Designing Disclosure Regimes for Responsible Financial Inclusion

In East Africa, a microborrower who goes to pay off his loan early is surprised by a hefty prepayment penalty that was not mentioned in his loan agreement. A small business owner in Southeast Asia becomes frustrated trying to determine which of several loans is the least expensive—one comes with a flat charge, another a weekly interest rate, and still another a monthly rate with an upfront deduction.

Situations like these can be quite common. Country-level policy makers working to expand financial inclusion are increasingly recognizing the need for complementary efforts in financial consumer protection. Recent initiatives at the global level include the G-20 High-Level Principles on Financial Consumer Protection and work within the Global Partnership for Financial Inclusion. If financial service delivery is transparent, services will be used more, customers will benefit more, and inclusion in the formal financial sector will pose fewer risks for vulnerable, low-income people who have less experience with formal finance and lower levels of financial literacy and capability. (Such consumers are referred to as “low-income consumers” in this Focus Note.)

Transparency is a basic element of consumer protection. To determine whether a product or service is appropriate for them, customers first need to know what they are getting. Pricing and other terms of financial products can often be opaque or even deceptive, particularly for low-income consumers. Advertisements can mislead them, and excessive fine print can flood them with information, distracting from the factors that are most important for their decisions.

“Disclosure regime” in this Focus Note refers to regulation and guidelines, supervision and enforcement efforts, and other policy initiatives meant to increase transparency. Disclosure regimes can increase transparency by targeting two key objectives: (1) increasing consumer comprehension, allowing consumers to understand and choose appropriate products, and (2) increasing market competition, allowing comparison shopping by consumers and greater competition among providers, which may help to lower prices and improve the quality of products offered. Though there is little available data on impact, preliminary evidence suggests a positive correlation between disclosure and favorable pricing trends, which may indicate improved consumer comprehension and increased market competition.

Designing an effective disclosure regime is complicated. Behavioral biases, such as the tendency of borrowers to focus more on the item being financed than on the terms of a loan, pose a challenge. In developed countries, disclosure regimes have had mixed results. The task is all the more difficult in developing countries where levels of financial access and financial literacy and capability are low and regulators face significant capacity constraints. (Such environments will be referred to as “low-access environments” in this Focus Note.) And even where such issues can be addressed, markets with limited product options and many unregulated informal providers reveal some of the fundamental limitations of disclosure regimes. Low-access environments are likely to call for approaches that differ from those used in developed countries. Despite increased attention...
to transparency issues in general,² there is little
guidance for these situations.

This Focus Note offers practical guidance to policy
makers who are developing disclosure regimes in
low-access environments (see Box 5 for a summary
of recommendations). It highlights three main
dimensions of disclosure:

- **Content of disclosure at the consumer level** — What information should be disclosed to the individual low-income consumer?
- **Methods of disclosure at the consumer level** — How should information be disclosed to the individual low-income consumer?
- **Disclosure to the public** — What information should be disclosed to the public (e.g., other providers, general consumers, the media, and other stakeholders), and how?

In addition to these three dimensions, the Focus
Note briefly explores broader implementation
issues, such as developing disclosure regimes
incrementally to strike a careful balance between
transparency and added costs for providers and to
work within the capacity constraints of regulators
and providers. The limitations of disclosure and its role as one piece of a larger puzzle in
achieving financial consumer protection through
complementary initiatives beyond regulation are
also addressed.

The Focus Note draws on disclosure regimes
primarily focused on providers serving low-income
consumers in eight countries and regions: Armenia,
Bosnia–Herzegovina, Cambodia, Ghana, Pakistan,
the Philippines, Peru, and the West African
Economic and Monetary Union (WAEMU).⁶⁷ These
examples were selected to reflect differing regions,
levels of regulatory capacity, and stages of financial
sector development and evolution of disclosure
regimes. All eight have robust credit markets
targeting low-income consumers, and a majority
are low-access environments.

The Focus Note also draws on the relatively
limited existing research and analysis on the topic
generally, as well as on specific examples, where
relevant, from disclosure regimes in developed
and emerging market countries. In addition, initial
results from consumer testing on disclosure issues
by CGAP and partners are incorporated where they
provide insights of specific relevance to low-income
consumers. The focus is on credit products, though
many of the basic transparency principles discussed
apply to other types of financial products as well.

**Main Dimensions of Disclosure Regimes**

**Content of Disclosure at the Consumer Level**

The disclosure of sufficient information regarding
pricing and other terms is necessary to enable
consumers to assess a product’s affordability and
risks and to make informed choices regarding
which product suits their needs. The objective at
this level is consumer comprehension, and the
focus is on the individual consumer engaged in a
potential transaction. This section examines what
information is required to be disclosed by different
disclosure regimes regarding pricing (e.g., interest
rates, fees, cash collateral, or mandatory savings),
other key terms beyond pricing, and consumer
rights and recourse mechanisms.

**Pricing**

Clear information on pricing is fundamental for
transparency. This section (1) describes the three

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² According to CGAP and the World Bank (2010), the percentage of surveyed countries with disclosure requirements on opening an account
was 81 percent for banks, 73 percent for other regulated financial institutions, and only 24 percent for unregulated institutions. Requiring
some type of disclosure is the most common form of consumer protection regulation, though the content and scope of the requirements vary
widely.

⁶ WAEMU is an organization of eight West African states: Benin, Burkina Faso, Côte d’Ivoire, Guinea-Bissau, Mali, Niger, Senegal, and Togo.
Financial sector regulation and supervision is shared among the Central Bank of West African States (BCEAO) and the respective Ministry of
Finance for each member country.

⁷ Information on disclosure regimes has been drawn from publicly available laws, regulations, research, and communications with regulators.
In some countries, disclosure rules examined are specific to microfinance institutions; in other countries, disclosure rules apply across
multiple provider types. A table comparing the key components of the disclosure regimes in the eight countries and regions can be found in
Annex A. The analysis may not fully reflect the reality of how disclosure regimes are implemented in practice.
main methods of disclosing pricing and the items that should be included in pricing disclosure to ensure that consumers have adequate information, and (2) discusses the pros and cons of different methods of pricing disclosure.

All disclosure regimes examined were found at a minimum to require disclosure of an interest rate for credit products. However, disclosure of nominal interest rate alone is not sufficient, since it does not adequately represent true cost and does not equip consumers with the information necessary to accurately assess product affordability and suitability or to comparison shop. More comprehensive disclosure regimes therefore go beyond nominal interest rates by requiring use of one or more of the following methods of disclosing pricing: (1) total cost of credit, (2) repayment schedules, and (3) annual percentage rate (APR) or effective interest rate (EIR).

Total cost of credit is the total cumulative amount a borrower must pay for a loan product. This presentation should ideally combine all interest, fees, and charges over the duration of the loan. In particular, up-front fees and deductions for items such as credit life insurance and mandatory savings/cash collateral should be included in total cost of credit (as well as in APR or EIR) where such items are mandatory and bundled along with a credit product. These items present an additional cost of which consumers may be unaware unless they are included in total cost metrics. The disclosure regimes in the Philippines, Peru, and Ghana require the presentation of the total amount that a credit product will cost.

The conversion of total cost, including interest rates and fees, into a comprehensive standardized annual rate, APR or EIR is the generally accepted standard in developed countries to allow for more accurate comparison of pricing across providers and product options. A majority of disclosure regimes examined require APR or EIR.

Repayment schedules present the schedule of installment amounts to repay a loan. They are fundamental to disclosing pricing and serve a complementary role to both total cost of credit and APR or EIR by helping consumers assess affordability in addition to total price. The disclosure regimes in Peru, Armenia, Ghana, Bosnia–Herzegovina, and Cambodia require that the borrower receive repayment schedules. Disclosure regimes generally require that repayment schedules include the number, date, and amount of installment payments at a minimum. Additional elements to include in repayment schedules (such as fees and interest rates) can be tailored to country context, including the types of products in the market and the literacy of consumers using them.

Which method or combination of methods is most effective in conveying the true cost of a loan to low-income consumers is open to debate. While APR and EIR allow for greater comparability, total cost of credit and repayment schedules may be easier for low-income consumers to comprehend, as price is expressed in concrete terms that present the total cumulative cost and the regular cycle of payments required for a credit product. Though data are limited, recent studies as well as consumer testing by CGAP in Mexico and the Philippines suggest that low-income consumers tend to focus on installment payment amounts, rather than on interest rates, as their main concern is whether their cash flow will cover weekly or monthly loan payments. Research has also shown

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8 The methods of standardizing and presenting product pricing, and key issues arising from each method, are explored in greater detail in Annex B.

9 Note that EIR differs from APR (i.e., nominal APR) in that it takes into account compounding interest when converting nominal rates into an annualized rate. APR is mainly used in the United States, while EIR is used in other countries.

10 In the Philippines, Circular No. 730, issued by Bangko Sentral ng Pilipinas in July 2011, includes a sample disclosure form containing a repayment schedule, though the circular itself does not indicate whether a repayment schedule (or use of the sample disclosure form) is mandatory.

11 Further research is warranted on how to make repayment schedules a more useful tool for consumers to assess affordability, including analysis on what information consumers respond to in a repayment schedule format. Duplicating all fees and charges found in total cost of credit and APR or EIR in a repayment schedule runs the risk of information overload and detracts from the usefulness of presenting pricing in a repayment schedule format.

12 For background on this issue, see FSD-Kenya (2009), Hastings and Tejeda (2008), Bertrand and Morse (2009), and MFTransparency (www.mftransparency.org).

that disclosure of total cost of credit has a greater impact on consumer behavior than disclosure of APR or EIR, making consumers less likely to borrow or more likely to choose products with lower fees.\(^\text{14}\)

Loans used most frequently by low-income consumers are relatively small, and their terms are often less than one year. Compounding the nominal rates of such loans into APR or EIR produces rates that appear considerably higher than the rates of larger loans in the market, by annualizing loans that have terms of less than a year and including origination and servicing fees that reflect the actual costs associated with any loan, no matter its size. Although it is not surprising that smaller and shorter term loans must be priced to cover higher lending costs, this standardized comparison risks creating an unfair apples-to-oranges situation. It can also open providers of such loans to public criticism and reputational risk, which may pose a disincentive from serving the low-end sector of the market and have negative consequences for financial inclusion.

To address the drawbacks of APR and EIR, policy makers can provide clear, standardized guidelines on APR and EIR calculation to facilitate compliance by providers (see Box 1 for further discussion on the necessity of clear, specific disclosure rules) and allow a reasonable time period to come into compliance, given that there may be a learning curve for providers to become proficient in accurate calculation of APR and EIR. Policy makers in Peru and Ghana centralize the calculation of APR or EIR with regulators specifically to address the capacity constraints of smaller, less formal institutions. Allowing for the monthly presentation of APR or EIR is another practical option recently introduced in the Philippines.\(^\text{15}\) Monthly APR or EIR may be more appropriate for loans of less than a year and more comprehensible to consumers. APR or EIR can also be introduced at a later stage as it is arguably of greater importance for transparent pricing to the broader market and the objective of increased market competition (further discussed below), as opposed to the immediate objective of consumer comprehension by low-income consumers.

**Other Key Terms**

The disclosure of other key terms beyond pricing is necessary for transparency. Which specific terms should be disclosed will vary depending on product type and country context. However, the guiding principle for disclosure should be to inform consumers of the responsibilities and potential risks, particularly those triggered by a future event, that come with a product so that consumers are fully aware of what they are undertaking and can assess which products are most appropriate for their financial circumstances and risk tolerances.

For credit products, examples of key terms include prepayment penalty fees and variable interest rates. The features of both the credit product itself and bundled services, such as credit life insurance and mandatory savings, should be disclosed, as should the rights and responsibilities of the provider and the consumer. In addition, the conditions for acceleration or default and the terms that apply in each case, such as default interest rates, should be disclosed.\(^\text{16}\)

Disclosure of these types of terms is generally required in more comprehensive disclosure regimes. Default rates and penalties for breach of contract must be disclosed in Peru, Armenia, and Ghana. In Ghana, the method used for assessing penalties also must be disclosed. When interest rates are variable, providers in Peru are required to disclose the criteria for modification of rates. For loans provided in foreign currency, Armenian regulation requires providers to disclose to consumers that changes in the exchange rate might affect repayments.

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\(^{14}\) See Hastings and Tejeda (2008) and Bertrand and Morse (2009). Results from focus groups in Kenya also indicate that low-income consumers understand total cost of credit, especially when paired with repayment schedules, far more than APR or EIR. See FSD-Kenya (2009).

\(^{15}\) Circular No. 730 of July 2011 allows for EIR to be expressed as a monthly rate for loans with monthly interest rates. The circular currently applies only to banks, whether a similar circular is forthcoming for nonbank financial institutions is unclear.

\(^{16}\) Directly regulating product features such as penalty fees, as opposed to requiring disclosure, can be another approach to protecting consumers. See discussion in Box 3.
Box 1. How Specific Should Disclosure Regulations Be?

One of the most noticeable variances among disclosure regimes examined in this Focus Note is the level of specificity with which disclosure rules are drafted. In some countries, a few general principles or simple rules on disclosure are provided. For example, the disclosure regime in Cambodia requires that all microfinance institution loan agreements include an amortization table, but does not provide for specific content or a standardized format. The State Bank of Pakistan requires microfinance banks to make “adequate efforts to educate their clients on important terms and conditions of all their products including loans and savings.” It is not clear how such a standard would be implemented in practice if it is left to the discretion of providers.

By contrast, other disclosure regimes provide detailed disclosure rules and standardized formats. The Law on Consumer Credit in Armenia defines APR, provides a formula for calculation, and details what charges are not included in APR. The disclosure regime in the Philippines provides a methodology for calculating EIR explicitly for the purpose of standardizing the measure and defines the types of fees to be included in the disclosed finance charge. The disclosure regime in Peru specifies what information repayment schedules must contain, while the disclosure regime in Bosnia–Herzegovina provides a template for repayment schedules. And in Ghana, a standardized preagreement statement which includes APR and various other key terms is provided by regulation.

Disclosure regimes should provide clear rules for providers to allow for consistent application of disclosure rules across providers. Particular attention should be paid toward drafting precise requirements for those items for which nonstandardized disclosure defeats the purpose of disclosure. For example, without a standard definition or formula for calculating total cost of credit or APR or EIR, providers left to their own discretion will likely differ in the fees and charges included in their calculations (including such distortive costs as credit life insurance premiums and cash collateral), resulting in amounts that purport to but do not capture the true cost of a credit product and cannot be used for effective comparison shopping. Specifying the minimum content or format of repayment schedules would help create more consistent experiences for consumers and aid in consumer comprehension. Clear rules should also ease provider compliance and the ability of regulators to enforce compliance.

However, specificity in disclosure requirements does not mean that highly detailed information should be disclosed. More information is not necessarily better. There are diminishing returns to consumer comprehension if excessive information is presented that overwhelms consumers and makes it difficult to sort important from trivial information. Complex regulatory requirements may make compliance more challenging for providers. Striking the right balance is critical so that disclosure regulations are clear, sufficiently detailed and easily administered.

Consumer Rights and Recourse

Consumer rights, such as the right to make inquiries or complaints via provider or third-party recourse mechanisms, are important as a general matter of consumer protection. Information about the availability of recourse and rights regarding recourse is an essential—but sometimes overlooked—component of disclosure regimes. Of the eight jurisdictions surveyed for this Focus Note, only two require disclosure of consumer recourse across a range of financial products and institutional types. The disclosure regime in Peru requires businesses to make public in their establishment a clear statement on the procedures for handling questions or complaints. The disclosure regime in Armenia goes further by requiring providers to both orally advise consumers about complaint procedures before entering into a contract and include information on dispute resolution in the contract.

Accessible and responsive consumer recourse can itself help to make a disclosure regime more effective. Consumer recourse mechanisms such as specialized help desks within financial institutions not only handle complaints, they often handle questions and can play a role in facilitating consumer comprehension of disclosed information. In addition, regulators should and often do require financial institutions to periodically report on

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17 This is partially a reflection of the fact that there may be no law or regulation yet requiring consumer recourse mechanisms in general. In jurisdictions such as the Philippines, there are recourse requirements only for e-money transactions and, thus, corresponding requirements for disclosure of these mechanisms to e-money consumers. Bangko Sentral ng Pilipinas, Manual of Regulations for Non-Bank Financial Institutions, S Reg. § 46425.4(f) and (g); Bangko Sentral ng Pilipinas, Manual of Regulations for Banks, § X780.4(f) and (g).

18 For further discussion, see Thomas and Frizon (2011), p. 9.
consumer inquiries and complaints, and can then use such reports to assess the effectiveness of disclosure requirements and identify areas for improvement.

**Methods of Disclosure at the Consumer Level**

How information is disclosed and at which stage in the transaction is as important as what is disclosed. Unless presented clearly and simply, disclosure of the various cost components and other terms of a financial product can be overwhelming and counterproductive to the objective of consumer comprehension. For example, during recent consumer testing in Mexico, regulators were surprised at how little low-income consumers actually understood of what was disclosed. Not specifying the format of disclosure will likely result in disclosures that vary in quality and do not highlight key information identified by regulators as necessary for informed decision-making.

This section examines ways in which disclosure regimes can address the issue of effective communication of disclosed information to a consumer engaged in a potential transaction, including via standardized disclosure forms, plain language and clarity requirements, and rules regarding timing of disclosure.

**Summary Sheets/Disclosure Statements**

Disclosure will be ineffective if important information is buried in loan agreements. A single page summarizing key information (such as the items highlighted in the previous section) is one of the most useful tools for enabling consumer comprehension. In Peru, a summary sheet with key items of information must be annexed to credit contracts. In the Philippines, banks are required to provide borrowers with a disclosure statement.

Disclosure regimes can go beyond specifying the minimum content of summary sheets by providing a standardized summary sheet for use by providers. Standardized forms facilitate consumer comprehension and comparison shopping, which can be further enhanced by incorporating such forms into consumer awareness and financial capability programs to familiarize consumers with the format. Standardized forms also ease compliance by providers, particularly smaller, less sophisticated providers who will save time and resources by not having to develop their own disclosure forms to meet regulatory requirements.

Monitoring use of standardized forms is also a simpler task for regulators than reviewing forms that may be different for each provider. The disclosure regime in Ghana requires lenders to provide a standardized preagreement statement to consumers. The preagreement statement provided by regulation discloses APR, finance charges, filing fees, and late charges (with short plain-language explanations of each term) and includes prominent checkboxes for other key terms, such as credit insurance, variable interest, and prepayment penalties.

Consumer focus group testing can be a useful tool to ensure that the content and format of standardized summary sheets and disclosure statements are effective for low-income consumers (see Box 2). In the Philippines, consumer testing was recently used to create a standardized form of disclosure statement. Among other findings, the testing revealed that presenting a single interest rate such as APR or EIR rather than multiple interest rates is better in order to avoid information overload and confusion (nominal monthly rates can be provided in the details of the contract itself) and that consumers prefer to have recourse mechanisms displayed prominently on the disclosure statement. Periodic consumer testing and review processes along with open consultation with financial providers and industry associations can be used to keep such forms relevant and up-to-date.

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19 See, for example, Peru and Armenia.
21 Includes EIR, a repayment schedule, total amount of interest payments, fees and commissions, prepayment rights, etc. See Regulation of Transparent Information and Negociation with Financial Consumers, 2005 (as modified through July 2011), Superintendency of Banking and Insurance.
23 CGAP supported Bangko Sentral ng Pilipinas to conduct 12 focus groups in March 2011 to test various disclosure statement formats and assess how well low-income consumers comprehended key terms and cost. See Collins, Jentzsch, and Mazer (2011).
Language and Clarity
Disclosure rules requiring providers to use clear language and present information in a format that is easily visible can help to ensure that disclosed information is comprehensible, particularly for low-income consumers. Several of the disclosure regimes reviewed included qualitative descriptors that require disclosed information be “clear,” “not hidden,” and “simple.” For example, form contracts in Peru made available to the public must be sufficiently legible, be printed in a font larger than 3 millimeters, and use comprehensible phrasing and terms.

Where literacy rates are low, it is particularly important that information be orally communicated to consumers in addition to being conveyed in writing. Creditors in Armenia are required to orally advise customers regarding information such as the material terms of the service to be provided, associated costs and risks, customers’ rights and obligations, and mediation. In Pakistan, the regulatory requirement to orally communicate to clients the terms of contracts is less precise, though with the same intent. Again, greater specificity in requirements for oral communication would help to better guide providers and prevent them from complying with general requirements in a manner that evades regulatory intent.

Timing
The timing of disclosure is critical for informed decision-making by consumers. Consumers tend to focus on the present and discount the future. In addition, consumers are often preoccupied with the product they are financing with credit, and pay less attention to the actual terms of credit. Therefore, sufficient time and distance from a credit provider and a potential transaction is necessary for consumers to fully consider disclosed information and assess affordability and risks.

As a basic step, disclosure regimes can require that information be disclosed before the consummation of a transaction. In Peru, information relating to EIR, commissions, fees and conditions, as well as a copy of the summary sheet, must be delivered to a customer before signing. A better approach may be to specify information disclosure earlier in the product selection cycle.24 The disclosure regime

Box 2. Consumer Testing and Behavioral Research
The perspective of the individual consumer is not always fully considered when disclosure regimes are developed, yet it is critical. Consumer testing through group discussions, individual interviews, and testing of draft summary sheets and disclosure statements are essential tools for better understanding consumers’ comprehension levels, biases, and decision-making processes and for providing real-world data so that disclosure rules can be tailored accordingly.

In focus groups conducted by CGAP in Mexico and South Africa, consumers were asked to explain what they did and did not understand in a sample summary sheet and then narrate their financial decision-making process. Their responses to different terms shed light on which methods most effectively convey information and what elements consumers deemed most essential in assessing a financial product. The placement of information also affected what was more likely to be noticed by consumers.a

Behavioral studies regarding financial decision-making have revealed common biases in consumer thinking that further impact disclosure efforts.b Consumers tend to underestimate the costs of financial products and overestimate their capacity to repay. Consumers also tend toward hyperbolic discounting, giving more weight to present benefits and less to future costs. Such biases can cause consumers to borrow at higher costs than they fully realize, while anticipating unrealistic future revenues, a pattern that may lead to over-indebtedness. There is a small but increasing amount of research in developed countries on counteracting these biases, which may provide lessons that are transferable to policy makers developing disclosure regimes in other contexts.c

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24 The issue of timing arises at both the individual consumer level as well as with respect to disclosure to the public (i.e., advertising and branch displays). Disclosure to the public may have an even greater positive impact than information conveyed on a transactional level to an individual consumer, particularly in terms of facilitating comparison shopping.

a For more information, see Collins, Jentzsch, and Mazer (2011).
b E.g., Laibson (1997) and Stango and Zinman (2011).
c E.g., Barr, Mullainathan, and Shafir (2008), Belsky and Essene (2008), and Campbell, Jackson, Madrian, and Tufano (2011).
in Bosnia–Herzegovina requires that microcredit organizations and, in part of the country, banks inform clients of EIR both before a client receives a loan application and before concluding a loan agreement. The disclosure regime in Armenia requires that customers be provided with sufficient time to become familiar with the provisions of the contract.

Additional Steps to Ensure Consumer Comprehension
A number of additional steps can help to improve consumer comprehension. The disclosure regimes in the Philippines and Peru include the simple and useful requirement that providers obtain written acknowledgment from consumers (via signed summary sheets or disclosure statements) that they have received disclosed information. This requirement facilitates supervision and enforcement as well since examiners can later check for these documents.

Disclosure requirements can also include the expectation that providers educate or inform clients. Financial institutions in Peru are obligated to resolve all questions that customers may have relating to the content of their contract before signing. In addition, financial institutions in Peru must have personnel specialized in customer service and designated to consult with clients on the scope of standardized form contracts. Such an approach partially shifts the burden of achieving comprehension onto the provider, but should not be viewed as a substitute for clear instructions on what and how information is disclosed.

Disclosure to the Public
The issues explored regarding the content and methods of disclosure at the consumer level focused on disclosure to an individual consumer engaged in a potential transaction, with the primary objective to increase consumer comprehension and allow the individual consumer to choose an appropriate product. Disclosure regimes can also work toward disclosure to the public at large. Though consumer comprehension is still relevant, the main objective here is increased market competition.

In theory, this can be achieved from the demand side by providing consumers in the general market with sufficient information to comparison shop and “vote with their feet” (i.e., choose better products and providers). However, in practice, low-income consumers are likely constrained by search costs and information and power asymmetries, among other barriers. Relying solely on the impact of improved consumer decision-making to reap the benefits of transparency, even where disclosure regimes provide a full basis for comparison shopping, will likely be a slow process.

To increase market competition at a faster pace, disclosure regimes should be crafted to harness other forces in addition to comparison shopping by consumers, including competition among providers, moral suasion by regulators (see Box 4), and pressure by media. Donors and investors can also use their leverage and support to motivate MFIs to increase the transparency of their products. Increasing competition on the supply side among providers themselves will be necessary to have any real impact on market competition. Information on pricing and terms that is accessible by the public

Box 3. Regulation of Product Features
Strictly regulating product features is a more blunt approach to addressing consumer protection goals similar to those of disclosure regimes. In South Africa, the only permissible fees for credit products aside from interest are initiation fees, monthly all-inclusive service fees, and debt collection charges; penalty interest and other fees are explicitly prohibited. A simpler example comes from Cambodia, where flat interest is banned. Strategic, targeted regulation of product features may be appropriate in cases where certain features are clearly detrimental to consumers or frequently abused, such as flat interest rates or punitive prepayment or post-delinquency penalties. However, product regulation can have many potential downsides and unintended consequences and warrants a much fuller discussion than the scope of this publication allows.

\[a\] See National Credit Act, Act No. 34 of 2005, South Africa.
(and not just by an individual consumer engaging in a potential transaction) can provide the basis for moral suasion by regulators and pressure by the media, who are in a better position than low-income consumers to track such data, identify undesirable practices, and influence provider behavior.

For example, the Peruvian Association of Consumers and Users receives and forwards consumer complaints to the Superintendency of Banking and Insurance, and the media in Peru publicize which providers have the least favorable rates. International initiatives such as the SMART Campaign have drawn together microfinance industry leaders to develop the Client Protection Principles for MFIs (which include transparency as a principle), while MFTransparency is working with the microfinance industry in 26 countries to make prices transparent and comparable at a market level using APR and EIR.

Given these multiple forces at work, policy makers drafting disclosure rules should keep in mind what parties disclosed information is intended to reach and the desired effect of such information. For example, to disclose information as broadly as possible to competing providers, media, and investors, focusing on key terms that are immediately comparable, such as APR and EIR, may be warranted. Unlike with low-income consumers, this audience will be able to fully benefit from and use APR and EIR data. Conversely, to reach and inform low-income consumers, newspapers may be a more conducive medium for disclosing information than Web sites.

This section examines several methods for disclosing information to the public, including branch displays, brochures, and advertising on Web sites and in other media, and explores the factors that should be considered regarding content and format.

**Branch Displays**

Displays and other materials in physical branches should offer information that accurately conveys pricing and other key terms clearly and prominently. Disclosure regimes relying on general principles and simpler rules, such as that in Pakistan, require the display of “important terms and conditions of products on [the] entrance/or window of branches” for microfinance banks or focus on a particular item, such as EIR, that must be clearly and prominently displayed in microcredit organizations and bank premises in Bosnia–Herzegovina.

Regulators seeking more comprehensive disclosure to consumers can expand on the basic approach by specifying in greater detail which key terms must be disclosed, requiring that disclosures be legible and displays be visible and ensuring that consumers are aware such information is available. Consumer recourse information should be displayed as well. In the Philippines, banks are required to post all information that would be contained in disclosure statements in a conspicuous place in their branches. They must also post an explicit notification that customers have a right to demand a copy of the disclosure statement. In Armenia, banks and credit organizations must make information bulletins available in branches that disclose information such as maximum and minimum amounts of credit, term of credit, nominal interest rate and APR, frequency of repayments, and penalties.

The disclosure regime in Peru includes particularly detailed requirements for disclosure to the public. Financial institutions are required to disseminate, among other items, EIR, commissions and fees, details regarding insurance coverage, and methods for calculating penalty interest rates or fees. A schedule containing interest rates, commissions, and fees must be visibly posted in an institution’s place of business and printed in legible characters when exhibited in windows. If a schedule is not displayed in a window, providers must post a notice in the window informing customers about the availability of the schedule by other means. Form contracts must be available in places of business, allowing consumers to review a contract before entering into a

26 See www.smartcampaign.org.
28 See Central Bank Regulation 8/03 on Disclosure of Information of 2009 for further information on the required content of information bulletins.
Such publicly displayed information facilitates both comprehension and comparison shopping by consumers, and may also provide the further benefit of increasing competition among providers.

Advertising and Marketing Materials
Advertising and marketing materials are likely to be used by consumers in earlier stages of comparison shopping and are critical to consumers’ initial impressions and decision-making process. Although disclosures at this stage can be less detailed, they should be current and easily comparable across institutions. In Peru, information on a financial institution’s Web site must be continuously updated and identical to information available in its place of business, and the fee schedule must be “easily accessible” on the Web site. If informational brochures are used, they must include updated information on rates and fees, or alternatively convey only nonquantitative information and refer customers to fee schedules available in the place of business or on the Web.

Advertising and marketing materials are also useful to foster competition among providers. Emphasizing the prominent disclosure of APR or EIR may provide greater benefits at the market level than at the consumer level by facilitating comparison by regulators, media, and investors. The disclosure regime in Armenia requires that any advertisement or public offer referring to interest rate or cost of credit include APR. In Peru, informational brochures must include not only EIR, but also explanatory examples of how a particular EIR would apply to a sample transaction.

Disclosing information via multiple channels may also help to reach a wider number of consumers, competing providers and other stakeholders in the market. Policy makers should consider how low-income consumers are most likely to receive information (not online), and tailor regulations accordingly. In WAEMU, banks and MFIs are required to disseminate the terms of their credit products by all forms of communication “as widely as possible” at the start of each year and must publish their minimum and maximum rates in at least one daily newspaper semi-annually and immediately after any modification. Again, the disclosure regime in Peru goes the furthest by obligating financial institutions to “constantly disseminate the interest rates, commissions, and

Box 4. Regulator Facilitation of Market Transparency
Financial regulators can play a strategic role in actively spurring the dissemination of comparative pricing information to the public. The Bank of Ghana publishes monthly tables online that compare key pricing terms of banks’ credit products, and a similar table covering both banks and MFIs is being planned in Senegal. In Peru, the law calls on regulators to supervise dissemination of pricing information so that customers can compare rates. The Superintendency of Banking and Insurance directly publicizes information on its Web site regarding financial institutions’ current interest rates, commissions, and fees in a format that allows easy comparison of standard characteristics of similar products and services offered by different institutions. To allow regulators to monitor market trends in product offerings, it may be necessary to first require that providers report additional information on pricing and other key terms. For example, the disclosure regime in Bosnia–Herzegovina requires that MFIs report EIR to the regulator on a monthly basis.

Publishing such information provides regulators with the opportunity to use moral suasion to influence provider behavior and facilitate market competition. In one instance, the Superintendency of Banking and Insurance prepared a table comparing EIR to be paid on deposits, which revealed one bank would be paying a negative EIR. Before publication, the regulator called the bank to inform them what the publication would show—and very quickly, the bank changed its pricing terms for that product.

Though online pricing information is useful for the goal of increased market competition driven by providers, investors, and media, such information is unlikely to reach retail, and particularly low-income, consumers. Static comparative tables published in print newspapers and other offline channels may reach a broader percentage of the public where readership levels are sufficiently high. Any approach should be tailored to country context and be realistic about the purpose of such dissemination.

29 See Regulation of Transparent Information and Negotiation with Financial Consumers, 2005 (as modified through July 2011).
fees... [D]issemination should guarantee customers’ access to such information.” 30 Information must be disclosed to the market through multiple channels (including via the Web, television, radio, or newspaper), thus ensuring information is broadly conveyed and up to date.

Implementation Considerations

Drafting a regulatory framework represents only one aspect of a disclosure regime. How best to stage implementation of disclosure regimes in the face of market and capacity constraints is an immediate concern. Further issues down the road include how disclosure regimes work as one piece of the puzzle in achieving transparency and how to expand coverage across the market. This section will briefly highlight a few important issues for policy makers in low-income environments to consider.

Taking an Incremental Approach

Ideally, a disclosure regime would cover all three dimensions of disclosure discussed above: disclosure of pricing, key terms, and rights and recourse, in a format that can be understood by low-income consumers, and disclosure of key information to the public to increase market competition. However, it is often not feasible or practical to address all issues at once. An incremental approach to developing a disclosure regime may be necessary, taking into consideration compliance costs and working with industry as well as regulatory capacity and supervisory strategies.

At a basic level, policy makers can begin by assessing what transparency issues are critical in a particular country context (such as a certain problematic type of product, provider, or contract term). After addressing these priority issues, broader disclosure rules can be added incrementally. Simpler, less intensive approaches in capacity-constrained countries can target discrete issues, such as in Cambodia, which focused on banning flat interest and requiring amortization tables.

An intermediate approach would be to develop a disclosure regime that works toward the baseline objective of increasing consumer comprehension. Policy makers can initially require the disclosure of total cost of credit and repayment schedules given their relevance to low-income consumers and provide clear, standardized rules on how such information is calculated by providers and communicated to consumers.

Working with industry and compliance costs should be considered by policy makers when developing and implementing such rules. Compliance costs are frequently raised, particularly by providers, as an obstacle to disclosure regimes. Given the higher costs of providing products to low-income consumers, there is a risk that compliance costs may discourage responsible providers serving this market. 31

The main components of compliance costs for providers include changes to management and information systems, changes to written materials such as contracts and advertising, and training of staff. These can generally be viewed as one-time expenses; recurring costs may therefore be much lower. 32 Policy makers can take steps to lessen the burden of up-front compliance costs by developing standardized disclosure documentation and taking into account the operational realities of different types of providers, such as the degree of automation or capacity to calculate APR or EIR. Striking the right balance between costs and benefits should be the objective—what is required to be disclosed should be highly beneficial to low-income consumers so that such disclosure requirements do not represent unnecessary compliance costs.

30 Article 8, Complementary Law No. 28587 to the Consumer Protection Law Concerning the Topic of Financial Services of 2005 (as incorporated in the Consumer Protection and Defense Code).
31 Though data on the impact of compliance costs are limited, there is some positive evidence from developed and emerging market countries. Reforms in South Africa following implementation of the National Credit Act of 2005 and recent reforms in credit card disclosure in the United States show that well-crafted disclosure rules need not necessarily result in decreased access or higher rates due to compliance costs. See FEASIBILITY (Pty) Ltd. (2009) and Frank (2011).
32 For example, unpublished reports by Deloitte commissioned by the Micro Finance Regulatory Council in South Africa estimated that recurring costs of compliance for the National Credit Act would decrease by an average of 89 percent from up-front compliance costs.
At a later stage, disclosure regimes could be expanded to include the disclosure of APR or EIR. In terms of pricing, the ultimate goal would be the prominent disclosure of pricing using total cost of credit, APR or EIR, and repayment schedules, as all three methods of pricing disclosure work in a complementary fashion to achieve transparency. Strategies can be used to improve the effectiveness of this standard, such as allowing for monthly APR or EIR. Again, working with industry and considering compliance costs will be important.

The success of the disclosure regime in Peru can be partly attributed to the Superintendency of Banking and Insurance’s extensive efforts to work with stakeholders during the development of disclosure rules. Regulators spent two years discussing disclosure rules with the industry, addressing issues with compliance costs and working with providers to build familiarity with formulas for calculating EIR. In addition, a large campaign was launched coinciding with the new disclosure regime to educate consumers on EIR and help ensure that they understand the new disclosure rules. Allowing sufficient implementation time frames and extensively disseminating new disclosure requirements to industry can also help to decrease compliance costs, and consumer testing can be used to further refine disclosure rules at each stage and build a stronger disclosure regime over time.

Once efforts to improve consumer comprehension are underway, regulators can also move toward the objective of reinforcing market competition by requiring broad dissemination of comparable metrics for total cost (such as APR and EIR) and other key terms through advertising and media channels, allowing market forces in addition to consumers to apply pressure on providers.

Across all stages of development, the strategy for supervising and enforcing disclosure regimes needs to evolve over time and best use available regulatory resources. The Superintendency of Banking and Insurance has a department specializing in consumer protection, and regulators in Peru can receive and resolve consumer protection complaints. As regulators in other low-access environments may not have similar resources at their disposal, using monitoring structures already in place or other market monitoring tools may be more efficient. Onsite prudential supervisory teams can be trained to examine compliance with disclosure rules. Requiring that providers report the nature of complaints and the outcomes of resolution procedures may help alert regulators to particular disclosure gaps in the market that require attention. And a main strategy for stretching limited regulatory resources will be to optimize the other “pieces of the puzzle” described below.

Disclosure as One Piece of the Puzzle

There are fundamental limitations to disclosure regimes, particularly in low-access environments. Low levels of financial literacy, regulatory and supervisory capacity constraints, markets with few providers and limited options, unregulated informal providers, and over-reliance by low-income consumers on advice from loan officers all pose significant obstacles. Transparency cannot be achieved by regulation or regulatory bodies alone. Complementary initiatives can help address some of these limitations.

Industry associations and individual financial providers can play a role in transparency. For example, individual MFIs in Cambodia have created their own codes of conduct that include guidelines on truth-in-advertising and transparency in transactions and business conduct. However, industry self-regulation often can be problematic for issues such as transparency, where financial institutions may have strong incentives to engage in deceptive behavior.
behavior and may not comply with industry or self-imposed codes. Furthermore, membership of industry associations rarely comprises all providers of a product in question, which limits the scope of protection and can even place compliant providers at a competitive disadvantage. Interestingly, the pending microfinance bill in India gives the Reserve Bank of India powers to issue directives to MFIs to observe industry codes of conduct. This approach could be a practical means of combining industry codes with broader government authority to enforce compliance with such codes.

Financial literacy and education can also complement disclosure regimes by providing consumers with the ability to analyze the information disclosed to them and better assess the benefits and risks posed by different product features. In recent years, policy makers in many developing and emerging markets have been increasing their efforts to improve the financial capability of low-income consumers by championing initiatives such as awareness campaigns, education and training targeted to specific client segments and students, and even alternative approaches, such as “entertainment education” and social marketing, that employ popular media to raise awareness and support changes in financial behavior.

**Expanding Coverage across Providers and Products**

A fundamental issue of disclosure regimes is coverage—to which financial products, providers, and customers do disclosure rules apply. Consistent coverage across all formal and semi-formal providers of similar products is important to provide comprehensive protection for all consumers, create a more level playing field for providers, and mitigate the risk of regulatory arbitrage. Several different approaches to expand the scope and coverage of disclosure regimes are discussed below.

Some disclosure regimes have limited or differentiated coverage by provider type. In Pakistan, for instance, there is no country-wide disclosure regime that applies across financial providers. Rather, the State Bank of Pakistan has issued separate sets of prudential regulations for microfinance banks and for consumer financing by banks and development financial institutions, both of which contain a limited number of provisions related to disclosure. Another approach is to cover credit agreements of a certain size. The disclosure regime in Armenia applies to consumer credit agreements for amounts between 100,000 and 10 million Armenian drams (US$269–26,885), while the disclosure regime in Ghana applies to all credit agreements for an amount of €100 Ghana cedis (US$66.7) or more. Regulator, provider, and consumer capacity can be taken into consideration if using the approach of setting a value threshold.

By comparison, the disclosure regimes in the Philippines and Peru aim for broader, more consistent applicability. In the Philippines, the Truth in Lending Act applies (in theory) to all credit granting institutions; specific disclosure regulations...
are structured by product and provider type. Similarly, the disclosure regime in Peru applies certain disclosure requirements to all consumer credit contracts across provider type (including lesser requirements for providers not regulated by the Superintendency of Banking and Insurance), while other disclosure requirements apply by type of financial service (e.g., credit, deposit, and credit card services) for regulated institutions. The initial focus was on general disclosure requirements for a few key types of financial providers and products, with a gradual expansion to apply more specific requirements comprehensively across additional providers and products. Such an incremental approach may be advisable to expanding coverage of disclosure regimes.

However, even where provided for by law, broad application and enforcement can be difficult to achieve in practice. Challenges include consistent application of rules and coordination among multiple regulators where supervisory authority is divided. In the Philippines, disclosure regulations applying to all types of banks as well as nonbank financial institutions (NBFIs) performing quasi-banking functions, while substantially similar, contain variations that undermine the goal of providing broad protection and consistent experiences to consumers. For example, new regulation requires that banks provide borrowers with a disclosure statement, while NBFIs performing quasi-banking functions must provide disclosure statements only if information mandated for disclosure cannot be found in the contract itself.

### Box 5. Main Recommendations

#### Content of Disclosure at the Consumer Level
- Provide a complete picture of a product's pricing and other key terms
- Require disclosure of total cost of credit as a standalone metric, accompanied by repayment schedules
- Low-income consumers focus on repayment schedules, so ensure that they are prominent and comprehensible
- Total cost of credit, APR or EIR, and repayment schedules are complementary, and all three metrics are ultimately desirable in conveying total cost
- Provide clear definitions and standardized formulas for calculating total cost of credit and APR or EIR to facilitate consistent compliance by providers and enforcement by regulators
- Require disclosure of other key terms, particularly those that pose risks in the future, rights and responsibilities, and recourse mechanisms

#### Methods of Disclosure at the Consumer Level
- How information is disclosed and at which stage in the transaction is as important as what is disclosed
- Require standardized summary sheets or disclosure schedules, and use consumer testing to ensure forms are comprehensible to consumers
- Require that disclosed information be conveyed in a clear manner and before the consummation of a transaction

#### Disclosure to the Public
- Regulators can play a direct role in increasing market competition by disseminating pricing information
- Consider the target audience (e.g., general consumers, competing providers, media, investors, etc.) for disclosed information and the desired effect
- Ensure that branch displays convey pricing and key terms in a clear and prominent manner
- Require that providers present comparable information and disseminate advertising and marketing materials through media and channels likely to reach a wide audience (general consumers, competing providers, and other stakeholders)

#### Implementation Considerations
- Use an incremental approach based on country context, taking into consideration compliance costs and industry and regulator capacity
- Industry associations and financial literacy and education can complement regulatory transparency efforts
- Work to expand towards broad, consistent coverage across providers and products

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44 There are separate disclosure requirements particular to credit products, savings products, remittances, and microinsurance.
The minimum information required in such disclosure statements is specified for “small business/retail/consumer credit,” but not for other types of credit.\textsuperscript{47} Such inconsistencies result in gaps in coverage. Furthermore, enforcement across other types of NBFIs is inconsistent, given that the Cooperative Development Authority supervises cooperatives and the Securities and Exchange Commission oversees NGO-MFIs for compliance with consumer protection regulations (though actual oversight is limited).

These experiences suggest that while regulators can aim to craft disclosure regimes that apply broadly across financial institutions and products, particular attention will be required to achieve consistency and expand coverage to those institutions that are not otherwise actively regulated. Bangko Sentral ng Pilipinas has been working on this exact point by reaching out to other regulators, which recently resulted in the Securities and Exchange Commission harmonizing its disclosure rules with new Bangko Sentral ng Pilipinas regulations.\textsuperscript{48} Bangko Sentral ng Pilipinas has also entered into a memorandum of understanding with the national MFI association to bring the association’s members under formal disclosure rules.

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Armenia. 2009. Regulation on Minimum Requirements on Order, Terms and Methods of Communications between the Bank and Depositor, Consumer and Creditor. Central Bank Regulation 8/05.


\textsuperscript{47} See Manual of Regulations for Non-Bank Financial Institutions and Circular No. 730 of July 2011, which amends the Manual of Regulations for Banks.

\textsuperscript{48} See SEC Memorandum Circular No. 7, issued by the Securities and Exchange Commission in September 2011 and addressed to all lending and financing companies, which adopted Circular No. 730 of July 2011 issued by Bangko Sentral ng Pilipinas.


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Reserve Bank of India. 2011. The Micro Finance Institutions (Development and Regulation) Bill.


## ANNEX A: Comparison Tables of Disclosure Regimes

### Background Information by Country/Region

<table>
<thead>
<tr>
<th>Country/Region</th>
<th>Income level</th>
<th>Percent banked</th>
<th>Main financial institutions serving low-income markets</th>
<th>Relevant regulators</th>
<th>Reason chosen for Focus Note</th>
</tr>
</thead>
<tbody>
<tr>
<td>Armenia</td>
<td>Lower middle income</td>
<td>50–75</td>
<td>Predominantly donor-supported universal credit organizations</td>
<td>Central Bank of Armenia</td>
<td>Comprehensive approach to disclosure and transparency regulation</td>
</tr>
<tr>
<td>Bosnia – Herzegovina</td>
<td>Upper middle income</td>
<td>0–25</td>
<td>Nonprofit or for-profit microcredit organizations; commercial banks</td>
<td>Central Bank of Bosnia–Herzegovina (BiH), Banking Agency of the Federation of BiH, Banking Agency of Republic Srpska</td>
<td>Example of microfinance-specific disclosure regime and anecdotal evidence of price declines</td>
</tr>
<tr>
<td>Cambodia</td>
<td>Lower income</td>
<td>0–25</td>
<td>One specialized microfinance bank (ACLEDA); licensed MFIs and MFI-NGOs</td>
<td>National Bank of Cambodia</td>
<td>Demonstrated impact of transparency on pricing in low-income market</td>
</tr>
<tr>
<td>Ghana</td>
<td>Lower income</td>
<td>25–50</td>
<td>Mix of formal, semi-formal, and informal institutions</td>
<td>Bank of Ghana</td>
<td>Example of limited capacity interventions, e.g., through standardized forms</td>
</tr>
<tr>
<td>Pakistan</td>
<td>Lower middle income</td>
<td>0–25</td>
<td>Microfinance banks, MFI-NGOs, commercial banks and Rural Support Programs</td>
<td>State Bank of Pakistan</td>
<td>Example of limited capacity intervention through principles-based regulation</td>
</tr>
<tr>
<td>Peru</td>
<td>Upper middle income</td>
<td>0–25</td>
<td>Predominantly formal institutions; some semi/informal providers</td>
<td>Superintendency of Banking and Insurance, National Institute for Defense of Competition and Protection of Intellectual Property</td>
<td>Comprehensive approach to disclosure and transparency regulation</td>
</tr>
<tr>
<td>Philippines</td>
<td>Lower middle income</td>
<td>25–50</td>
<td>Mix of formal, semi-formal and informal institutions</td>
<td>Bangko Sentral ng Pilipinas, Securities and Exchange Commission</td>
<td>Comprehensive approach to disclosure and transparency regulation</td>
</tr>
<tr>
<td>WAEMU</td>
<td>Six lower income and two lower middle income members</td>
<td>0–25</td>
<td>Predominately mutual or cooperative savings and credit institutions; credit-only NGOs</td>
<td>Central Bank of West African States (BCEAO)</td>
<td>Example of regional-level intervention on disclosure regulation</td>
</tr>
</tbody>
</table>

### Notes

- d MFTransparency (2011).
<table>
<thead>
<tr>
<th>Major Aspects of Disclosure Regimes by Country/Region</th>
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</thead>
<tbody>
<tr>
<td><strong>Content of disclosure to consumer</strong></td>
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<tr>
<td><strong>Armenia</strong></td>
</tr>
<tr>
<td>• APR, with formula</td>
</tr>
<tr>
<td>• Fees and penalties (no penalty allowed for prepayment)</td>
</tr>
<tr>
<td>• Insurance premiums</td>
</tr>
<tr>
<td>• Repayment schedule</td>
</tr>
<tr>
<td>• Foreign currency indexing (if any)</td>
</tr>
<tr>
<td>• Right to complain and internal/external complaint procedures</td>
</tr>
<tr>
<td><strong>Bosnia – Herzegovina</strong></td>
</tr>
<tr>
<td>• EIR, with formula</td>
</tr>
<tr>
<td>• General reference to terms</td>
</tr>
<tr>
<td>• Repayment schedule</td>
</tr>
<tr>
<td>• Foreign currency indexing (if any)</td>
</tr>
<tr>
<td>• Interest assessed on declining balance (rather than flat rate)</td>
</tr>
<tr>
<td>• Amortization table</td>
</tr>
<tr>
<td><strong>Cambodia</strong></td>
</tr>
<tr>
<td>• APR</td>
</tr>
<tr>
<td>• Other credit costs</td>
</tr>
<tr>
<td>• Total amount of payments</td>
</tr>
<tr>
<td>• Costs for breach</td>
</tr>
<tr>
<td>• Repayment schedule</td>
</tr>
<tr>
<td>• Demand clause or variable rate (if any)</td>
</tr>
<tr>
<td>• Insurance premiums</td>
</tr>
<tr>
<td><strong>Ghana</strong></td>
</tr>
<tr>
<td>• APR</td>
</tr>
<tr>
<td>• General reference to important terms</td>
</tr>
<tr>
<td><strong>Pakistan</strong></td>
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<tr>
<td>• Annual EIR, with formula</td>
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<td>• Total amount of interest</td>
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<tr>
<td>• Default rate</td>
</tr>
<tr>
<td>• Commissions and fees, including insurance</td>
</tr>
<tr>
<td>• Repayment schedule</td>
</tr>
<tr>
<td>• Source of variable terms</td>
</tr>
<tr>
<td>• Right to prepay and prepayment penalty fees</td>
</tr>
<tr>
<td>• Information about complaints mechanism</td>
</tr>
<tr>
<td><strong>Peru</strong></td>
</tr>
<tr>
<td>• Simple annual rate, with formula; EIR in certain circumstances</td>
</tr>
<tr>
<td>• Finance charges (interest + fees)</td>
</tr>
<tr>
<td>• Other charges (e.g., insurance, taxes)</td>
</tr>
<tr>
<td>• Total amount financed</td>
</tr>
<tr>
<td>• Delinquency rate</td>
</tr>
<tr>
<td><strong>Philippines</strong></td>
</tr>
<tr>
<td>• EIR</td>
</tr>
<tr>
<td>• Nominal interest</td>
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<tr>
<td>• General reference to terms</td>
</tr>
<tr>
<td><strong>WAEMU</strong></td>
</tr>
<tr>
<td>• Form of pre-agreement statement</td>
</tr>
<tr>
<td>• Before conclusion of agreement</td>
</tr>
<tr>
<td><strong>Methods of disclosure to consumer</strong></td>
</tr>
<tr>
<td><strong>Armenia</strong></td>
</tr>
<tr>
<td>• Simple language, no hidden terms</td>
</tr>
<tr>
<td>• Oral advice on main terms and costs before signing</td>
</tr>
<tr>
<td>• Sufficient time for customer</td>
</tr>
<tr>
<td><strong>Bosnia – Herzegovina</strong></td>
</tr>
<tr>
<td>• Before client receives loan application and before concluding agreement</td>
</tr>
<tr>
<td><strong>Cambodia</strong></td>
</tr>
<tr>
<td>• Form of pre-agreement statement</td>
</tr>
<tr>
<td>• Before conclusion of agreement</td>
</tr>
<tr>
<td><strong>Ghana</strong></td>
</tr>
<tr>
<td>• Oral</td>
</tr>
<tr>
<td>• Legible and comprehensible form contracts</td>
</tr>
<tr>
<td>• Summary sheet</td>
</tr>
<tr>
<td>• Specialized personnel</td>
</tr>
<tr>
<td>• Before signing, signed by borrower</td>
</tr>
<tr>
<td><strong>Pakistan</strong></td>
</tr>
<tr>
<td>• Clear statement in writing</td>
</tr>
<tr>
<td>• Standardized disclosure form if info not in contract</td>
</tr>
<tr>
<td>• Before signing, signed by borrower</td>
</tr>
<tr>
<td><strong>Peru</strong></td>
</tr>
<tr>
<td>• N/A</td>
</tr>
<tr>
<td><strong>Philippines</strong></td>
</tr>
<tr>
<td>• Required in formation visible in branches, ads, media</td>
</tr>
<tr>
<td><strong>Disclosure to public</strong></td>
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<tr>
<td><strong>Armenia</strong></td>
</tr>
<tr>
<td>• Required information on Web, ads, bulletins</td>
</tr>
<tr>
<td><strong>Bosnia – Herzegovina</strong></td>
</tr>
<tr>
<td>• EIR clearly and prominently in branches, ads, media</td>
</tr>
<tr>
<td><strong>Cambodia</strong></td>
</tr>
<tr>
<td>• Required information in written solicitations</td>
</tr>
<tr>
<td>• Regulator publishes online table comparing prices for products</td>
</tr>
<tr>
<td><strong>Ghana</strong></td>
</tr>
<tr>
<td>• General requirement to display in branches, brochures</td>
</tr>
<tr>
<td><strong>Pakistan</strong></td>
</tr>
<tr>
<td>• Required information constantly disseminated via branches, Web, other media, brochures</td>
</tr>
<tr>
<td>• Rules on font, placement</td>
</tr>
<tr>
<td>• Regulator publishes online table comparing prices for products</td>
</tr>
<tr>
<td><strong>Peru</strong></td>
</tr>
<tr>
<td>• Required information in branches</td>
</tr>
<tr>
<td>• Rules on poster size</td>
</tr>
<tr>
<td><strong>Philippines</strong></td>
</tr>
<tr>
<td>• Required information in branches</td>
</tr>
<tr>
<td>• Dissemination in all forms of media</td>
</tr>
</tbody>
</table>

(continued)
## ANNEX A: Comparison Tables of Disclosure Regimes (continued)

<table>
<thead>
<tr>
<th></th>
<th>Armenia</th>
<th>Bosnia – Herzegovina</th>
<th>Cambodia</th>
<th>Ghana</th>
<th>Pakistan</th>
<th>Peru</th>
<th>Philippines</th>
<th>WAEMU</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Applicability</strong></td>
<td>Consumer credit contracts US$269-US$26,885</td>
<td>Banks and micro-credit organizations</td>
<td>Rural credit specialized banks, licensed MFIs, NGOs</td>
<td>Credit agreements of US$66.7 or more</td>
<td>Microfinance banks</td>
<td>Credit contracts involving installment payments, regulated and unregulated providers</td>
<td>Credit granting institutions</td>
<td>Banks, MFIs, government and post office financial</td>
</tr>
</tbody>
</table>
Annex B: Total Cost of Credit, APR and EIR, and Repayment Schedules

This Annex provides further detail on the various methods of disclosing pricing found in the disclosure regimes examined and discusses issues that arise from these various methods.

Total Cost of Credit

Total cost of credit may be a better introductory metric to convey pricing as consumer testing suggests that a monetary sum is easier for low-income consumers to comprehend than percentages. Among the disclosure regimes examined, total cost of credit is required less frequently and with much less standardization than APR or EIR.

A majority of disclosure regimes examined focus more on disclosure of APR or EIR or include only a general reference to the disclosure of fees and commissions rather than requiring these be summed into an amount representing the total cost of credit. As Box B1 shows, the disclosure regimes in Ghana, Peru, and the Philippines require disclosure of some elements that would go into calculating the total cost of credit.

While the disclosure regime in Ghana does require the disclosure of the “finance charge,” there are no further instructions or guidelines as to what this metric includes so as to make it a meaningful way to measure true cost that is uniformly calculated and comparable. The regulatory regime in Peru requires the disclosure of the total amount of interest and the amount of commissions and fees, but not in a single combined metric.

Given that total cost of credit can be a helpful tool to convey true cost to low-income consumers, regulators should consider requiring that it be disclosed prominently as a stand alone, separate metric. A clear definition of total cost of credit and a formula for its calculation is essential to ensure that all appropriate components of cost are fully and consistently captured and reflected and not left to provider discretion.

Box B1. Getting at Total Cost of Credit in Ghana, Peru, and the Philippines

Total cost of credit is the total cumulative amount a borrower must pay for a loan, including interest, fees, and charges over the duration of the loan. Although disclosure regimes often require disclosure of certain components that may allow total cost of credit to be approximated, a clear definition and standardized format for this metric are often not provided.

- Ghana—Preagreement statement discloses the total finance charge, described as the “amount the credit will cost you.”
- Peru—Total amount of interest, and amount and details of commissions and fees passed on to client (including insurance premium), must be individually disclosed.
- Philippines—The total amount of finance charges must be disclosed, as well as nonfinance charges. “Finance charge” is defined as amount to be paid by debtor incident to extension of credit, such as interest or discounts, collection fees, credit investigation fees, attorney’s fees, and other service charges. “Nonfinance charges” are defined as amounts advanced by financial institutions for items normally associated with availment of service purchased that are not incident to extension of credit, such as advances for insurance premiums or registration fees.\(^a\)

Those in Peru, Armenia, and Bosnia–Herzegovina each include a clear definition of APR or EIR and a formula for its calculation with sufficient detail to provide guidance to providers and allow for consistent administration of disclosure rules. (See Box B2)

The definitions for APR and EIR in Armenia, Bosnia–Herzegovina, and Peru are similar except for the treatment of credit insurance and cash collateral. To calculate APR or EIR requires converting the total cost of credit into a percentage of the original loan amount standardized to an annual loan period. Formulas for calculating APR and EIR differ based on whether certain cost elements are included. For instance, the formula prescribed in Bosnia–Herzegovina factors in cash collateral, if...
Box B2. Defining APR and EIR in Armenia, Bosnia–Herzegovina, and Peru

Seven out of the eight disclosure regimes examined in this Focus Note include reference to APR or EIR, and three of these include a formula for its calculation.

- **Armenia**—APR is defined as the total cost of credit reflected in the form of interest on the credit provided and “other payments,” such as credit origination and service fees, insurance, and valuation services. A formula for calculating APR is provided, as well as details on what payments are not included in APR.

- **Bosnia–Herzegovina**—EIR includes nominal interest, commissions and fees to be charged during the loan approval process, any other commissions and fees that are known at the time of calculation to be charged to the client during the loan period, and cash collateral. Detailed methodology for calculating EIR is prescribed by the regulator.

- **Peru**—Annual EIR must include all installments of principal and interest, all commission charges, fees for services provided by third parties, and any other fees that the provider has incurred and that by agreement will be passed on to the consumer, including insurance fees where applicable. A specific formula for calculating EIR as an annualized rate is provided by regulation.

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Any. In Peru and Armenia, insurance premiums are explicitly included, while in Bosnia they are not, though insurance may be implicit in the general reference to any known fees. A standardized industry-wide approach to such features would be helpful given their prevalence with respect to microfinance products.

In other disclosure regimes, requirements regarding APR or EIR are not clearly defined. Definitions vary by country, and formulas for its calculation are not always provided. The disclosure regime in WAEMU requires banks and MFIs to notify borrowers of EIR, the rate per period, and nominal interest rate at the time of granting any credit. The disclosure regime in Pakistan also requires microfinance banks to disclose lending rates using APR. However, neither regime provides a standard definition or formula for calculating APR or EIR.

Several disclosure regimes use terminology that is unclear or confusing. In Ghana, the Borrowers and Lenders Act of 2008 requires lenders to provide prospective borrowers with a preagreement statement that specifies the “interest rate,” but the form of preagreement statement required by law refers specifically to APR, causing confusion as to what is actually required. In the Philippines, Bangko Sentral ng Pilipinas regulations for banks and NBIs used to require disclosure of a “simple annual rate,” defined as “the uniform percentage which represents the ratio, on an annual basis, between the finance charges and the amount to be financed.” However, the standard disclosure statement provided by regulation refers to EIR. Such inconsistent use of terminology and conflicting rules undermine the goal of standardizing interest rate disclosure.

Bangko Sentral ng Pilipinas recently issued a new circular requiring that EIR (rather than the simple annual rate) be disclosed when loans are not payable in one year with a single payment on maturity. In addition, EIR may be expressed as a monthly rate for loans with monthly interest rates. This change may benefit providers of short-term loans given the noted drawbacks of using APR or EIR for such loans. Unfortunately, these benefits are limited by permissive language, which again undermines the goal of standardization and increases the potential for confusion, since some loans may be disclosed using either an annual basis or a monthly basis, apparently at the discretion of the provider. Whichever standard

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49 See Rules, Instruments and Procedures to Implement the Monetary and Credit Policy of the Central Bank of the West African States, Decision No. 397/12/2010, BCEAO.
50 Decision No. 397/12/2010 includes a reference to “regulatory requirements on the subject,” which leaves the possibility that further details may be forthcoming, though none were available at the time of writing this Focus Note.
52 See Circular No. 730 of July 2011, Bangko Sentral ng Pilipinas. The new circular currently applies only to banks.
methods are chosen, a disclosure regime should clarify that use of the standard method is mandatory rather than discretionary.

Although disclosure regimes should include a standardized definition and formula for APR or EIR for providers and general transparency, recent consumer testing in the Philippines suggests that the actual formula need not be disclosed to consumers as such information is excessive and not relevant to decision-making or consumer comprehension.

**Repayment Schedules**

Consumer testing suggests that repayment schedules are one of the most important tools to convey costs to low-income consumers, and therefore should play a central role in disclosure regimes. They serve a complementary role to total cost of credit and APR or EIR, helping consumers assess affordability in relation to their cash flow in addition to total price. The specific elements to be included in repayment schedules can be tailored to context. Regulators should ensure that repayment schedules are displayed prominently and that the content of such schedules is comprehensible and comparable, to the extent possible.

As with total cost of credit, a first step for regulators is to make the provision of repayment schedules to consumers a clear regulatory requirement. In Cambodia, providers of microfinance loans are required to include an amortization schedule with any contract, but there are no requirements as to its content or form. By contrast, the disclosure regime in the Philippines includes an amortization schedule in its sample disclosure form, specifically targeted at small business, retail, and consumer credit. However, use of the sample form is not explicitly required by regulation.

To be useful for low-income consumers, repayment schedules should be prominently displayed in summary sheets and disclosure statements, not only in loan contracts or annexes. The disclosure regime in Ghana addresses this issue by including a payment schedule in its required preagreement statement form. (See Box B3)

Given how heavily low-income consumers focus on repayment schedules, determining which elements render them most effective for assessing affordability is useful. At a minimum, repayment schedules should provide information on the number, date, and amount of installment payments, as is the case in the majority of disclosure regimes that include reference to repayment schedules. Disclosure regimes in the countries studied vary regarding whether disaggregation of payments is required. The disclosure regime in Ghana does not require further breakdown of payments. By contrast, disclosure regimes in Peru and Armenia require that repayment schedules be disaggregated into principal, interest, and other fees (with explicit reference to insurance premiums in Peru), further conveying the price of the financial service.

Accurately portraying the total cost of a loan product requires that repayment schedules include all elements of price, such as fees and charges, cash collateral, mandatory insurance premiums, and taxes. However, arguably not all of these items are appropriate for display in repayment schedules, and the additional detail runs the risk of confusing consumers, particularly if not presented in a clear format. A sensible approach may be to provide a sufficient level of detail so that repayment schedules are comprehensible and consistent and provide the information necessary to assess affordability. The optimal level of detail will need to be tailored to country context and tested through consumer research, after which guidelines regarding format and what other fees must be included in repayment schedules should be provided to ensure a level of consistency across providers.
Repayment schedules in Armenia, Ghana, Peru, and the Philippines must include the number, date, and amount of payments. Some countries also require that payments be disaggregated into detailed cost components.

- **Armenia**—Repayment schedule should specify total amount and schedule of repayment of principal, interest, and other fees.
- **Bosnia–Herzegovina**—Minimum content and a standard template for repayment schedules are specified in regulation (translation not available).
- **Cambodia**—Amortization tables are required in all loan agreements, although no standardized format or content is prescribed by regulation.
- **Ghana**—Standardized preagreement statement provided by law includes a repayment schedule with the number, amount, and date of payments.
- **Peru**—Repayment schedules must include (1) number, frequency, and date of installments or payments to be made, disaggregated into principal, interest, and insurance premium (if applicable); (2) total amount to be paid (sum of principal, interest, and commissions and fees passed on to client); (3) EIR; and (4) reduction in installments or amount owed for early payment, if agreed upon.
- **Philippines**—Sample amortization schedule includes (1) installment number and total installment payment, disaggregated into principal and interest; (2) gross loan amount; and (3) outstanding principal balance.

Box B3. Repayment Schedules in Armenia, Bosnia–Herzegovina, Cambodia, Ghana, Peru, and the Philippines

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