ensure during supervision that the regulations are effectively being implemented. See also Section B.6 and Recommendation A.1-1.
Good Practice B.2	***Advertising and Sales Materials*** **a. Insurers should ensure that their advertising and sales materials and procedures do not mislead customers. Regulatory limits should be placed on investment returns used in life insurance value projections.** **b. Insurers should be legally responsible for all statements made in marketing and sales materials they produce related to their products.** **c. All marketing and sales materials should be easily readable and understandable by the general public.**
Description	a. SECP publishes circulars specifying the rates of interest required to be used in life insurance (and family takaful) product descriptions The most recent such

	circular (01/2011), dated January 4, 2011, referred to the calendar year 2011. It is noted that the long-term illustration template provides financial outcomes in nominal interest rates. The use of nominal interest rates, as opposed to real interest rates, can be misleading because the nominal rate results in very large numbers over a long projection period (for example, more than 10 years), and readers often interpret results using nominal rates of interest as if they were determined using real rates of interest. This would require the specification of an appropriate inflation rate. If the use of real rates of interest was required, care would need to be taken to ensure both that illustration guidelines become rules, so that all insurers are required to provide illustrations on a level playing field, and also that other providers of comparable products (in particular unitized investment products) are also required to provide illustrations under the same conditions to avoid the risk of the life insurers being put at a marketing disadvantage. b. Insurers are legally responsible for marketing and sales materials produced or used by their agents; however, the extent to which such requirements are enforced by the insurer responsible for the agent is unclear. The legal position and concerns about level of enforcement were recently reiterated by SECP in Circular No. 19 of 2011. c. This issue, in the context of websites, has been recently highlighted by SECP through Circular No. 18 of 2011. This also highlights the desirability of having information available in both English and Urdu. The extent to which such requirements are applied by SECP as part of their "file and use" (see Section F.1) process for life insurance products is unclear. SECP in its Circular No. 18 of 2011 requires all insurers to present information regarding their products on their websites in an easy to follow manner and in both English and Urdu. Suggestions were also made that materials should be provided in major regional languages, although it was acknowledged that this may not always be practical. SECP also intends to include requirements with regard to readability of marketing and sales materials for microinsurance products in the microinsurance regulations and guidelines currently being developed (Section F1). SECP Consultation Paper covers both life and nonlife insurance.
Recommendations	**B.2-1.** SECP should consider increasing its focus on the readability and access to marketing and sales materials used by insurers and their agents. More widely, see also Recommendation A.1-1. **B.2-2.** SECP should consider requiring illustrations for life insurance products to provide outcomes based on real rates of interest (without introducing competitive disadvantage). **B.2-3.** SECP should follow through on its intention of requiring marketing and sales materials to be readable and understandable to the public for microinsurance products, and extend this requirement to other insurance it covers.
Good Practice B.3	***Understanding Customers' Needs*** **The sales intermediary or officer should be required to obtain sufficient information about the consumer to ensure an appropriate product is offered. Formal "fact finds" should be specified for long-term savings and investment**

	products and they should be retained and be available for inspection for a reasonable number of years.
Description	Formal fact finds (and associated documentation) are not required. There are requirements that insurance advice provided, in writing, to a person, be relevant to the circumstances of that person. The burden of proof that due regard was given to the circumstances of the policyholder and that the advice given was reasonable rests with the insurer (or broker). In practice, it is unclear that the extent to which such requirements may be followed or enforced or the extent of records retained throughout the industry.
Recommendation	**B.3-1.** As part of broader initiatives to enhance consumer awareness, SECP and industry should consider how policyholder and potential policyholder needs can be better identified, recorded, and then addressed. See also Recommendation A.1-1.
Good Practice B.4	***Cooling-off Period*** **There should be a reasonable cooling-off period associated with any traditional investment or long-term life savings contract, after the policy information is delivered, to deal with possible high-pressure selling and mis-selling.**
Description	Section 39 of SECP (Insurance) Rules, 2002, specifies a trial period of 14 days from commencement for life insurance policies (excluding group insurance and those having a term exceeding one year). There are no corresponding requirements for nonlife insurance products.
Recommendation	No recommendation.
Good Practice B.5	***Key Facts Statement*** **A Key Facts Statement should be attached to all sales and contractual documents, disclosing the key factors of the insurance product or service in large print.**
Description	Key Facts Statements are not required at any point during the sales or policy issuance process.
Recommendation	**B.5-1.** SECP and the industry should consider the appropriate use of Key Facts Statements during the sales process and in policy contracts.
Good Practice B.6	***Professional Competence*** **a. Sales personnel and intermediaries selling and advising on insurance contracts should have sufficient qualifications based on the complexities of the products they sell.** **b. Educational requirements for intermediaries selling long-term savings and investment insurance products should be specified, or at least approved, by the regulator or supervisor.**
Description	a. There are no prescribed educational, or other, requirements for sales personnel (that is, employees of insurers, not agents or brokers). However, insurers are obliged to take responsibility for the actions of their employees. In practice, it is unclear the extent to which such requirements may be followed or enforced

	by insurers or supervised by SECP. There are only minimal prescribed educational (or other) requirements for intermediaries (that is agents or brokers). Section 97 of the Insurance Ordinance permits SECP to prescribe minimum qualifications, including educational requirements, for agents. Section 102 permits SECP to prescribe educational requirements for brokers as part of the licensing requirements. It appears there are differing levels of industry requirements for agents. Most (at least the leading) insurers report they have invested in developing their own training programs for sales personal and their agents. Future changes should recognize this investment and seek to leverage it and not waste it. Especially with the introduction of microinsurance and, to a lesser extent, bancassurance, consideration needs to be given to different types of agents needing different skills. SECP intends to include requirements on training of agents for microinsurance products in the microinsurance regulations and guidelines currently being developed (Section E3). SECP Consultation Paper covers both life and nonlife insurance. This raises the possibility of establishing a more consistent approach to the development of strengthened agent training for all types of insurance. It is noted that the Pakistan Insurance Institute already provides training courses for agents of nonlife insurers, and other intermediaries. The Institute of Capital Markets has also recently been established (with support from SECP among others) with a mandate that includes developing human capacity in both capital markets and insurance (with the first certified insurance training programs planned to be offered in 2013), and coordinating with SECP and others to develop financial services consumer and investor education programs to address the current lack of awareness. There is broad consensus that it would be valuable for SECP to specify more rigorous minimum training requirements for intermediaries, and agents in particular. There is also broad agreement that it would be valuable for SECP to license (even if in a devolved manner) agents industry-wide. This would permit the establishment of an industry-wide register, accessible to both insurers and a wider public, regarding the licensing status and history of agents. b. Following from a. above, there are only minimal prescribed educational requirements for intermediaries selling long-term savings and investment insurance products.
Recommendations	**B.6-1.** SECP should prescribe educational (and other as appropriate) requirements for all agents to satisfy, recognizing that agents selling different classes of business may need different qualifications.

	B.6-2. SECP should supervise the capabilities and activities of agents more vigorously, either directly or through the insurers. After a suitable transition period, it should be required of insurers that all agents meet the minimum specified SECP requirements. **B.6-3.** SECP should license all insurance agents, either directly or in a devolved manner. Such licensing (and associated training) should take into account programs already established by some insurers, to avoid losing the value and expertise already developed.
Good Practice B.7	***Regulatory Status Disclosure*** **a. In all of its advertising, whether print, television, radio, or other, an insurer should disclose** **(i) that it is regulated, and** **(ii) the name and address of the regulator.** **b. All insurance intermediaries should be licensed and proof of licensing should be readily available to the general public, including through the Internet.**
Description	a. These conditions are not met. In Circular No. 3 of 2012, SECP has specifically banned insurers from mentioning the name or logo of SECP in their "publicity ads" regarding their products (newspapers, websites, posters, leaflets, etc.). Previously, the 2009 SECP guidelines (which are not compulsory) for life insurance and family takaful specified that a footer must state that the insurer is registered and supervised by SECP. Also, SECP Circular No. 22 of 2005 contains the following: "On the first page of the policy document, brochures, leaflets, advertisements and any other promotional material whether used electronically or in print, it shall be clearly mentioned that the insurer is 'Registered and Supervised by the Securities and Exchange Commission of Pakistan.' This must be done by 31 January 2006." b. SECP currently does not license insurance agents and does not maintain lists of agents. It does license insurance brokers and insurance surveyors. Lists of registered insurance brokers and insurance surveyors are available on SECP website. The issue of licensing insurance agents is a major one. The mission understands that SECP supports an initiative to develop a database that includes all insurance agents and historical data. This would be a valuable tool in general and, in particular, for insurers who wish to review the history of agents with prior experience. Such a register could be made mandatory through a requirement that all insurers keep their agent force fully recorded. Insurers report that they sometimes make informal checks with each other when an agent changes insurer, but there are no formal or established processes to support such checks in the industry.
Recommendations	**B.7-1.** SECP should reconsider its approach to clarifying that registered insurers are supervised by SECP with respect to all appropriate materials and publicity produced by insurers. This may assist raising the profile and status of the industry and be particularly relevant to microinsurance and mandated third-party motor vehicle insurance.

	B.7-2. SECP should continue to support the development of an industry-wide, comprehensive, and mandatory data base of insurance agents of all types.
Good Practice B.8	***Disclosure of Financial Situation*** **a. The regulator or supervisor should publish annual public reports on the development, health, strength, and penetration of the insurance sector either as a special report or as part of the disclosure and accountability requirements under the law governing it.** **b. Insurers should be required to disclose their financial information to enable the general public to form an opinion on the financial viability of the institution.** **c. If credible claims paying ability ratings are not available, the regulator or supervisor should periodically publish sufficient information on each insurer for an informed commentator or intermediary to form a view of the insurer's relative financial strength.**
Description	a. There is no requirement that SECP publish annual reports as to the status of the insurance industry. Some industry summary information has been provided on SECP website and in recent annual reports, but this includes no insurer-specific information. Other information is not provided by SECP on an ongoing basis. SECP collects information from insurers in prescribed formats. It has recently introduced an electronic data collection process. This should facilitate the data collection and validation processes, permitting SECP to develop its capacity for statistical analysis of the industry. b. Insurers are required to fulfil the requirements of the relevant accounting standards in force and, for those insurers that are listed, also required to fulfil exchange requirements. Summary information is also published in the annual reports of Insurance Association of Pakistan. c. SECP does not publish additional information to allow an informed commentator to form a view of insurer's financial strength. A number of insurers, particularly the larger ones, are currently rated by ratings agencies in Pakistan.
Recommendation	**B.8-1.** SECP consider developing its capacity to do statistical analysis of the insurance industry and then consider producing annual reports for public access. Appropriate confidentiality requirements also need to be put in place.
SECTION C	**CUSTOMER ACCOUNT HANDLING AND MAINTENANCE**
Good Practice C.1	***Customer Account Handling*** **a. Customers should receive periodic statements of the value of their policy in the case of insurance savings and investment contracts. For traditional savings contracts, this should be provided at least yearly; however, more frequent statements should be produced for investment-linked contracts.** **b. Customers should have a means to dispute the accuracy of the transactions recorded in the statement within a stipulated period.**

	c. Insurers should be required to disclose the cash value of a traditional savings or investment contract on demand and within a reasonable time. In addition, a table showing projected cash values should be provided at the time of delivery of the initial contract and at the time of any subsequent adjustments. **d. Customers should be provided with renewal notices a reasonable number of days before the renewal date for nonlife policies. If an insurer does not wish to renew a contract it should also provide a reasonable notice period.** **e. Claims should not be deniable or adjustable if nondisclosure is discovered at the time of the claim but is immaterial to the proximate cause of the claim. In such cases, the claim may be adjusted for any premium shortfall or inability to recover reinsurance.** **f. Insurers should have the right to cancel a policy at any time (other than after a claim has occurred if material nondisclosure can be established.**
Description	a. There is no prescribed requirement for insurers—life insurers in particular—to provide policyholders with regular statements. b. Strictly speaking, this item is not applicable because detailed statements are not required. In practice, policyholders are typically able to contact their life insurer and obtain information regarding their policies (e.g., total bonuses available on their participating life policies). Assuming a statement (either formal or informal) has been obtained, policyholders could use standard complaint procedures to query values and transactions if dissatisfied. c. Insurers are required to disclose the projected cash values of life insurance policies at inception of the policy (via the illustrations). For unitized investment policies, life insurers are required to publish "in a newspaper having general circulation" unit values on a monthly basis. For current policyholders, there are no prescribed requirements; however, it was reported that life insurers consider it good practice to respond to such requests. There are not prescribed time frames for responses to policyholder requests to insurers. d. Such notices are required to be given at least one month prior to the renewal date. e. These conditions are met for both life and nonlife insurance (Section 79 of the Insurance Ordinance). f. These conditions are met. Section 82 of the Insurance Ordinance is specific regarding life insurance. More generally, material misrepresentation can be considered a breach of the "utmost good faith" obligations (Section 75 of the Insurance Ordinance) Further commentary: From a consumer perspective, the management of claims is also of critical importance. This issue is of higher importance in for insurance than for other financial services sectors because of the nature and purpose of insurance contacts and their longer-term nature. There seems widespread, although not universal, agreement that claims processes, both before and after disputes may arise, need to be improved. From the perspective of consumer confidence in insurance, the quality and fairness of claims management must be addressed, both in terms of actual processes and in terms of perception.

	Many anecdotal instances of poor claims management and the perception (at least) of claims being inappropriately denied were reported. Some industry respondents felt that a significant part of this issue revolved around lack of consumer understanding leading to inappropriate expectations. However, this belies the insurer's obligation to manage consumer expectations (both at point of sale and at the time of claim) given the typical knowledge imbalance between consumers and providers (including their agents). The experience with the mandated third-party motor vehicle insurance also does not help create a positive perception of insurance. The argument that a low level of complaints demonstrates there is not a major issue is problematic because it belies the issue of lack of awareness of consumers and the lack of promotion of dispute resolution processes. On a positive note, some insurers also indicate that they were taking a more proactive approach to claims management and initiating contact with claimants when they could. This is a good initiative. In non-life insurance, insurance surveyors (including loss adjusters and loss assessors) are required to be licensed by SECP unless they are performing their duties as an employee of an insurer. In the context of microinsurance, there may be a need to review the processes by which nonlife claims may be assessed, to avoid the need to use insurance surveyors (in the traditional ways they are used). Such a review may require changes to the Insurance Ordinance or the prescription of relevant rules or regulations under the ordinance with regard to microinsurance. Claim dispute resolution processes, while they exist in the law, need to be better implemented, and consumers need to be made more aware of their rights. However, claim dispute resolution processes, although necessary, are reactive in nature. See also Section E.
Recommendations	**C.1-1.** Requirements for periodic (at least annual) statements for life insurance policies should be clarified and enforced. It is noted that SECP is in the process of developing guidance for the management of unitized investment products. This guidance should include appropriate disclosure and information requirements for policyholders. See also Recommendation A.1-1. **C.1-2.** SECP should consider requiring more detailed data regarding claims and their processing from insurers under its powers to collect data. It should also consider increasing the priority given to inspection activities regarding claims management. Not only would this support consumers, but it would also support prudential oversight of insurers because poor claims management may threaten solvency. **C.1-3.** As part of a broader campaign to increase the awareness of insurance and its benefits, the adverse perceptions around the payment of claims (whether valid or not) should be addressed. This may have particular relevance to the development of microinsurance.
SECTION D	**PRIVACY & DATA PROTECTION**
Good Practice D.1	***Confidentiality and Security of Customers' Information***

	Customers have a right to expect that their financial transactions are kept confidential. Insurers should protect the confidentiality and security of personal data, against any anticipated threats, or hazards to the security or integrity of such information, and against unauthorized access.
Description	SECP does not require specific steps to be taken by insurers to preserve the confidentiality and security of customer information they hold. This is the case both with regard to internal management and integrity of data held by insurers and with regard to protecting data held from any form of unauthorized access. Insurers reported awareness of the importance of data security and correctness from the perspective of good business practice for delivering service to policyholders and for reputational reasons. According to a recent survey,[35] as of March 2012, there is "'no legislation regulating the protection of data in Pakistan." Consequently, issues regarding privacy, confidentiality, data integrity, and data protection are broader than insurance and broader than financial services, although there may be a heightened need for such protections in insurance and the financial services because they can hold sensitive personal information, including personal information collected through "know your customer" requirements under anti-money-laundering procedures and information collected from prospective policyholders as part of a needs analysis. With the development of bancassurance (sold through banks) and microinsurance with a variety of intermediaries and innovative distribution channels, and the general increase in volumes of information held electronically (and possibly involving third-party service providers), the risks of breaches of confidentiality and misuse of personal information increase. Further commentary: In addition to the level of security and protection of customer data provided by insurers, there is also the question of whether insurers share their data with other entities (e.g., banks) for various purposes such as marketing. There are no formal requirements regarding this topic, but the general attitude reported to the mission was that insurers only disclose information, as required by law, to the relevant authorities.
Recommendations	**D.1-1.** SECP and the insurance industry (potentially via the IAP) collaboratively develop guidelines (or stronger requirements) regarding minimum acceptable levels of privacy, confidentiality, data integrity, and data protection for insurance consumers and policyholders. This would include both processes internal to insurers and the sharing of data between entities. Once established, SECP would monitor the application of such guidelines by insurers, and take steps to ensure that breaches were properly addressed. SECP may be able to draw on work done in areas other than insurance, and work done by the State Bank of Pakistan in this regard. **D.1-2.** Given that privacy and the protection of personal information is a wider

[35] Data Protection Laws of the World, DLA Piper, March 2012.

	issuer than insurance and financial services, consideration should be given to reaching out to other interested parties and drawing on their experience with regard to privacy and personal data protection.
SECTON E	**DISPUTE RESOLUTION MECHANISMS**
Good Practice E.1	***Internal Dispute Settlement*** **a. Insurers should provide an internal avenue for claim and dispute resolution to policyholders.** **b. Insurers should designate employees to handle retail policyholder complaints.** **c. Insurers should inform their customers of the internal procedures on dispute resolution.** **d. The regulator or supervisor should investigate whether insurers comply with their internal procedures regarding consumer protection.**
Description	a. The insurance law and rules do not directly require insurers to have an internal disputes settlement process. Section 83 of the Insurance Ordinance would appear to provide SECP with the power to prescribe requirements in this area if it wishes to (to date, this power has not been exercised). It is reported that most insurers have put in place some form of internal dispute resolution system (all the life, nonlife, and takaful insurers interviewed asserted they had a system in place). The quality and robustness of these systems is not clear, and there is some concern that smaller or less reputable insurers may provide limited support for internal dispute resolution. The IAP Code of Conduct makes no reference to dispute resolution processes (internal or external). SECP intends to include requirements with regard to complaint handling for microinsurance products in the microinsurance regulations and guidelines currently being developed (Section F2). SECP Consultation Paper covers both life and nonlife insurance. This raises the possibility of establishing a more consistent approach to the development of strengthened internal complaint-handling processes for all types of insurance. b. As above, such designated employees are not required by insurance law or rules. Also, as above, it is reported most insurers have designated employees to redress complaints, although that may not be their sole focus. The quality and robustness of these systems is not clear, and there is some concern that smaller or less reputable insurers may provide limited support for internal dispute resolution. c. SECP Circular No. 18 of 2011 requires all insurers to display on their websites "The information relating to claim/grievance handling mechanism/procedure in detail" no later than January 15, 2012. d. SECP does not investigate whether insurers comply with their internal complaints procedures.

	Overall there is wide, if not universal, agreement on a need for internal dispute resolution processes to be strengthened and insurance users, particularly retail insurance users, made more aware of them and their rights.
Recommendations	**E.1-1.** SECP should consider formalizing minimum requirements for internal dispute resolution processes for all insurers and insurance products, preferably in collaboration with the industry, and then monitors the effectiveness of insurers' internal dispute resolution processes. **E.1-2.** SECP should finalize and implement the microinsurance rules that allow for internal dispute resolution mechanisms by insurers for microinsurance products. **E.1-3.** SECP should collect and analyze data from all industry participants regarding the numbers, causes, and resolution of internal disputes. Such matters are related to the market conduct of insurers and so it appears that Section 83 of the Insurance Ordinance provides SECP with the power to do this.
Good Practice E.2	***Formal Dispute Settlement Mechanisms*** **a. A system should be in place that allows consumers to seek affordable and efficient third-party recourse, which could be an ombudsman or tribunal, in the event the complaint with the insurer cannot be resolved to the consumer's satisfaction in accordance with internal procedures.** **b. The role of an ombudsman or equivalent institution vis-à-vis consumer disputes should be made known to the public.** **c. The ombudsman or equivalent institution should be impartial and act independently from the appointing authority and the industry.** **d. The decisions of the ombudsman or equivalent institution should be binding on the insurers. The mechanisms to ensure the enforcement of these decisions should be established and publicized.**
Description	a. The Insurance Ordinance specifies three types of external dispute resolution process: (i) Small Disputes Resolution Committees (Section 117). SECP Circular No. 4 of 2007 purports to establish a Small Disputes Resolution Committee. This committee has never met. It is intended that the committee adjudicate on a restricted set of types of life and nonlife policies, deal with claims less than a specified ceiling, and have its decisions be binding on all parties. Although the concept may be useful, the implementation has failed. (ii) Federally Constituted Insurance Tribunals (Part XV). These tribunals have the powers of civil courts, and decisions may be appealed only to the high court. SECP Circular No. 15 of 2006 announced that in October 2006, the federal government established four provincially limited (Punjab, Sindh, Khyber Pakhtunkhwa, and Balauchistan) insurance tribunals by conferring the powers of an insurance tribunal on specified district and sessions judges. Claim amounts more than PRs 100,000 may be appealed to the relevant provincial high court. The linkage between these provincial courts and SECP for insurance matters is not strong and should be improved so that the provincial courts have access to the appropriate level of current insurance expertise when

	making their decisions. (iii) A Federal Insurance Ombudsman (Part XVI). The insurance ombudsman may investigate allegations of misadministration (Section 127(2)) by insurers. The office of the insurance ombudsman was established in May 2006. Decisions of the insurance ombudsman may be appealed to SECP who will make a final decision. Complainants also retain the right to file a suit against insurers if their complaints are rejected by the insurance ombudsman. The insurance ombudsman may also pass matters on to SECP for further investigation. Information about the insurance ombudsman is not available at the time of the writing of this report.[36] It has been reported that a relatively small number of complaints have been investigated by the Insurance Ombudsman, on the order of 50–100 in recent years. This is a surprisingly low number and is considered to be mostly attributable to lack of awareness or access as opposed to lack of valid complaints. Costs of the insurance ombudsman are met though a levy on the insurance industry collected by SECP. There is also a federal ombudsman (distinct from the insurance ombudsman). Both State Life Insurance Corporation (SLIC) and Postal Life Insurance use this office for external dispute resolution, and both indicated they were unaware of the insurance ombudsman. With PLI being outside the effective ambit of SECP, this is possibly understandable, but the SLIC has been informed of the insurance ombudsman through SECP circulars. The use of the federal ombudsman for insurance matters should be discontinued. Finally, complaints may be made against insurers directly through the legal system. However, it is generally accepted that the legal system in Pakistan is very slow and costly, and so may be impractical for many to use in practice. b. The consensus is that none of the external dispute resolution processes are well known to the public and hence their effectiveness is limited. It is generally accepted that there is a need to raise the awareness among insurance users, particularly retail insurance users, of the possibility of using either the insurance tribunals or the insurance ombudsman for external complaints resolution. It is also accepted that both these routes can be slow. c. The insurance tribunals are, effectively, courts of law and so should be expected to operate with the level of independence and impartiality expected of courts of law. The insurance ombudsman, according to SECP website, "is an autonomous national dispute resolution body which independently and impartially resolves insurance disputes between insurance policyholders and participating companies, absolutely free of cost."

[36] The current insurance ombudsman's website is reported to be http://www.fio.gov.pk, but it has been suspended since October 2012. The mission was not able to meet with the insurance ombudsman while in Pakistan. Consequently annual Insurance Ombudsman Reports and other information were not available to the mission.

	d. Decisions by the insurance ombudsman (or SECP if an insurer appeals there) are binding on the insurer and if not implemented leave the insurer liable to a fine or penalty from SECP. Decisions made by the insurance tribunals follow the prescribed legal processes for enforcement. The argument that there is not a problem with external dispute resolution systems because there are currently not many complaints made through them is rejected, particularly in the retail insurance consumer context. A system that is difficult to use or inaccessible, for whatever reason, will automatically generate low usage. That does not imply there is not a problem, merely that the system is difficult to use. See also the comments re microinsurance in Section E.1. In summary, the external dispute resolution processes for insurance in Pakistan may appear quite good on paper but are not effective in practice for a variety of reasons. The issues to address include lack of access, awareness, and poor functioning, so consequently the implementation, access, and awareness need to be improved for them to be effective for retail insurance consumers.
Recommendations	**E.2-1.** The Small Disputes Resolution Committee(s) need to be either made widely known, functional, and effective (including having appropriate personnel on them, which is not currently the case) or abandoned. **E.2-2.** The insurance tribunals, being effectively courts, need to be both brought into closer liaison with SECP and made genuinely accessible to retail insurance consumers to be effective for retail insurance consumers. **E.2-3.** Effective means for external dispute resolution for microinsurance policyholders need to be developed. Although the court system may be available theoretically, it is not in practice. **E.2-4.** The office of the insurance ombudsman needs to become more widely known, more accessible, and more cost-effective. It is currently not as effective as it should be for retail insurance consumers. **E.2-5.** The SLIC and PLI (assuming they are brought under the effective supervision of SECP) should use the insurance ombudsman and not the federal ombudsman.
SECTION F	**GUARANTEE SCHEMES AND INSOLVENCY**
Good Practice F.1	***Guarantee Schemes and Insolvency*** **a. With the exception of schemes covering mandatory insurance (and possibly long-term insurance), insolvency guarantee schemes are not to be encouraged for insurance because of the opaque nature of the industry and the scope for moral hazard. Strong governance and prudential supervision are better alternatives.** **b. Nominal defendant arrangements should be in place for mandatory**

	insurances such as third-party motor vehicle insurance to cover situations where there is no insured guilty party. **c. Assets covering life insurance mathematical reserves and investment contract policy liabilities should be segregated or at the very least earmarked, and long-term policyholders should have preferential access to such assets in the event of a winding-up.**
Description	a. Insolvency guarantee scheme There is no insolvency guarantee scheme in place for either life or nonlife insurers. The SLIC, being a government-owned insurer, report they have a government guarantee and consider insolvency concerns to not be applicable. Similarly, the PLI report they have a government guarantee. b. Nominal defendant for mandatory insurances The key mandatory insurance cover is third-party motor vehicle insurance (discussed above). The legislation governing this is Chapter XIII of the Motor Vehicles Act 1939 (when this act was repealed, this chapter was not, hence its name as the Saved Chapter). There is no mention of either a nominal defendant or a guarantee fund to address issues that might arise due to insurer bankruptcy, the guilty driver/vehicle not being able to be identified, or the guilty driver not being insured. c. Life insurance—segregation of assets, and policyholder preferential access in case of wind-up Life insurers are required to establish statutory funds (Part III of the Insurance Ordinance). This clearly segregates assets between different types of insurance, establishes a separate shareholder fund, specifies criteria for the referral of all assets, liabilities, and expenses to statutory funds or the shareholder fund, and provides SECP with the power to prescribe rules. The Insurance Ordinance specifies (Sections 26 and 27) certain duties for the appointed actuary and SECP has the power to prescribe further duties (which it has done through the Securities and Exchange Commission [Insurance] Rules, 2002, most recently updated in a notification dated January 9, 2012). These duties include the requirement to provide directors of life insurers with written advice regarding any distribution of capital in a statutory fund (Insurance Ordinance, Section 21(3)) and, more generally, providing an annual *Financial Condition Report* to the boards of insurers (with a confidential copy provided to SECP). The statutory fund approach coupled with the use of an appointed actuary regime provides a strong process for the protection of policyholder interests. There are no comparable requirements of nonlife insurers. In the event of the windup of an insurer, life or nonlife (Part XVIII of the Insurance Ordinance), the court is required to be satisfied that a windup order is in the interests of the policyholders. SECP has a number of powers that it can exercise, including application for directions from the court and obtaining information. With regard to life insurers, additional requirements apply to the application of statutory fund assets with the first priority being application in accordance with Section 405 of the Companies Ordinance, 1984, and the

	second priority being the discharge of policy liabilities referable to the statutory fund. This provides some further policyholder protection in the event of windup of a life insurer. Further commentary: There are other aspects of the supervision and management of insurers, in addition to the segregation of assets (via statutory funds for life insurers in Pakistan) that contribute, possible indirectly, to the protections of consumers and their interests. Several are noted here: (i) Review of products—new or changing For life insurance a "file and use" approach is applied by SECP (following Section 13 of the Insurance Ordinance) with regard to new products and changes to existing products. Under this approach, specific approval to offer new products is not required, but SECP retains the right (for a period of 30 days after full submissions) to direct a life insurer to make changes in the particulars and materials submitted. This is a valuable consumer protection process as it can be employed to prevent (in SECP's opinion) inappropriate policy conditions being applied, inappropriate marketing materials being used, and inadequate (or overly adequate), premiums being charged, among other things. No such requirements apply to nonlife insurers. There is a view that a significant issue facing the nonlife insurance sector in Pakistan is that there is a lot of price cutting and this affects the profitability (and potentially, the ongoing solvency) of the industry. The sale of unprofitable policies is not in the longer-term interests of consumers. However, Section 12(4) of the Insurance Ordinance specifies: "The insurer or applicant shall not be regarded as conducting its business in a sound and prudent manner if it fails to conduct its business with due regard to the interests of policyholder and potential policy-holders." SECP intends to include requirements with regard to submission of product details for microinsurance products in the microinsurance regulations and guidelines currently being developed (Section I2). SECP Consultation Paper covers both life and nonlife insurance. This raises the possibility of establishing a more consistent approach to the development of products for all types of insurance. Also, because health insurance can be offered by both life and nonlife companies, care needs to be taken to avoid introducing regulatory arbitrage into the health insurance market (microinsurance or not). (ii) Role of appointed actuary Life insurers are required to appoint an appointed actuary (Insurance Ordinance Sections 26 and 27). Duties of the appointed actuary include certifying that the terms and conditions of policies issued by the life insurer are "sound and workable" and certifying the premium rates for new products and any changes in premium rates. These duties are clearly in the interests of consumers. As noted earlier, there are no comparable appointed actuary requirements for

	non-life insurers. Section 50(7) of the Insurance Ordinance permits SECP to prescribe actuarial investigations with respect to classes or subclasses of non-life insurance of an insurer or insurers generally.
Recommendations	**F.1-1.** If a fault-based approach is retained with mandatory third-party motor vehicle insurance then the role of the "nominal defendant" should be properly implemented. However, see the prior wider discussion regarding this mandated class of insurance. **F.1-2.** SECP should complete its intention of applying a "file and use" approach to microinsurance products. **F.1-3.** SECP should consider applying a "file and use" approach to nonlife insurance products. **F.1-4.** SECP should consider introducing the appointed actuary and *Financial Condition Report* concepts for nonlife insurers, particularly with regard to matters like premiums that directly affect consumers.
SECTION G	**CONSUMER EMPOWERMENT**
Good Practice G.1	***Broadly Based Financial Capability Program*** **a. A broadly based program of financial education and information should be developed to increase the financial capability of the population.** **b. A range of organizations—including government, state agencies, and nongovernmental organizations—should be involved in developing and implementing the financial capability program.** **c. The government should appoint an institution such as the central bank or a financial regulator to lead and coordinate the development and implementation of the national financial capability program.**
Description	The development of national financial capability program is an issue that is wider and deeper than the insurance sector. The current Nationwide Financial Literacy Programme[37] is noted. This program focuses on budget and money management. However, there needs to be recognition that the insurance sector has some distinct characteristics that must be considered in the development of broader financial capability programs. These include: (i) Mandated insurances Leaving aside the question of how effectively such coverage has been implemented, by virtue of being mandated, such coverage places a higher level of obligation on the government, supervisors, and providers to make the performance and delivery of such products effective, efficient, and cost-

37 The Nationwide Financial Literacy Programme was launched by the State Bank of Pakistan (SBP) in January 2012 under the Asian Development Bank Improving Access to Financial Services Fund. The pilot phase has concluded and is being evaluated prior a rollout on a large scale.

	effective. (ii) Risk-management nature of protection insurance Insurance purchased for protection purposes (as distinct from investment purposes) should not be assessed on a simple "was my premium recovered" basis. The purpose of protection insurance is, in principle, to harness the power of participating in a group so that when an event that is "catastrophic" to an individual occurs, the resources of the group can be used to redress that loss (which is not "catastrophic" for the group). Protection insurance is a risk-management tool, not an investment tool. This can be quite an abstract concept to convey. (iii) Long-term nature of some insurances Some insurance covers, including traditional covers, are long-term contracts and need a long-term perspective. A key feature of such products is that often when the end of the contract is reached, if the objectives have not been achieved, there is no option to start again in some way. This applies to both the protections and investment aspects of insurance contracts. Also, in many cases where insurance contracts have an annual duration, this does not imply the risk they are covering has only an annual duration. A recurring theme in discussions was the need to raise awareness of the role of insurance for consumers. There was also broad agreement that such awareness raising would best be addressed at an industry level or higher as part of a broader financial awareness and literacy program. a. In principle all insurers agreed with this. Little or no work in this direction has been undertaken by the insurance sector to date. A number of insurers, life insurers in particular, noted the potential for industry support for an program to raise awareness of insurance issues. b. There is also general support for a broad-based initiative to develop financial education and awareness. It is understood that SECP is participating in the development of some such broader initiatives. c. The development of a national financial capability program is an issue that extends beyond the insurance sector. However, as noted above, some particular aspects of insurance need to be recognized.
Recommendation	**G.1-1.** SECP should continue to participate in the development of financial capability–building initiatives, recognizing the particular needs of insurance, and seek active involvement and support from the insurance industry.
Good Practice G.2	***Unbiased Information for Consumers*** **a. Consumers, especially the most vulnerable, should have access to sufficient resources to enable them to understand financial products and services available to them.** **b. Financial regulators should provide, via the Internet and printed**

	publications, independent information on the key features, benefits, and risks—and, where practicable, the costs—of the main types of financial products and services. **c. Nongovernmental organizations should be encouraged to provide consumer awareness programs to the public regarding financial products and services.**
Description	The implied presumptions of literacy and the educational capacity to understand matters relating to insurance in the above item need to be recognized. The overall literacy rate in Pakistan is estimated to be just under 60 percent, with a wide disparity between males and females (approximately 70 percent and 45 percent, respectively) and also a wide disparity between urban and rural populations (approximately 75 percent and 50 percent, respectively). a. SECP intends to include requirements with regard to disclosure in the microinsurance regulations and guidelines currently being developed (Section F1). SECP Consultation Paper covers both life and non-life insurance. This raises the possibility of establishing a more consistent approach to developing products for all types of insurance. Where consumers may be more vulnerable, there is a heightened responsibility for intermediaries and their insurers they represent to ensure that they are not taken advantage of. b. Some basic information is available via the Internet with regard to generic insurance products for retail consumers.[38] There appears to be little other independent information available to consumers, in particular regarding costs and comparative premium rates. c. Nongovernmental organizations do little or no work to develop consumer awareness with regard to retail insurance. This could pose problems in the microinsurance market. There appears to be little media or other independent commentator interest in insurance matters to support the development of consumer awareness.
Recommendations	**G.2-1.** SECP should follow through on its intention to develop appropriate disclosure requirements for all microinsurance products. **G.2-2.** SECP and industry should collaboratively seek means for retail insurance consumers to access independent and unbiased information regarding insurance products.
Good Practice G.3	***Measuring the Impact of Financial Capability Initiatives*** **a. Policymakers, industry, and advocates should understand the financial capability of various market segments, particularly those most vulnerable to abuse.** **b. The financial capability of consumers should be measured through a broad-based household survey that is repeated periodically.** **c. The effectiveness of key financial capability initiatives should be evaluated.**
Description	In principle, such initiatives are supported by the insurance industry, especially life insurers who have more contact with retail insurance consumers. From a pragmatic

[38] See the SECP website and their publication "How Insurance Works for You," December 2010.

	point of view such initiatives should be established at a higher level than the insurance industry and be part of a broader program to improve financial awareness and literacy of the population overall. a. In practice, no specific initiatives have been taken by SECP or the insurance industry to measure the financial capability of market segments. b. Such broadly based householder surveys, in particular relating to insurance, have not yet been conducted in Pakistan. c. This, given the prior comments, remains to be assessed.
Recommendation	**G.3-1.** As part of a broader program to develop and measure the changes in financial literacy, SECP and the insurance industry should be encouraged to support financial capability development initiatives. This should include regular surveys to assess financial literacy and assess the impact of initiatives to improve financial literacy.

4. Securities Sector: Good Practices

SECTION A	INVESTOR PROTECTION INSTITUTIONS
Good Practice A.1	***Consumer Protection Regime*** **The law should provide for clear rules on investor protection in the area of securities markets products and services, and there should be adequate institutional arrangements for implementation and enforcement of investor protection rules.** **a. There should be specific legal provisions in the law, which create an effective regime for the protection of investors in securities.** **b. There should be a governmental agency responsible for data collection and analysis (including complaints, disputes, and inquiries) and for the oversight and enforcement of investor protection laws and regulations.**
Description	The Securities & Exchange Commission of Pakistan (SECP) has a strong mandate to protect the rights and interests of investors in the securities sector. SECP Act, 1997, provides a strong mandate for SECP to "strive to maintain confidence of investors in the securities markets by ensuring adequate protector for such investors." SECP has also issued the Broker and Agents Registration Rules, 2001, which requires brokers who fail to resolve an investor's complaint to be liable for suspension and ineligible for registration or licensing by SECP. An open-end fund (CIS) is created as a trust under the Trusts Act, 1882, and the fund is required to be registered with SECP under the NBFC Rules, 2003, with a custodian that meets the eligibility criteria spelled out by SECP. The Mutual Fund Association of Pakistan's (MUFAP's) Code of Conduct introduces minimum requirements for the distributors of mutual funds, including fit and proper criteria to ensure that only those with sufficient level of knowledge and expertise can be registered. SECP has issued Circular No. 35 of 2009 for brokers and Circular No. 34 of 2009 for CIS distributors requiring all brokers, asset managers, and distributors of mutual fund products to have certified a minimum of 20 percent of personnel, or two persons, who deal with clients. Under Circular No. 34, all mutual fund distributors are required to be registered with MUFAP and be certified; the MUFAP code requires certification as well. MUFAP has also proposed a Code of Ethics and Standards of Professional Conduct for asset management companies, but is still awaiting SECP's final approval as required under the Non-Banking Finance Companies Rules, 2003. Investor protection is widely recognized under the securities laws and the rules made pursuant to them. SECP has extensive powers in regard to the registration and regulation of stock exchanges, regulation of issuers, prohibition against market abuse such as insider trading and market manipulation, as well as enforcement powers for breaches against the laws and regulations. The stock

	exchange's internal operations are based on its regulation of trading and membership. These regulations provide for arbitration for the handling of disputes related to activity on the exchange. SECP Act vests SECP with an explicit mandate to resolve complaints between securities brokers and their clients. SECP receives complaints from investors and directs them to the different operations within SECP according to the subject matter. SECP publishes statistics on the nature and number of complaints and their status in its annual reports, but no dedicated centralized unit monitors and analyzes these complaints to ensure effectiveness. However, after the World Bank mission, SECP has established a centralized unit to monitor complaints. SECP collects and publishes statistics on the numbers of consumer complaints filed with SECP, the exchanges, and the broker. After the mission, a centralized unit handled complaints to SECP; before that, complaints from investors were monitored by the Broker Registration & Investor Complaints Wing of the Securities Market Division. Its *2011 Annual Report* provides broad trends in types of complaints and final resolutions. However, statistics are not sufficiently detailed to assist the analysis of the key issues and common trends. For example, based on the statistics[39] on the number and nature of complaints SECP received by year-end 2011, out of 11 categories of complaints received, the one with the largest number of complaints is categorized as "Miscellaneous." This does not provide clarity on the nature of complaints for monitoring purposes. The relevant self-regulatory organizations (SROs) have adopted their own regime for investor protection and maintain data on investor complaints for resolution in a timely manner**.** SECP also takes part in resolving investor complaints independently in case there is any delay by the SROs. Further, SECP has powers to suspend the registration of or impose a fine on a broker who fails to settle an investor complaint that has been adjudicated by an SRO, its committee, or SECP itself. SECP, based on analysis of inspection reports and of the nature of complaints received against the registered brokers, suggests amendments and makes new regulations for market oversight and enforcement. Data regarding initial public offerings (IPOs), debts issue of securities, and their redemption status are maintained by SECP and is available on SECP's website.
Recommendations	SECP can further strengthen its own transparency and accountability regarding treatment of consumer complaints. This is because both disputes and inquiries provide valuable early warning signals to both the intermediaries' management and the supervisor regarding possible future problems. A central location should be established to collect, record, redirect, and publish statistics on complaints related to capital market services. SECP informed the mission that it is in the process of establishing a centralized department to handle complaints, and on December 19, 2012 (after the mission), SECP announced a central service for complaints. The central service within SECP should receive and respond to all securities markets' complaints (even though the central service should pass them on to the financial institution or relevant departments within SECP for them to make necessary inquiries and investigations if necessary. Following the mission (December 19, 2012) SECP announced the launch of a service desk to act as just such a central point to handle complaints and inquiries.

[39]These statistics appear to be provided by the Enforcement Department of the SECP, because no centralized database on complaints is maintained.

	SECP should develop a clients' charter to ensure effective and efficient complaint-handling processes within SECP. The central service within SECP should publish aggregate statistics on the number and nature of complaints received each month (or for the year) and what happened to the complaints - whether they resulted in a resolution by the market intermediary, and of those complaints that went into dispute resolution - the number resolved in favor of the investors and the number in favor of the market intermediary.
Good Practice A.2	***Code of Conduct for Securities Intermediaries (SIs) and Collective Investment Undertakings (CIUs).*** **a. Securities Intermediaries and CIUs should have a voluntary code of conduct.** **b. Securities Intermediaries and CIUs should publicize the code of conduct to the general public through appropriate means.** **c. Securities Intermediaries and CIUs should comply with the code and an appropriate mechanism should be in place to provide incentives to comply with the code.**
Description	Brokers are registered with SECP under Brokers and Agents Registration Rules, 2001 (BARR 2001), which mandate that all registered brokers shall comply with the code of conduct as prescribed in Third Schedule to the BARR 2001. Further relevant stock exchanges have also laid down their own code of conduct through the general regulations under which all brokers and their employees are required to abide by the same. The existing Code of Conduct for Brokers provides for the following: • General: integrity, exercise of due skill and care, manipulation, compliance with statutory requirements • Duty to the Investor: execution of orders, issue of contract note, breach of trust, business and commission, business of defaulting clients, fairness to clients, investment advice, broker competence • Broker vis-à-vis other Brokers: conduct of dealings, protection of clients' interest, transactions with brokers, publicity, inducement of clients, false or misleading returns • Brokers vis-à-vis Commission and Stock Exchange: general conduct, failure to give information The Code of Conduct for Debt Securities Trustees is covered under Schedule II of the Debt Securities Trustees Regulations, 2012. The Mutual Funds Association of Pakistan "MUFAP" has drafted a Code of Ethics and Standards of Professional Conduct for Asset Managers that provides for business conduct standards of asset managers andis still awaiting SECP's approval at mission date. SECP, through a

	September 2011 SRO, amended the Non-Banking and Notified Entities Regulations, 2008, which introduced the MUFAP registration requirements for distributors and the need for the distributors to abide by the Code of Qualification and Conduct for Registered Service Providers that came into effect in July 2012. Through the code of conduct, the MUFAP has introduced entry minimum requirements, including fit and proper criteria. In order to revamp the existing code of conduct, SECP is in the process of implementing new code of conduct for stockbrokers in light of International Organization of Securities Commissions (IOSCO) principles and international best standards that broadly cover the following sections: • Act honestly, fairly, and with integrity • Due skill, care, and diligence • Adequate resources and procedures • Information from clients • Information to clients • Conflicts of interest • Compliance • Client assets • Dealing with other brokers • Investor grievances In Pakistan, the brokers' code of conduct is prescribed as a subsidiary legislation by SECP rather than by the stock exchange. Over the years, the stock exchanges have adopted some aspects of business conduct standards in their general regulations and instructions to their members. With the recent demutualization of stock exchanges, there is a need to rationalize the business conduct standards in the regulatory framework in the form of the codes of conduct. This is because regulation comes with a cost and it would be more important that industry participants are actively involved in developing and promoting high conduct standards than for such standards to be "legislated." What are critical are the legal consequences that would flow with breaches of business conduct rules by financial service providers. The MUFAP, as a relatively new SRO, has taken the initiative to propose a Codes of Ethics of Professional Conduct for Asset Managers (still not approved by SECP at mission date) as well as for distributors of mutual funds (approved by SECP). However, none of the codes of conduct is well known to investors, even to the members of each association.
Recommendations	The codes of conduct should be placed in brokers' branches and intermediaries' retail offices and websites. The value of a code of conduct is its widespread distribution so that consumers know that, in principle, financial institutions have agreed to provide minimum levels of service and to respond to complaints and disputes. Consumers should be advised upfront that if an intermediary fails to comply with the code of conduct, a complaint can be submitted to the institution, the professional association, and SECP.

	There should be a strong mechanism to investigate code of conduct breaches, including the possibility that these breaches be publicized and that SECP use these breaches as early warning signals. Industry codes of conduct should be developed for each segment of the financial sector, or one could be prepared for use across the securities sector. Codes should be as similar as possible across segments, ideally based on basic common rules for all segments, with specifics added for individual segments, to make sure conditions are equal for financial products that have similar features but are legally different (such as mutual funds and structured and leveraged products). A policy of "comply or explain" could be useful to strengthen the enforcement of codes of conduct that go beyond regulatory requirements. Under this policy, the financial institution is assumed to comply with the code of conduct, otherwise the financial institution would have to explain reasons for noncompliance. Noncompliance and non-explanation would be considered misleading business practices and be subject to sanctions. The same policy could be applied to standard contract provisions; the need to deviate from a standard contract provision would have to be explained.
Good Practice A.3	***Other Institutional Arrangements*** **a. The judicial system should provide an efficient and trusted venue for the enforcement of laws and regulations on investor protection.** **b. The media should play an active role in promoting investor protection.** **c. The private sector, including voluntary investor protection organizations, industry associations, and, where permitted, self-regulatory organizations, should play an active role in promoting investor protection.**
Description	The judicial system as one of the venues for investors to bring complaints against a securities intermediary is expensive and time consuming and does not appear to be useful for small complaints by retail investors. Pakistan has a three-tiered judicial system. There is one high court in each province, and one in the federal capital, Islamabad. These are the appellate courts for all civil and criminal cases in each respective province. District courts exist in every district of each province, and have civil and criminal jurisdictions. District and sessions judges have executive and judicial power over all the districts under their jurisdiction. The sessions court is a trial court for various offenses and the appellate court for summary conviction offenses and low-value civil suits. The high court of each province has appellate jurisdiction over the lower courts. The supreme court has exclusive jurisdiction over disputes between and among provincial governments, and appellate jurisdiction over high court decisions. The media's role on investor protection issues is limited by the information that is provided to them.

	Registered SROs and industry associations play a role in promoting fair and transparent trading and safeguarding investors' interests and assets in their respective capacities. The SROs have dedicated staff for dealing with investor protection issues. The Financial Markets Association of Pakistan, formed in 1997, is a noncommercial, nonprofit, self-financed, professional association of dealers of financial instruments. The members of the association are drawn from dealing room staff of all nationalized banks, foreign banks, private sector banks, NBFCs, and foreign exchange/money market interbank brokerages houses. The Financial Markets Association of Pakistan (FMAP) has about 285 members, who annually elect the governing body. The FMAP has recently been granted SRO status with a mandate from the State Bank of Pakistan, and will work toward achieving the tasks elaborated in the Mission Statement. FMAP is affiliated with "Association Combsite Internationale - Paris", like other similar national associations across the world. FMAP is also recognized as Self-Regulatory Organization (SRO). There is hardly any consumer organization that focuses on financial products or services.
Recommendations	The media and industry associations should be encouraged to promote awareness of consumer protection. SECP should encourage involvement of consumer organizations by engaging with them on policy formulation. In view of the weak capacity of the courts, the establishment of a financial ombudsman for the disputes between investors and securities intermediaries would be critical because it would provide a speedy, efficient, and cost-effective avenue for dispute resolution. And, as noted in the section on banking in this diagnostic, it would be helpful to further strengthen the system of consumer advocacy organizations, including non-profit credit counseling centers. SECP should consider consultation with consumer advocacy organizations on a regular basis in the preparatory work on legislation affecting consumers of financial services in the securities sector.
Good Practice A.4	***Licensing*** **a. All legal entities or physical persons that, for the purpose of investment or speculation, solicit funds from the public should be obliged to obtain a license from the supervisory agency.** **b. The securities supervisory agency should have broad powers to investigate fraudulent schemes.**

Description	The securities laws require that all persons who solicit funds from the public need to be authorized by SECP. Hence, an issuer that intends to raise funds from the general public is required to get approval from SECP under Section 57 or 62 of the Companies Ordinance, 1984. If a prospectus includes any untrue statement, every person who signed or authorized the issue of the prospectus is punishable with imprisonment for a term that may extend to two years, or with a fine that may extend to PRs 10,000, or both (Section 60 of the Companies Ordinance, 1984). In addition, any person who, either by knowingly or recklessly making any statement, promise, or forecast that is false, deceptive, or misleading, or by any dishonest concealment of material facts, induces or attempts to induce another person to enter into, or to offer to enter into (i) any agreement for, or with a view to, acquiring, disposing of, subscribing for, or underwriting shares or debentures; or (ii) any agreement the purpose or pretended purpose of which is to secure a profit to any of the parties from the yield of shares or debentures, or by reference to fluctuations in the value of shares or debentures; is punishable with imprisonment of either description for a term that may extend to three years, or with fine that may extend to PRs 20,000, or with both. Moreover, any misstatement in the prospectus will attract penal action as mentioned in Sections 59 and 60 of the Companies Ordinance, 1984. Agents and branch managers of the brokers are required to be registered with SECP under the BARR 2001; educational qualifications and experience are also prescribed therein. They are also bound to seek permission from the relevant stock exchanges. However, the law does not stipulate fit and proper criteria for the registration of securities and commodity futures brokers that are corporate entities. Currently, under the BARR 2001 and the relevant rules for commodity brokers, fit and proper criteria are specified in relation to the registration of individual agents of such brokers. Even though SECP has mitigated this gap by requiring directors and the chief executive of a broker to meet minimum eligible criteria, it is nonetheless insufficient. The above aspects of fit and proper will be covered under new Broker Rules being developed by SECP. Third-party investment advisors are required to be registered with the commission under the Investment Companies and Investment Advisers Rules, 1971.
Recommendations	The brokers' and agents' rules for both securities and commodities brokers should be amended to, among other things, incorporate a fit and proper criteria and requirement for high capital standards for brokers that are corporate entities. This should reduce risks to investors of loss caused by negligent or illegal behavior or inadequate capital of the brokers. In addition, it will be critical to introduce an advanced risk-based supervision system for identifying the brokers that are at highest risk for noncompliance and misconduct.

SECTION B	**DISCLOSURE AND SALES PRACTICES**
Good Practice B.1	***General Practices*** **There should be disclosure principles that cover an investor's relationship with a person buying or selling securities, or offering to do so, in all three stages of such relationship: pre-sale, point of sale, and post-sale.** **a. The information available and provided to an investor should inform the investor of:** **(i) the choice of accounts, products, and services;** **(ii) the characteristics of each type of account, product, or service; and** **(iii) the risks and consequences of purchasing each type of account, product, or service.** **b. A securities intermediary or CIU should be legally responsible for all statements made in marketing and sales materials related to its products.** **c. A natural person acting as the representative of a securities intermediary or CIU should disclose to an investor whether he is licensed to act as such a representative and by whom he is licensed.**
Description	Under the Brokers' Code of Conduct that is prescribed by SECP and the directive issued in February 2008 (and therefore part of the regulatory measures implemented by SECP), there are broad disclosure principles that cover an investor's relationship with a person buying or selling securities, or offering to do so, in all three stages of such relationship. For example, at the time of opening of an account, the general disclosure is made to an investor regarding inherent risks associated with investment and trading in the capital market. Similarly, pursuant to the Non-Banking Finance Companies and Notified Entities Regulations, 2008, SECP has imposed broad responsibilities on the asset managers and trustees of the CIS. In respect of trading in leverage markets, brokers are obligated to ensure that all risks involved in the relevant transactions are fully disclosed and they have obtained a written confirmation from clients that they have understood and have the ability to bear the risks in such transactions. In cases of IPOs, all material information as mentioned in the second schedule to the Companies Ordinance, 1984, are required to be disclosed in the prospectus for potential investors. The information includes financial information, information about the issuer and its project, information about all risk factors, and memoranda and articles of association of the issuer. Under Section 59 of the Companies Ordinance, in cases of any loss or damage to every person who subscribes for or purchases any share or debentures on the faith of the prospectus, the following persons of the concerned company shall be liable to pay compensation to them: • every person who is a director of the company at the time of the issue of the prospectus;

	• every person who has authorized himself to be named and is named in the prospectus either as a director, or as having agreed to become a director, either immediately or after an interval of time; • every person who is a promoter of the company; and • every person who has given consent to the issue of the prospectus under Section 55 or Subsection (5) of Section 57. Representatives of brokers who operate through a branch office of the broker are required to disclose that they are registered with SECP as agents under the BARR 2001. Brokers, CIUs, and asset managers are fully responsible and liable for all the dealings and acts of agents and employees in accordance with the Rules & Regulations of the Exchange; Securities and Exchange Ordinance, 1969; Securities and Exchange Rules, 1971; and Brokers and Agents Registration Rules, 2001.
Recommendations	There is certainly a need to modernize the securities law and regulations on principles relating to an investor's relationship with a person buying or selling securities, or offering to do so, in all three stages of such relationship: pre-sale, point of sale, and post-sale. The current provisions—which are scattered—do not clarify which part of the sales product cycle the principles on fair dealing and disclosure relate to. Hence, the securities law (or relevant subsidiary legislation) should be amended to provide greater guidance on what is meant by unreliable and misleading advertisement by securities intermediaries. For example, there are no detailed regulations on permissible advertising practices in the securities sector, other than the general requirement not to make misleading statements. The result of the lack of specific guidance is that compliance with the abovementioned rules would inevitably depend on an individual broker/dealer's own interpretation of the general requirements that may not address fully the three stages of the investors' relationship with the broker. In addition, more specific guidance can be provided by SECP in the form of policy explanatory notes to the industry on what may constitute legitimate advertising by securities intermediaries and what is meant by the "unreliable and misleading" advertisement rule under the securities laws.
Good Practice B.2	***Terms and Conditions*** **Before commencing a relationship with an investor, a securities intermediary or CIU should provide the investor with a copy of its general terms and conditions, and any terms and conditions that apply to the particular account.** **Insofar as possible, the terms and conditions should always be in a font size and spacing that facilitates easy reading.** **The terms and conditions should disclose:** **a. details of the general charges;** **b. the complaints procedure;**

	c. information about any compensation scheme that the securities intermediary or CIU is a member of, and an outline of the action and remedies which the investor may take in the event of default by the securities intermediary or CIU; **d. the methods of computing interest rates paid or charged;** **e. any relevant non-interest charges or fees related to the product;** **f. any service charges;** **g. any restrictions on account transfers; and** **h. the procedures for closing an account.**
Description	Under the General Regulations of the Stock Exchange, a member broker firm is required to adopt standard terms and conditions at the time of opening of an account with such broker. The broker provides to the client a copy of the Standardized Account Opening Form (SAOF), which includes minimum terms and conditions that are equally binding on the broker and its client. The terms and conditions are annexed to the SAOF and are available to the client at any point in time. Further, these terms and conditions are also available for access along with the account opening form on the websites of the stock exchanges and some brokers. The SAOF discloses the details of • The issuer of the product • General and specific fees and charges • Interest rate paid or charged • Method of calculation of interest charges • Commissions • Significant tax implications • Any cooling-off period • Complaints procedures • Compensation/dispute resolution scheme and steps to activate • Restrictions on account transfer • Restrictions on withdrawals or realizing an investment • Procedure for closing an account/withdrawals/realizing an investment On the websites of some brokers, the special terms and conditions are provided in English and Urdu, but there is no requirement for plain English.
Recommendations	At its heart, consumer protection is needed to address imbalances of power, information, and resources between consumers and financial institutions, which place consumers at a disadvantage. Securities intermediaries/CIS are very familiar with the terms and conditions of their financial services, but retail consumers may find it difficult or costly to obtain sufficient information on their financial purchases, or to assess complex financial services even when relevant information is disclosed. The overarching aim of any program to strengthen consumer protection is to redress the imbalances of power, information, and resources, by giving individuals clear and complete information that would allow them to make informed decisions, and by prohibiting financial institutions from engaging in unfair or deceptive practices.

	SECP should make sure that the public clearly understands the disclosed standard terms and conditions and knows how to use it to make informed decisions. In spite of contracts that appear to be easy to understand, a common complaint is that consumers did not understand the terms and conditions of the financial service contracts they signed. Consumer testing of the standard terms and conditions may be helpful.
Good Practice B.3	***Professional Competence*** **Regulators should establish and administer minimum competency requirements for the sales staff of securities intermediaries and CIUs, and collaborate with industry associations where appropriate.**
Description	Not all securities and futures brokers who deal with potential and actual customers are required by law to be properly trained and certified. However, SECP has issued Circular No. 35 of 2009 requiring brokers to ensure that at least 20 percent of the number of staff, or a minimum of two employees, who deal with clients are certified by examinations administered by the Institute of Capital Markets (ICM). Hence, at least two or 20 percent (whichever is higher) of the sales agents and professionals of SIs providing investment advice to clients are mandated to obtain certification from the ICM and new professional entrants are required to attain the relevant certification within one year from the date of employment with the SI. To date, no brokers have fully complied with this requirement (The compliance data is for the circular dated June 30, 2011). Sales personnel and traders of brokers should be formally trained through a certified system and licensed to ensure only those who possess professional expertise and competence deal with clients, so that clients make informed investment decisions. This is particularly important in a demutualized environment where a wider range of products would be distributed to investors. The requirement of ongoing staff training on investor protection obligations is not prescribed in the regulatory framework; however, brokers normally arrange training for their staff depending on their internal training requirements.
Recommendations	A standard industry-wide examination for determining the competency of individual personnel in the brokerage industry should be required. Nonetheless, in view of the widespread non-compliance by brokers in respect of this requirement, SECP may wish to consider a “tiered” approach towards accreditation, where different levels of certification are required for products of varying degrees of complexity. For example, a three-tiered level of training for officers of securities intermediaries/CIU distributors would only involve internal training by the securities intermediary/ CIU for those who sell only simple

	services. However, for those personnel who sell complex financial services to retail clients, they should be required to attend training provided by the relevant professional association, with a curriculum approved by the ICM (or similarly qualified body) and SECP. The industry-wide certification should also include training on a code of ethical standards, including issues of conflicts of interest.
Good Practice B.4	***Know Your Customer (KYC)*** **Before providing a product or service to an investor, a securities intermediary or CIU should obtain, record and retain sufficient information to enable it to form a professional view of the investor's background, financial condition, investment experience and attitude toward risk in order to enable it to provide a recommendation, product or service appropriate to that investor.**
Description	Pursuant to the know your customer/customer due diligence (KYC/CDD) guidelines approved by SECP, brokers are required to obtain and document sufficient information on the purpose and intended nature of the account to be opened or maintained with them and develop a profile of the client based on results of client identification and the risk assessment. Information regarding the intended investment plan of the client must also be obtained to the extent possible and should be documented. Further, SECP directive dated February 7, 2003, made it mandatory for the brokers to assess their clients' age, financial situation, investment objective, and investment experience while making any recommendation for buying or selling any security to their clients. In addition to this, a centralized KYC registration organization has been established for securities market investors, verifying KYC information provided by the applicants, and maintaining a KYC database of all clients. The risk profiling of the customer, documenting investment knowledge, and determining the suitability of a particular transaction with specific reference to an investor's unique characteristics will assist in ensuring that the advice being provided adheres to professional standards. Under a Karachi Stock Exchange notice dated March 16, 2012, in regard to Guidelines for the brokers for developing effective Know Your Customer (KYC) and Customer Due Diligence (CDD) policies and procedures, detailed requirements are imposed on brokers to develop KYC/CDD policies in line with international best practices and recommendations from relevant bodies such as the Financial Action Task Force (FATF). The KYC/CDD policy, at minimum, must provide for the following: • Customer identification • Customer risk assessment • Circumstances where enhanced due diligence is required • Ongoing due diligence

	• Circumstances where simplified due diligence can be adopted • Compliance function • Data retention • Training and employee screening Brokers should obtain and document sufficient information on the purpose and intended nature of the account to be opened or maintained with them and develop a profile of the customer based on results of customer identification and the risk assessment. Information regarding the intended investment plan of the customer must also be obtained to the extent possible and should be documented. Brokers must obtain sufficient information to determine the expected source of funding for the account, particularly whether the client shall be receiving or remitting funds in foreign currency The brokers shall ensure the physical presence of the customer at the time the account is opened. In cases of offshore clients or clients in cities where the broker does not have a branch, the broker must apply appropriate procedures, such as verification by a reliable third party or confirmation from previous broker of the clients. When obtaining confirmation from the third parties in different jurisdictions, the brokerage house must consider whether that jurisdiction is following the FATF recommendations.
Recommendation	No recommendation.
Good Practice B.5	***Suitability*** **A securities intermediary or CIU should ensure that, taking into account the facts disclosed by the investor and other relevant facts about that investor of which it is aware, any recommendation, product or service offered to the investor is suitable to that investor.**
Description	The February 7, 2003, directive that SECP issued to brokers on conduct of business states, "A broker shall not recommend to an investor the purchase or sale of a security that is unsuitable given the investor's age, financial situation, investment objective and investment experience. Without limitation, investment in a particular type of security may be considered unsuitable or the amount or frequency of transactions may be excessive and therefore unsuitable for a given investor." Section 42A of the General Obligations of Members/Brokers of the Karachi Stock Exchange in relation to leveraged markets provides that, "in addition to any obligation of a broker/member under the applicable laws, agreements or as specified in the Standardized Account Opening Form, the Broker shall ensure the following: • No transaction is executed by the broker on behalf of a client in the leveraged market unless an appropriate agreement has been executed between the broker and such client. • All risks involved in the relevant transactions have been fully disclosed

	and the broker has obtained a written confirmation from its clients that they have understood and have the ability to bear the risks in such transactions. • The various financing options available to a client. • The creditworthiness of clients is evaluated through a proper credit risk assessment methodology and credit limits are assigned to each client beyond which the client shall not be allowed to take a position in the leveraged market." However, the abovementioned requirements are not accompanied by a civil liability established by law on the brokers and other intermediaries for breach of such a "suitability rule." There is no civil liability in the law to empower investors to claim damages from the brokers should investors suffer loss as a result of brokers' failure to meet their duty to ensure suitability of investments for their clients consistent with their risk profiles. This, therefore, does not facilitate private sector enforcement against the brokers, as is done in other markets. Different investors, due to factors such as age, health, investment goals, and risk appetites, will have different suitability for different types of financial instruments. Determining which investments are appropriate for the investor requires full and clear disclosure of the characteristics of the investment and expert advice as to the benefits and risks. The situation is aggravated by the lack of training on the part of the staff offering the financial instruments, and the fact that market-based financial instruments with high risk (such as margin trading facilities) are offered to investors who may not have the requisite level of sophistication and investment experience. The MUFAP's various business conduct codes provide for fiduciary responsibility and due diligence, but stop short of requiring CIUs to take responsibility to assess the risk profile of their clients and the suitability of particular investments for their clients when matched against their risk appetite and level of their customers' competence and knowledge on investments. One of the most important vehicles for consumer protection in the securities market is the requirement that a broker or collective investment undertaking advise a client as to the suitability of an investment for the client. This can be done only if the broker knows the financial situation and investment goals of the client. There is also no requirement for a Key Facts Statement to be provided to a customer by brokers and CIUs. Key Facts Statements should be developed for all basic retail securities services and products and should lay out the key terms and conditions, including fees and charges, for all types of retail financial services.
Recommendations	Special training should be established for those intermediaries who deal with retail customers. As a starting point, regulations (or legislation) should introduce the concept of those who work with the public and sell financial services to consumers. Then the financial supervisory agencies and professional associations

	should collaborate to set competency requirements for staff of financial institutions who work with retail customers. The securities law should be amended to establish a civil liability as a basis for civil claims against intermediaries who fail to assess the suitability of investments for investors. This would empower investors to claim in a court of law damages they may suffer as a result of breaches of the suitability rule by such intermediaries. The codes of conduct for brokers and CIU and other investment advisors should be amended to make clear this requirement that a broker or CIU or investment advisor advise a client on the suitability of an investment for the client. In addition, the industry codes of conduct should provide for Key Facts Statements for all basic retail securities services and products in consultation with SECP. Such a Key Fact Statement should lay out the key terms and conditions, including fees and charges, for all types of retail financial services.
Good Practice B.6	***Sales Practices*** **Legislation and regulations should contain clear rules on improper sales practices in the solicitation, sale and purchase of securities. Thus, securities intermediaries, CIUs and their sales representatives should:** **a. Not use high-pressure sales tactics;** **b. Not engage in misrepresentations and half-truths as to products being sold;** **c. Fully disclose the risks of investing in a financial product being sold;** **d. Not discount or disparage warnings or cautionary statements in written sales literature;** **e. Not exclude or restrict, or seek to exclude or restrict, any legal liability or duty of care to an investor, except where permitted by applicable legislation.** **Legislation and regulations should provide sanctions for improper sales practices.**
Description	The regulatory framework does not contain clear and comprehensive rules for disclosure and sales practices. SECP's Directive dated 7 February 2003 on conduct of business by brokers only specifies minimum standards of market conduct for brokers. It does not provide in greater detail clear rules on improper sales practices in the solicitation, sale, and purchase of securities. For the brokerage industry, this is particularly relevant in the context of margin trading where investors trade on a leveraged basis and may not understand the full extent of the risks involved. Before making any purchases, consumers should receive easy-to-understand information about financial services. Once a service has been bought, consumers should receive clear information about any changes to terms and conditions—and be able to withdraw without penalty to the consumer where the changes are not satisfactory.

	Section 3.5 of the MUFAP Code of Ethics of Professional Conduct has explicit provisions on professional selling practices: "Members shall not use any unethical means to sell, market or induce any investor to buy their products and schemes. Members shall not make any exaggerated statement regarding performance of any product or scheme. Members shall endeavor to ensure that at all times: • Investors are provided with true and adequate information without any misleading or exaggerated claims to investors about their capability to render certain services or their achievements in regard to services rendered to other clients; • Investors are made aware of attendant risks in members' schemes before any investment decision is made by the investors; • Copies of prospectus, memoranda and related literature is made available to investors on request; • Adequate steps are taken for fair allotment of mutual fund units and refund of application moneys without delay and within the prescribed limits." Robust disclosure and sales practices would require that providers and distributors of investment products consider the impact of their action (or inaction) on the customer in various stages of the product lifecycle, or the various stages of provision of the service. Depending on the precise nature of a firm's business, this could mean addressing the fair treatment of customers at the following stages: design and governance; identifying target markets; marketing and promotion; sales and advice processes; after-sales information; and service and complaint handling. When providing information to customers, a firm should pay regard to its target market, including its likely level of financial capability; should take account of what information the customer needs to understand the product or service, its purpose and the risks, and communicate information in a way that is clear, fair, and not misleading; and should have in place systems and controls to manage effectively the risks posed by providing information to customers. In the area of post-sale responsibility, a firm should (i) in supplying information directly to the customer, ensure that the information is communicated in a way that is clear, fair, and not misleading; (ii) periodically review products whose performance may vary materially, to check whether the product is continuing to meet the general needs of the target audience that it was designed for, or whether the product's performance will be significantly different from what the provider originally expected and communicated to the distributor or customer; and (iii) act fairly and promptly when handling claims or when paying out on a product that has been surrendered or reached maturity. In doing this, the provider should meet any reasonable customer expectations that it may have created with regard to the outcomes or how the process would be handled.
Recommendations	SECP should ensure that useful comparative information is available for consumers regarding costs of transactions in securities markets and investment products. The industry association (in this case, the MUFAP and relevant exchanges) should publish information (or require that their intermediaries publish data) to allow easy comparisons of fees, charges, and commissions

	charged for that service. Publication of the different costs by each institution would allow consumers to conduct accurate cost comparisons. The result would be informed consumers and an increasingly competitive securities sector. SECP should require market intermediaries who distribute investment products including margin trading facilities and mutual funds to provide their customers with a Key Facts Statement (KFS). The KFS would disclose in simple language the costs, returns, and risks relating to the type of investment product that is marketed to the customer. A KFS for all standard retail financial products would help consumers understand material conditions of their contracts. For financial products, consumers need a short description written in plain language that is comparable across products provided by different institutions. For example, for a consumer credit, the KFS should provide a summary in a page or two of all key terms and conditions. This would include (i) all fees—particularly prepayment and overdue penalty fees—and any other charges that could potentially be incurred; (ii) any required deposits or advance payments; and (iii) the contact information for submission of inquiries, complaints, and disputes. In particular, the Key Facts Statement should indicate the name of the department (with telephone and fax numbers and e-mail address) where inquiries, complaints, and disputes can be submitted to the intermediary. Hence, an easily similarly readable and comprehensible Key Facts Statement should appear at the front of all proposal and policy documents. The Key Facts Statements would not replace the contract for legal purposes. It is therefore recommended that the standard formats for Key Facts Statements be developed by the SROs. SECP should also review and comment on the formats (e.g., to ensure that they provide material information that would not mislead consumers) but the preparation of the formats would best be done by the respective SROs. Cooling-off periods should be set for complex structured products. Cooling-off periods are an effective method of protecting consumers from high-pressure sales tactics and giving them an opportunity to study their investments and make a final decision. During this period, the service provider is not permitted to change the terms of the agreement without the approval of the customer. Cooling-off periods are also important for any service that has a large savings component.
Good Practice B.7	***Advertising and Sales Materials*** **a. All marketing and sales materials should be in plain language and understandable by the average investor.** **b. Securities intermediaries, CIUs and their sales representatives should ensure their advertising and sales materials and procedures do not mislead the customers.** **c. Securities intermediaries and CIUs should disclose in all advertising, including print, television and radio, the fact that they are regulated and by whom.**
Description	In the code of conduct on the duty of brokers to investors, a broker is required not to encourage sales or purchases of securities with the sole object of generating

	brokerage or commission. A broker shall not furnish false or misleading quotations or give any false or misleading advice or information to a client with a view of inducing the client to do business in particular securities and enabling the broker to earn a commission thereby. Pursuant to the February 7, 2003, directive to brokers on conduct of business, SECP requires a broker to not misrepresent material facts concerning an investment. Examples of information that may be considered material and that should be accurately presented to an investor include the risks of investing in a particular security, the charges or fees involved, the company's financial information, or any other material information. Section 3.6 of the MUFAP Code of Ethics of Professional Conduct has explicit provisions on advertisements and promotional materials. In addition to rules relating to advertising and promotional materials contained in the regulations, "Members when advertising or promoting their mutual funds should not be deceptive, ambiguous or make false or misleading statements. The principle of honesty and greatest accuracy must underlie all promotional statements. A promotional statement should be clearly distinguishable as a statement issued with the intent of promoting the investment, service or firm to which it relates. Published information in advertisements and promotional materials must be substantiated. "To avoid misleading advertisements and promotional materials on comparative performance of mutual funds, comparative performance data, which has been awarded or issued by a reputable agency or person approved or accredited by MUFAP may be published in an advertisement. The performance data used must be current and should only be used in advertisements if awarded or issued within the last twelve calendar months. The publication of performance data must be in accordance with criteria prescribed in the advertising and promotional materials contained in the Regulations. Personal opinions shall be clearly identified as such." In addition, the MUFAP has prepared a draft Code on Advertising & Communications Standards for the Mutual Funds Industry of Pakistan and was awaiting SECP's approval at mission date. The draft code contains detailed standards on honesty in advertising and presentation of promotional materials; language and graphics in regard to issues relating to pricing, guarantees, comparison of performance, and use of comparative indices, fees, and commissions; and rates of return, among other things. Section 60 of the Companies Ordinance creates a criminal liability for misstatements in prospectuses. Where a prospectus includes any untrue statement, every person who signed or authorized the issue of the prospectus shall be punishable with imprisonment for a term up to two years, or a fine up to PRs 10,000, or with both, unless he proves either that the statement was immaterial or that he had reasonable ground to believe, and did up to the time of the issue of the prospectus believe, that the statement was true.

Recommendations	Clear laws and regulations—and effective enforcement mechanisms—are needed to ensure meaningful disclosure of consumer financial products. In spite of contracts that appear to be easy to understand, a common complaint is that consumers did not understand the terms and conditions of the financial service contracts they signed. For all regulations regarding consumer disclosure, SECP should make sure that the public clearly understands the disclosed information and knows how to use it to make informed decisions. Consumer testing of proposed disclosure rules or formats would be helpful. Supervision of advertising in the securities market should also be strengthened by SECP. However, responsibility for the implementation and enforcement of advertising and marketing rules for the securities market should be supervised not just by SECP but also by SROs such as the exchanges and the MUFAP.
SECTION C	**CUSTOMER ACCOUNT HANDLING AND MAINTENANCE**
Good Practice C.1	***Segregation of Funds*** **Funds of investors should be segregated from the funds of all other market participants.**
Description	There are no specific provisions in the securities laws that mandate the segregation of funds of customers from market participants. SECP's Directive to Brokers on Conduct of Business dated February 7, 2003, contains the indirect requirement for "a broker not to remove funds or securities from an investor's account without the investor's prior authorization." Pursuant to the Non-Banking Finance Companies and Notified Entities Regulations, 2008, Section 57, requires a trustee of an open-end scheme or closed-end scheme to take under its control all the property of the scheme and hold it in trust for the unit or certificate holders in accordance with the rules, regulations, and provisions of the constitutive documents, and the cash and registerable assets shall be registered in the name of, or to the order of, the trustee. The General Regulations of the Karachi Stock Exchanges require that the brokers shall ensure that the assets belonging to their clients are kept separated from the assets of the broker. Clause 41 of the regulations provide that (i) The brokers shall ensure that the assets belonging to their clients are kept separated from the assets of the broker. For this purpose, the broker shall maintain (a) A separate bank account that will include all the fund deposits of their clients along with a record of clients' balances. (b) Separate subaccounts under his participant account in the Central Depository System (CDS) for each of his clients to maintain the custody of margins deposited by the clients in the form of securities and securities bought for clients. (c) A collateral account under his participant account in the CDS for all

	clients. (ii) Except as permitted above, the clients' funds and securities shall not be used by the broker for any purpose other than as authorized by the client in writing in the manner and procedure prescribed by the Exchange and/or Central Depository Company. In order to ensure this, the broker is required to maintain a separate bank account and subaccount for each client with the designated banks and central depository company of Pakistan, respectively.
Recommendation	The securities laws should be amended to provide clear statutory requirements that brokers must ensure that funds of their customers are segregated from their own funds. The Exchange General Regulations can continue to function to complement such a statutory requirement.
Good Practice C.2	***Contract Note*** **Investors should receive a detailed contract note from a securities intermediary or CIU confirming and containing the characteristics of each trade executed with them, or on their behalf. The contract note should disclose the commission received by the securities intermediary, CIU and their sales representatives (expressed as total expenses as a percentage of total assets purchased).**
Description	Pursuant to Rule 4(4) of the Securities and Exchange Rules, 1971, a member executing an order of a customer shall, within 24 hours of the execution of the order, transmit to the customer a confirmation that shall include the information, including the date the order is executed; name and number of the securities; nature of transaction (spot, ready, or forward and also whether bought or sold); price; commission, if the member is acting as a broker; and whether the order is executed for the member's own account or from the market. There is also the requirement that the trade confirmation statement should disclose the brokerage commission or any other charges in connection with the brokerage services rendered. The abovementioned provision is mirrored in Section 42 of the Karachi Stock Exchange's General Regulations as follows: "Whenever an order of any client has been executed by a Broker, confirmation of such execution shall be transmitted to the said client by the Broker within 24 hours of the execution of such transaction through any previously agreed mode of communication as specified in the Standardized Account Opening Form. The confirmation order shall precisely include the following specific information: a) Date on which order is executed; b) Name and number of securities; c) Nature of transaction (SPOT, Ready, Future, Leveraged Market, Debt Market and also whether bought or sold); d) Price; e) Commission rate;

	f) Whether the order is executed for the member's own account or from the market. {Rule 4(4) of Securities & Exchange Rules, 1971)". Although **there are clear requirements for the issuance of a contract note, there does not appear to be** a standardized format or at least standardized terms for contract note.
Recommendation	A useful step would be for the SROs (stock exchanges and professional associations such as MUFAP) to develop standardized contracts—or at least standard provisions of contracts. Standardized contracts could be developed by such an SRO, which would recommend the contracts for use by the financial institutions that are members of the associations. The standardized contract should include all the key terms and conditions of the financial product or service. For individuals, standardized contracts would be an effective measure for consumer protection.
Good Practice C.3	***Statements*** **An *investor* should receive periodic, streamlined statements for each account with a securities intermediary or CIU, providing the complete details of account activity in an easy-to-read format.** **a. Timely delivery of periodic securities and CIU statements pertaining to the accounts should be made.** **b. Investors should have a means to dispute the accuracy of the transactions recorded in the statement within a stipulated period.** **c. When an investor signs up for paperless statements, such statements should also be in an easy-to-read and readily understandable format.**
Description	Pursuant to the special terms and conditions at account opening, the customer who is an account holder has a right to obtain from the broker a copy of his or her ledger statement under official seal and signature of the broker or his authorized representative on a periodic basis on the customer's written request. For commodities futures contracts, the customer of the broker will be provided a detailed report containing the matched and unmatched trades before the end of the expiration date of the futures contract. In addition to the above, the broker is responsible for sending to each client, on a quarterly basis, a holding balance statement showing the number of every book-entry security entered in the account of that client. Further, the CDC may directly send holding balance statements to randomly selected subaccount holders from time to time. The aforementioned statement must be sent on a monthly or quarterly frequency, depending on clients' choice. In case of any discrepancy in the ledger statement, the account holder shall

	inform the broker within one day of receipt of the ledger statement to remove the discrepancy. As an investment account service provided by the Central Depository Company, account balances and activity reports are available to the account holder around-the-clock through CDC access. Electronic statements are generally legible because they conform with the format prescribed for contract notes as mentioned in C.2 above. Under the Non-Banking Finance Companies and Notified Entities Regulations, 2008, an asset management company is obliged to—within one month of the close of first and third quarters and within two months of the close of second quarter of the year of account of the open-end scheme or closed-end scheme—prepare and transmit to the unit or certificate holders, the trustee, the commission, and stock exchanges, on which the units or certificates of the scheme are listed (i) balance sheet as at the end of that quarter; (ii) income statement; (iii) cash flow statement; (iv) statement of movement in unit holders' or certificate holders' fund or net assets or reserves; and (v) statement showing the securities owned at the beginning of the relevant period, securities purchased or sold during such period, and the securities held at the end of such period together with the value (at carrying and at market) and the percentage in relation to its own net assets and the issued capital of the person whose securities are owned for that quarter.
Recommendation	More specific regulations as to the procedure for contesting the accuracy of statements should be placed in the regulatory framework for the securities industry, as well as provisions for paperless statements. Currently, brokers and their customers can agree to exchange information electronically, (inter alia through electronic statements) in the special terms and conditions in the account opening forms. The content of electronic statements should include the same information as paper statements.
Good Practice C.4	***Prompt Payment and Transfer of Funds*** **When an investor requests the payment of funds in his or her account, or the transfer of funds and assets to another securities intermediary or CIU, the payment or transfer should be made promptly.**
Description	Under the stock exchanges' General Regulations, payment and transfer requests of customers of brokers have to be responded to within 24 hours. The broker is responsible to ensure delivery of CDC-eligible securities in the account holder's

	CDC account subject to full payment by the account holder. The broker shall also be responsible for the payment of any credit cash balance available in the account of the account holder, preferably in form of A/c Payee cross cheque only within one business day of the account holder's request. No such provisions appear to be applicable for CIUs. Based on the above and the special terms and conditions in relation to all account opening forms with brokers, although the broker is required to credit the cash balance account of the client within 24 hours, there is no such requirement either in the rules or code of conduct for CIUs. Hence, there can be further strengthening of this requirement in the interest of protecting investors, because this has proven to be a problem in other jurisdictions where it is common practice for broker/dealers and management companies to benefit from the "float"—investing customer assets and receiving income during the delay in paying the customer.
Recommendation	There should be clear provisions in the law or the code of conduct of the SRO that provides for standard terms and conditions between such entities and their clients in requiring asset managers and CIUs to immediately pay the customers any cash balances in their accounts and proceeds from sales when the payment is received.
Good Practice C.5	***Investor Records*** **A securities intermediary or CIU should maintain up-to-date investor records containing at least the following:** **a. A copy of all documents required for investor identification and profile;** **b. The investor's contact details;** **c. All contract notices and periodic statements provided to the investor;** **d. Details of advice, products and services provided to the investor;** **e. Details of all information provided to the investor in relation to the advice, products and services provided to the investor;** **f. All correspondence with the investor;** **g. All documents or applications completed or signed by the investor;** **h. Copies of all original documents submitted by the investor in support of an application for the provision of advice, products or services;** **i. All other information concerning the investor which the securities intermediary or CIU is required to keep by law; and** **j. All other information which the securities intermediary or CIU obtains regarding the investor.** **Details of individual transactions should be retained for a reasonable number of years after the date of the transaction. All other records required under a. to j. above should be retained for a reasonable number of years**

	from the date the relationship with the investor ends. Investor records should be complete and readily accessible.
Description	Rule 8 of the Securities and Exchange Rules, 1971, requires that every member shall prepare and maintain the following in a manner that will disclose a true, accurate, and up-to-date position of his business, namely: (i) journal (or other comparable record), cash book, and any other books of original entry, forming the basis of entries into any ledger; the books of original entry that contain a daily record of all orders for purchase or sale of securities, all receipts and deliveries of securities, and all other debits and credits; (ii) ledgers (or other comparable records) reflecting asset, liability, reserve, capital, income, and expense accounts; (iii) ledgers (or other comparable records) reflecting securities in transfer, securities borrowed, securities loaned, and securities bought or sold, for which the delivery is delayed; (iv) record of all balances of all ledger accounts in the form of trial balances to be prepared at least once every six months of every year of account; (v) record of transactions with the banks; and (vi) contact books showing details of all contracts entered into by a member with other members of the exchange or counterfoils or duplicates of memos of confirmation issued to such other members. Brokers are required to maintain duplicates or counterfoils of memos of confirmation issued to customers. In addition, they have to maintain books of accounts and other documents for a period of not less than five years. Every broker is required under the law to maintain investors' records at all times and open subaccounts of an investor only on the basis of a subaccount opening form duly signed by or on behalf of such investor. Moreover, a broker must also keep in record all types of communications/correspondences exchanged whether in writing or recorded telephonically/electronically and placed on automated trading systems of the exchange in compliance with the relevant rules and regulations. Under the Non-Banking Finance Companies and Notified Entities Regulations, 2008, an asset manager is responsible - a. for maintaining proper accounts and records of the open-end scheme or closed-end scheme that will enable a complete and accurate view to be formed of (i) the assets and liabilities of the open end scheme or closed end scheme; (ii) the income and expenditure of the open end scheme or Closed End Scheme; (iii) all transactions for the account of the Open End Scheme or Closed End Scheme; (iv) amounts received by the Open End Scheme or Closed End Scheme in respect of issues of units;

	(v) pay out by the open end scheme on redemption of units and by way of distributions by the closed end scheme or open end scheme; and (vi) pay out at the termination of the scheme; (e) maintain the books of accounts and other records of the Open End Scheme and Closed End Scheme for a period of not less than 10 years; (f) within four months of closing of the accounting period of the Open End Scheme and Closed End Scheme, transmit to the unit or certificate holders, the trustee, the Commission, and stock exchanges, on which the units or certificates of the scheme are listed, the annual report as per the requirements set out in Schedule V, including (i) copy of the balance sheet and income statement; (ii) cash flow statement; (iii) statement of movement in unit holders' or certificate holders' fund or net assets or reserves; and (iv) the auditor's report of the Open End Scheme or Closed End Scheme; (g) within one month of the close of first and third quarters and within two months of the close of second quarter of the year of account of the Open End Scheme or Closed End Scheme, prepare and transmit to the unit or certificate holders, the trustee, the Commission, and stock exchanges, on which the units or certificates of the scheme are listed (i) balance sheet as at the end of that quarter; (ii) income statement; (iii) cash flow statement; (iv) statement of movement in unit holders' or certificate holders' fund or net assets or reserves; and (v) statement showing the securities owned at the beginning of the relevant period, securities purchased or sold during such period, and the securities held at the end of such period together with the value (at carrying and at market) and the percentage in relation to its own net assets and the issued capital of person whose securities are owned for that quarter, whether audited or otherwise and.ensure ,where it delegates the function of distribution, the written contract with the distributors clearly states the terms and conditions for avoidance of frauds and sales based upon misleading information; (h) be obliged to process payment instrument immediately on receipt of application; and

	(i) be obliged to provide such information and record to the trustee as may be necessary for the trustee to discharge obligations under these Regulations.
Recommendation	No recommendation.
C.6. Fair Treatment of Investors	**A. General** 1. Integrity - A broker shall maintain high standards of integrity, promptitude and fairness in the conduct of all his business. 2. .Exercise of due skill and care - A broker shall act with due skill, care and diligence in the conduct of all his business. 3. Manipulation - A broker shall not indulge in manipulative, fraudulent or deceptive transactions or schemes or spread rumors with a view to distorting market equilibrium or making personal gains. 4. Malpractices - A broker shall not create false market either singly or in concert with others or indulge in any act detrimental to the investors' interest or which leads to interference with the fair and smooth functioning of the market. A broker shall not involve himself in excessive speculative business in the market beyond reasonable levels not commensurate with his financial soundness. 5. Compliance with statutory requirements - A broker shall abide by all the provisions of the act and the rules, regulations issued by the commission and the stock exchange from time to time as may be applicable to him. **B. Duty to the Investor** 1. Execution of orders - A broker, in his dealings with the clients and the general investing public, shall faithfully execute the orders for buying and selling of securities at the best available market price and not refuse to. Deal With a small investor merely on the ground of the volume of business involved. A broker shall promptly inform his client about the execution or non-execution of an order, and make prompt payment in respect of securities sold and arrange for prompt delivery of securities purchased by clients. 2. Issue of contract note - (1) A broker shall not refuse to promptly issue to his clients purchase or sale notes for all the transactions entered into by hi with his clients.(2) A broker shall not refuse to promptly issue to his clients scrip wise lit purchase or sale notes: Provided that an agent shall only split the contract notes client-wise and scrip wise originally -issued to him by the affiliated broker into different denominations; and (3) an agent shall not match the purchase and sale orders of his clients and each such order must invariably be routed through a I: broker of the stock exchange with whom he is affiliated. 3. Breach of trust - A broker shall not disclose or discuss with any other person or make improper use of the details of personal investments and other information of a confidential nature of a client which he comes to know his business

	relationship. 4. Business and commission - (1) A broker shall no~ encourage sales or purchases of securities with the sole object of generating brokerage or commission.(2) A Broker shall not furnish false or misleading quotations or give any false or misleading advice or information to a client with a view of inducing him to do business in particular securities and enabling himself to earn brokerage or commission thereby. 5. Business of defaulting clients - A broker shall not deal or transact business knowingly, directly .or indirectly or execute.an order for. its client who has failed to carry out his commitments in relation to securities With another broker. 6. Fairness to clients - A broker, when dealing with a client, shall disclose whether he is acting as a principal or as an agent and shall ensure at the same time that no conflict of interest arises between him and the client. In the event of a conflict of interest, he shall inform the client accordingly and shall not seek to gain a direct or indirect personal advantage from: the situation and shall not consider client's interest inferior to his own. 7. Investment advice.- A broker shall not make a recommendation to any client who might be expected to rely thereon to acquire, dispose of, retain any securities unless he has reasonable grounds for believing that the recommendation is suitable for such a client upon the basis of the facts, if disclosed by such a client as to his own security holdings, financial situation and objectives of such investment. The broker should seek such information from clients, wherever he feels it is appropriate to do so. 8. Competence of broker - A broker should have adequately trained staff and arrangements to render fair, prompt and competent services to his clients.
	Pursuant to the brokers' code of conduct under the Third Schedule, brokers are required to maintain high standards of integrity, promptness, and fairness in the conduct of all their business. They are to treat their clients honestly and fairly, and act with due skill, care, and diligence in the conduct of all business. A broker is required to give best execution to his customers and disclose all conflicts of interest to its clients. A broker shall not disclose or discuss with any other person or make improper use of the details of personal investments and other client information of a confidential nature he comes to know in his business relationship. A broker shall not furnish false or misleading quotations or give any false or misleading advice or information to a client with a view of inducing the client to do business in particular securities and enabling the broker to earn a commission A broker shall not deal or transact business knowingly, directly, or indirectly, or execute an order for a client who has failed to carry out his commitments in relation to securities with another broker.

	Under Section 67 of the Non-Banking Finance Companies and Notified Entities Regulations, 2008, an investment advisor shall inform the commission before commencement of business and in managing discretionary portfolio and nondiscretionary portfolio of a client, that it shall among other things exercise due diligence, care, and prudence to achieve the investment objective.
Recommendation	The provisions relating to fair treatment of customers of securities intermediaries should be reflected in the securities law (Acts of Parliament). Currently, legal provisions for fair treatment of investors are not consolidated, and it is not apparent reading the main securities laws that such provisions are included until one reads the rules and schedules. SECP has submitted legislative changes to parliament and it would be useful if such legal provisions are presented in the main body of the law itself rather than in subsidiary legislation. The principle of fair dealing and treatment of customers by securities intermediaries is universal and is unlikely to change over time. The benefit of having such provisions in the main body of the law is the clarity and strength it provides on the standard of professional care and conduct expected of securities intermediaries and CIUs.
SECTION D	**PRIVACY AND DATA PROTECTION**
Good Practice D.1	***Confidentiality and Security of Customers' Information*** **Investors of a securities intermediary or CIU have a right to expect that their financial activities will have privacy from unwarranted private and governmental scrutiny. The law should require that securities intermediaries and CIUs take sufficient steps to protect the confidentiality and security of a customer's information against any anticipated threats or hazards to the security or integrity of such information, and against unauthorized access to, or use of, customer information.**
Description	There are no proper constitutional or statutory provisions on privacy issues in Pakistan. Currently, various laws empower federal agencies such as the National Accountability Bureau (NAB), National Clearing Corporation of Pakistan Limited (NCCPL), Federal Investigation Agency (FIA), and other federal agencies to seek information directly from securities intermediaries, CIUs, and the Central Depository Company, information relating to their customers for the purpose of the investigations of such agencies. In Pakistan, consumers are not aware of their rights to privacy. Subject to the above, pursuant to SECP Code of Conduct for Brokers, a broker owes the investor the duty not to disclose or discuss with any other person or make improper use of the details of personal investments and other client information of a confidential nature that he comes to know in his business relationship. Further, in cases of online trading, the brokers has to ensure application of encryption technology, firewalls, and other security measures to prevent intrusions by unauthorized persons. The Code of Ethics of Professional Conduct for asset management companies (AMCs) issued by MUFAP requires AMCs to ensure that their officers do not

	disclose any personal or financial information relating to the investors or clients except where such disclosure has been expressly authorized in writing by such investors or clients or where such disclosure is required to be made to any relevant authority pursuant to any relevant law or legal process.
Recommendation	An information campaign would help consumers learn about their legal rights on protection of personal data. The authorities might wish to consider preparation of an extensive nationwide information campaign, designed to inform consumers about their rights to keep private their personal data.
Good Practice D.2	***Sharing Customer's Information*** **Securities intermediaries and CIUs should:** **a. Inform an investor of third-party dealings in which they should share information regarding the investor's account, such as legal inquiries by a credit bureau, unless the law provides otherwise;** **b. Explain how they use and share an investor's personal information;** **c. Allow an investor to stop or "opt out" of certain information sharing, such as selling or sharing account or personal information to outside companies that are not affiliated with them, for the purpose of telemarketing or direct mail marketing, and inform the investor of this option.**
Description	The laws allow various institutions such as SECP, relevant stock exchanges, NCC, FIA, NAB, and other authorized federal agencies that can solicit client information to aid in carrying out investigation by these institutions. Pursuant to various contractual documents, investors are informed that information relating to their accounts can be shared with the authorized federal institutions as provided in the law only for the purpose of investigation. Contractually, an investor has the right to insist on privacy of information of his account and bar intermediaries from sharing information with third parties except in relation to the provision of information to the institutions that are authorized to receive such information for official use. Nonetheless, it would appear that not many investors are aware of their right to stop or "opt out" of certain information sharing, such as selling or sharing account or personal information to outside companies that are not affiliated with the SIs/asset manager, for the purpose of telemarketing or direct mail marketing.
Recommendations	The securities law should be strengthened to clearly set out the obligation of the securities intermediary and asset manager to provide investors with information on sharing of information and any "opt-out" provisions in the interest of protecting clients' privacy except for those institutions that are authorized by law to require information on investors' accounts. SECP should monitor that intermediaries make known this right of the investor in clear and explicit terms.

Good Practice D.3	***Permitted Disclosures*** **a. The law should state specific procedures and exceptions concerning the release of customer financial records to government authorities.** **b. The law should provide for penalties for breach of investor confidentiality.**
Description	Section 21 of the Central Depository Act (CDA) spells out the permitted categories of disclosures and exceptions (a) which an account holder or a subaccount holder has authorized in writing to disclose; (b) in a case where an account holder or a subaccount holder is declared bankrupt, or, if the account holder or subaccount holder is a company or corporate body and is being or has been wound up within or outside Pakistan; (c) in the case of any litigation or other legal proceedings; (d) to any person duly authorized by a competent court, the Authority or the State Bank of Pakistan (SBP) to investigate into any offense under any law for the time being in force; (e) for the purpose of enabling or assisting the Authority to exercise any power conferred on it by this Ordinance or by any other law for the time being in force; (f) for the purpose of enabling or assisting SBP to exercise any power conferred on it by any other law for the time being in force; (g) for the purpose of enabling or assisting a stock exchange or clearing house of a stock exchange to discharge its functions; (h) for the purpose of enabling or assisting auditors of a central depository or participant to discharge their functions; or (i) to the Authority if the disclosure is required in the interest of investors or in the public interest. Section 22 of the CDA provides for stringent regulation on access to computer systems containing investor account information. Section 28 of the CDA makes it an offense for breaches of the abovementioned provisions. Any person who contravenes these provisions could be fined up to PRs 500,000.
Recommendation	No recommendation.
SECTION E	**DISPUTE RESOLUTION MECHANISMS**
Good Practice E.1	***Internal Dispute Settlement*** **a. An internal avenue for claim and dispute resolution practices within a securities intermediary or CIU should be required by the securities supervisory agency.** **b. Securities intermediaries and CIUs should provide designated**

	employees available to investors for inquiries and complaints. **c. Securities intermediaries and CIUs should inform their investors of the internal procedures on dispute resolution.** **d. The securities supervisory agency should provide oversight on whether securities intermediaries and CIUs comply with their internal procedures on investor protection rules.**
Description	SECP requires all securities intermediaries to have internal complaint-handling procedures for their clients and its onsite inspection examines their effectiveness. Nonetheless, it is not clear if the onsite inspection is effective, especially in the absence of a centralized database of the complaints that are filed with SECP and the securities intermediaries (even though after the mission, a centralized unit within SECP would be consolidating the information relating to the complaints made against SIs/CIUs). There is also concern over the quality of these internal complaint-handling systems and the resources that are allocated by SIs/CIUs (particularly those that are smaller) to support for internal dispute resolution. Although the stock exchanges have information on their websites regarding how to complain against member companies of such exchanges, there are no explicit requirements in the exchanges' member rules that require their members to have minimum requirements on internal complaint-handling procedures. Similarly, Article 3.1.2 of the MUFAP Code of Conduct of Ethics and Professional Conduct for Asset Management Companies provides that a "Member shall establish and maintain written policies and procedures for the effective control and conduct of its business and the activities of their officers to ensure compliance with the Act, the Code and all other relevant laws" and Article 5 provides that "Adherence to the Code is mandatory for all Members and their officers and its provisions will be strictly enforced by MUFAP." The bylaws relating to "The Procedure for Disciplinary Proceedings" have also been drafted by the MUFAP, which will be enforced where necessary. In order to maintain high standards of professional conduct, members or their officers who have breached provisions of the code shall be subject to the appropriate disciplinary proceedings. Nonetheless, there are no explicit provisions in the code that spell out clearly minimum written requirements for internal dispute resolution processes for members.
Recommendations	SECP should assess the quality of the internal complaint-handling procedures and processes for all SIs/CIUs and develop structured processes within its operations to assess the effectiveness of internal complaint-handling operations of the SIs/CIUs. For example, SECP should specifically require that SIs/CIUs provide information to their clients on how to seek a remedy, including redress, for problems arising out of interactions with the securities intermediaries on their websites, and the intermediaries should also be required to prepare an annual report of compliance with their dispute resolution policy to SECP.

	Various SROs, such as the exchanges and MUFAP, would need to review their codes of conduct to ensure that minimum standards and processes on internal complaint-handling be required of their members and develop mechanisms to monitor their effectiveness.
Good Practice E.2	***Formal Dispute Settlement Mechanisms*** **There should be an independent dispute resolution system for resolving disputes that investors have with their securities intermediaries and CIUs.** **a. A system should be in place to allow investors to seek third-party recourse, such as an ombudsman or arbitration court, in the event the complaint with their securities intermediary or CIU is not resolved to their satisfaction in accordance with internal procedure, and it should be made known to the public.** **b. The independent dispute resolution system should be impartial and independent from the appointing authority and the industry.** **c. The decisions of the independent dispute resolution system should be binding upon the securities intermediaries and CIUs. The mechanisms to ensure the enforcement of these decisions should be established and publicized.**
Description	There is no ombudsman system in Pakistan for handling securities complaints, unlike the insurance sector. The securities laws and rules and industry codes do not provide for alternative dispute resolution systems or an ombudsman for market participants (other than those relating to trades executed on the stock exchanges, which may go to arbitration). The stock exchange's internal operations are based on its regulations of trading and membership. These regulations provide for arbitration for the handling of disputes related to transactions effected on the exchange. The "arbitration" process stipulated under these regulations is more akin to mediation involving representatives of brokers and the exchange, and is not necessarily done under the Arbitration Act. In the event that a broker and its customer is not able to resolve their dispute amicably, then either party may refer the dispute to the arbitration proceedings of the stock exchange, and the decision of the arbitration would be binding on both parties. This arbitration process has been found to be largely effective. The Karachi Center of Alternative Dispute Resolution has been operational since February 2007 and has recently signed a Memorandum of Understanding with SECP, among others, to provide input in developing effective alternative dispute resolution systems in the review of stock exchange regulations. Nonetheless, it would appear that to date, the primary arbitration system for the securities market is part of the stock exchanges' framework in relation to trades on its market. As a result, it does not cover all types of complaints, such as a complaint by a customer against CIU. Disputes/complaint cases can be filed with the arbitration committee of the relevant stock exchange where it concerns a securities intermediary, or with

	SECP and handled under arbitration procedures laid down by the relevant stock exchange. Inquiries are conducted through independent auditors or firms on the approved panel of auditors. Investors are informed about the modes available for dispute resolution. An aggrieved party may also approach SECP for resolution of a complaint. SECP has powers to suspend the registration of, or impose a fine on, a broker who fails to settle an investor complaint where such complaint has been adjudicated by an SRO or its committee or by SECP itself.
Recommendations	An out-of-court mechanism such as an ombudsman can take a more flexible approach than the courts for small claims by retail investors. For example, an ombudsman can decide a case not just on the basis of legal rules but also issues of equity and fairness as well as industry-accepted codes of conduct. The ombudsmen should be designed based on principles of transparency, due process, independence, legality, and effectiveness. In view of the fact that the ombudsman structure is already in place for the banking and insurance sectors, it is sensible to extend such an alternative dispute resolution mechanism to retail investors. Even though the arbitration proceedings that are implemented through the stock exchange (primarily the Karachi Stock Exchange) have been found to be largely effective, it nonetheless is not as speedy, low-cost, and efficient as an ombudsman for retail investors. A low-cost Ombudsman for resolution of disputes for retail customers should be considered for the securities sector. The arbitration system should still be maintained for larger disputes. Hence, it is recommended that an inexpensive means for retail investors to obtain redress for small claims should be created by the establishment of an ombudsman for the securities industry. SECP may need to consider the design parameters for such an ombudsman, such as the threshold of claims and whether such an ombudsman should be consolidated with the insurance ombudsman. To ensure a high level of accountability and transparency, the ombudsman should be obliged to publish an annual report describing decisions taken by the ombudsman so that consumers can identify the nature of the disputes referred to the ombudsman and assess the results of the ombudsman's actions.
SECTION F	**GUARANTEE SCHEMES AND INSOLVENCY**
Good Practice F.1	***Investor Protection*** **a. There should be clear provisions in the law to ensure that the regulatory authority can take prompt corrective action on a timely basis in the event of distress at a securities intermediary or CIU.** **b. The law on the investors guarantee fund, if there is one, should be clear on the funds and financial instruments that are covered under the law.**

	c. There should be an effective mechanism in place for the pay-out of funds and transfer of financial instruments by the guarantee fund or insolvency trustee in a timely manner. **d. The legal provisions on the insolvency of securities intermediaries and CIUs should provide for expeditious, cost-effective and equitable provisions to enable the timely payment of funds and transfer of financial instruments to investors by the insolvency trustee of a securities intermediary or CIU.**
Description	SECP possesses powers to issue directions and orders to intermediaries to take prompt corrective action in the event of distress of a stockbroking firm. Two types of guarantee funds are currently maintained: • Investor Protection Fund • Clearing House Protection Fund The Investor Protection Fund is established under the respective regulations of the stock exchanges as part of the overall legal and institutional infrastructure of the securities markets. All stock brokerage firms licensed by SECP are obligated to be members of the Investor Protection Fund. The NCCPL has formed the Clearing and Settlement Fund with an appropriation of PRs 100 million as an initial contribution. The above funds are used to meet members' settlement obligations and other outstanding dues to the stock exchange(s), other members, investors, and so forth in the event of a member's default or expulsion. In February 2012, the investor protection fund was raised from PRs 20 million to PRs 75 million per broker at the Karachi Stock Exchange to offer greater comfort to investors. This amount of PRs 75 million may still be considered insufficient, and the Karachi Stock Exchange has been working towards boosting its funds. In the event of default of a member, in addition to any surplus after distribution of losses, as per the Members' Default and Procedure for Recovery of Losses Regulations of the Exchange, an amount up to PRs 10 million shall be set aside out of the Investor Protection Fund to satisfy the claims of the investors against the defaulting member. In cases of eligible claims of investors determined against the defaulting member exceed the amount available for settlement, such claims shall be satisfied on a pro-rata basis. In addition to the above, a new fund called the settlement guarantee fund is also being envisaged by the Karachi Stock Exchange to be constituted consequent to the clearing company assuming the role of the central clearing counterparty. Regulations of stock exchanges prescribe utilization of a defaulting broker's assets and then the guarantee fund if the broker's assets are insufficient to fulfill its obligations.

	No such investor protection fund is available for the mutual fund industry.
Recommendations	With the demutualization of the stock exchanges, and the proposed enhancement of risk management infrastructure in the setting up of a central counterparty to guarantee the settlement of trades, there is a need to review the legal underpinning of the settlement guarantee fund. The objectives of the review would be to ensure that the counterparty role of the clearing house is not undermined by the application of insolvency law and that the integrity of its risk management infrastructure is protected by law. To do this, the authorities would need to review the Companies Ordinance, the Insolvency law, and Securities law to ensure these legal risks are addressed. In the long term, careful considerations may be given to have an investor protection fund for the mutual fund industry.
SECTION G	**CONSUMER EMPOWERMENT**
Good Practice G.1	***Broadly based Financial Capability Program*** **A broadly based program of financial education and information should be developed to increase the financial capability of the population.** **a. A range of organizations –including the government, state agencies and non-governmental organizations– should be involved in developing and implementing the financial capability program.** **b. The government should appoint a ministry (e.g. the Ministry of Finance), the central bank or a financial regulator to lead and coordinate the development and implementation of the national financial capability program.**
Description	SECP has developed a nationwide capital markets investor education program in collaboration with the three stock exchanges, the mercantile exchange, Central Depository Company, National Clearing Company (NCC), and the Mutual Funds Association of Pakistan. All stakeholders have come together to run a single nationwide program under the brand of the Institute of Capital Markets. The program was launched in July 2012. The investor education plan lays out all mechanisms for cooperation between the stakeholders. Furthermore, a memorandum of understanding between SECP, stock exchanges, and ICM is in the process of being signed that clearly lays out roles and responsibilities of each party. All three stock exchanges have been allotted different geographical areas across Pakistan where they are responsible for conducting seminars, and assistance across all areas is provided by the remaining stakeholders. Capital market institutions assist SECP in undertaking the capital markets investor education program. The content for the program is discussed and shared with all stakeholders, but the approval of the content remains with SECP. In

	addition, the South Asian Federation of Exchanges also runs a financial literacy program in Pakistan. Industry associations such as the MUFAP, Institute of Chartered Accountants of Pakistan, Institute of Cost and Management Accountants, and the Institute of Chartered Financial Analysts all assist SECP in operating the capital markets investor education program. For example, the Karachi Stock Exchange has on its website an "investor center" where guidance is given to new and experienced investors on various aspects of investing and the types of instruments available on its markets. Similarly, the MUFAP website provides investor education by making available an informative and interactive website that disseminates information about mutual funds such as net asset values, risk level, historical performance, and performance with benchmarks.
Recommendations	While SECP is the lead agency for developing the national strategy for investor education for the securities and insurance sectors, there needs to be effective coordination of financial capability initiatives between SBP and SECP in order to ensure the effectiveness of these initiatives. In addition, it may be helpful to further strengthen the system of consumer advocacy organizations. A system of consumer nongovernmental organizations is needed to serve low-income as well as heavily indebted households. Consideration should be given to the role of nonprofit financial advisors (such as the credit counseling center in Malaysia), which can help indebted people sort out their debts and provide them with necessary counseling. These organizations should also be encouraged to keep records of the cases they receive, conduct trend analysis of these data, and propose changes in legislation where appropriate. SECP should consider consultation with consumer advocacy organizations on a regular basis in the preparatory work on legislation affecting consumers of financial services in the securities sector.
Good Practice G.2	***Using a Range of Initiatives and Channels, including the Mass Media*** **a. A range of initiatives should be undertaken to improve people's financial capability.** **b. This should include encouraging the mass media to provide financial education, information, and guidance.**
Description	The implementation of SECP's Nationwide Investor Education and Awareness Program should include the following: a. SECP Investors' Education Website: Develop a dedicated investor website initially in English and later in Urdu. b. Awareness Seminars: Conduct awareness seminars in collaboration with SROs, associations, media, and universities. c. Investor Protection Services: Ensure investor protection through implementation of SECP Public Disclosure Policy, linkage with the IOSCO Investor Alerts Portal, and launch of SECP Service Desk Facility. d. Educational Material: Create and distribute educational material on various market products and services; create material in different languages spoken across Pakistan.

	e. Media Campaign: Educate investors through the use of electronic and print media as well as social media, and advertise the seminars being conducted in order to reach its target audience. At this point, the mass media does not provide financial education to the public; however, individual companies and institutions do use the media as a tool to disseminate information such as the publication of the financial results of a listed company.
Recommendation	The authorities and market participants should consciously work with the mass media to provide financial education, information, and guidance to investors.
Good Practice G.3	***Unbiased Information for Investors*** **c. Financial regulators should provide, via the Internet and printed publications, independent information on the key features, benefits, and risks—and, where practicable, the costs—of the main types of financial products and services.** **d. Nongovernmental organizations should be encouraged to provide investor awareness programs to the public regarding financial products and services.**
Description	The dissemination of financial education by SECP is done through a variety of mediums including the mass as well as through written publications. In the years following the stock market crisis in 2008, SECP has been particularly aggressive and committed to promoting investors' awareness and education. SECP has been maintaining on its website a detailed investor guide that includes an overview of the capital market institutions of Pakistan, elementary information about financial securities, and their associated costs, benefits, and other details. The above investor guide contains information relating to roles and responsibilities of the investors. SECP has also published a variety of brochures relating to the protection of rights of consumers in the different sectors of the financial system. In the Investors' Awareness Brochure, the areas that are addressed relate to the following: • With whom to trade • Opening account with the broker and dealings with the broker • Receipt of trade information and right of investor to periodical statement of their securities accounts • Payment of margins • Lodging of complaints There are also frequently asked questions (FAQs) for lodging complaints with SECP. The FAQs address the types of complaints that an investor may lodge against a stock exchange member and the circumstances of filing complaints with SECP. The FAQs also explain the processes to be expected in the handling of the complaints and the arbitration mechanism instituted by the stock exchange. The stock exchanges and MUFAP also maintain on their websites information for investors. For example, the Karachi Stock Exchange maintains on its website an

	"investor center" that provides a guide to investors on areas such as "market and its workings," "risk management," and 'investment instruments," among other things. It also provides information to first-time investors and experienced investors. The MUFAP website provides investors in mutual funds basic information on tax implications and fees as well as how to develop an investment plan. It also provides NAV returns performance reports that compare the different funds provided by its members and the funds' payouts. During the mission, SECP also has shared with the mission team a detailed "Investor Education and Awareness Program," in which it stated that it would partner with key capital market stakeholders, such as the various stock exchanges, the NCCPL, MUFAP, and CDC to undertake investor education programs across the nation. Key elements of the program such as educational materials and seminars will all be branded under the Institute of Capital Markets, with SECP acting as the overall implementing agency of the program.
Recommendation	Consumer organizations should be strongly encouraged and supported by the government and SECP to deliver financial education awareness programs throughout Pakistan.
Good Practice G.4	***Measuring the Impact of Financial Capability Initiatives*** **a. The financial capability of consumers should be measured through a broad-based survey that is repeated from time to time.** **b. The effectiveness of key financial capability initiatives should be evaluated.**
Description	No survey is undertaken to measure the financial capability of consumers in Pakistan as they pertain to the capital markets, nor is there any assessment of the effectiveness of the many financial capability initiatives undertaken by SECP, MUFAP, and the Karachi Stock Exchange. Although the investor education program launched by SECP seems comprehensive, it would appear that it was primarily based on SECP and other relevant stakeholders' perceptions of the key issues in investor education. The preferred approach would be to gauge the issues firsthand by organizing focus groups or existing investor survey data.
Recommendation	A baseline survey assessment should be conducted to better identify the segments of the population that require particular attention, measuring the effectiveness of financial education and determining education needs for the securities sector.