



PRUDENTIAL REGULATIONS FOR MICROFINANCE BANKS

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AGRICULTURAL CREDIT & MICROFINANCE DEPARTMENT

STATE BANK OF PAKISTAN

MicrofinanceRegulations@sbp.org.pk

CONTENTS

PREFACE	1
DEFINITIONS	2
Part 1: General	2
Part-2: Customer Due Diligence and Anti Money Laundering (M)	5
RISK MANAGEMENT (R)	7
Regulation R – 1: Minimum Capital Requirements	7
Regulation R – 2: Exposure against Contingent Liabilities	7
Regulation R – 3: Maintenance of Cash Reserve and Liquidity	7
Regulation R – 4: Statutory Reserve	8
Regulation R – 5: Maximum Loan Size and Eligibility of Borrowers	8
Regulation R – 6: Maximum Exposure of a Borrower from MFBs / MFIs / Other Financial Institutions	9
Regulation R – 7: Credit Report Check	9
Regulation R – 8: Classification of Assets and Provisioning Requirements	9
Regulation R – 9: Rescheduling/Restructuring of Loans	10
Regulation R – 10: Charging-off Non-Performing Loans (NPLs)	11
Regulation R – 11: Classification of Investments and Other Assets	11
Regulation R – 12: Investments of Funds	12
Regulation R – 13: Payment of Dividends	13
CORPORATE GOVERNANCE (G)	14
Regulation G – 1: Size and Composition of the Board	14
Regulation G – 2: Remuneration to Directors	14
Regulation G – 3: Responsibilities of the Board of Directors	14

Regulation G – 4:	Fit and Proper Test	16
Regulation G – 5:	Restriction on Certain Types of Transactions	16
Regulation G – 6:	Internal Audit	17
Regulation G – 7:	Policy Frameworks	17
Regulation G – 8:	Guidelines on Internal Controls and Risk Management	17
Regulation G – 9:	Credit Rating	17
Regulation G – 10:	Declaration of Fidelity and Secrecy	18
Regulation G – 11:	Contributions and Donations for Charitable, Social, Educational and Public Welfare Purposes	18
MONEY LAUNDERING, TERRORIST FINANCING AND OTHER UNLAWFUL ACTIVITIES (M)		19
Regulation M - 1:	Customer Due Diligence (CDD)	19
Regulation M - 2:	Record Retention	23
Regulation M - 3:	Reporting of Currency/Cash Transactions (CTR)	23
Regulation M - 4:	Reporting of Suspicious Transactions (STR)	24
Regulation M - 5:	Implementation of obligations under UNSC Resolutions	24
OPERATIONS (O)		25
Regulation O – 1:	Cash Payments Outside the Authorized Place of Business	25
Regulation O – 2:	Reconciliation/Settlement of Account Entries	25
Regulation O – 3:	Deposits	26
Regulation O – 4:	Consumer Protection	27
Regulation O – 5:	Submission of Quarterly Returns	28
Regulation O – 6:	Window Dressing	28
Regulation O – 7:	Permission Regarding Receipt of Grants	28
Regulation O – 8:	Reporting to Credit Information Bureau (CIB)	29

ANNEXURES	30
Annexure – A	31
Annexure – B	34
Annexure – B - 1	36
Annexure – B - 2	37
Annexure – C	38
Annexure – D	39
Annexure – E	42
Annexure – E - 1	44
Annexure – E - 2	46
Annexure – E - 3	47
Annexure – F	48
Annexure – G	53
Annexure – H	54

Preface

Cognizant of peculiar dynamics and evolution of microfinance sector, SBP maintains a 'proportional' regulatory approach to promote innovation and stability. The underlying principle has always been to keep balance between inclusion and prudence. Specifically, prudence relates to i) stability (Capital / managing credit / operations / liquidity risks) ii) financial integrity (AML/CFT) and iii) consumer protection.

In view of business growth and technological innovations in the sector, SBP has further strengthened the regulations in areas of governance, AML/CFT, consumer protection, and operations to help MFBs to manage the expected higher level of growth in future.

To add clarity, the PRs have been segregated in four categories viz. Risk Management (R), Corporate Governance (G), Customer Due Diligence and Anti Money Laundering (M), and Operations (O). In addition, few instructions in the prudential regulations which have already been covered under MFI Ordinance 2001, have been removed from regulations to avoid repetition. Nevertheless, the omitted clauses remain enforceable on MFBs as part of law.

These Prudential Regulations for Microfinance Banks do not supersede other directives issued by State Bank of Pakistan in respect of areas not covered here. Any violation or circumvention of MFI Ordinance 2001 and SBP regulations/directives for MFBs may render the concerned MFB or its concerned officer(s) liable for penalties as determined by SBP from time to time.

Further, State Bank of Pakistan will continue to oversee the sector-related developments with strategic perspective. For this purpose, SBP will remain open to review any of the existing regulations, while enacting new regulations where prudence is warranted.

Syed Samar Hasnain
Executive Director
(Development Finance Group)

Definitions

For the purpose of these regulations, unless there is anything repugnant in the subject or context:

Part 1: General

- a. **“Approved securities”** shall mean registered Pakistani rupee obligations of the Federal Government including, but not restricted to, Pakistan Investment Bonds (PIBs), Market Treasury Bills (MTBs) and Government of Pakistan Sukuk Bonds.
- b. **“Branchless Banking”** or **“BB”** means conduct of banking activities by authorized financial institutions for customers having a branchless banking account. It does not include the information services already being provided by various FIs to their existing customers using channels like, phone, internet, SMS etc.
- c. **“Contingent liabilities”** mean and include inland letters of credit, letters of guarantee, bid bonds/performance bonds, and advance payment guarantees.
- d. **“Deposit”** means the deposit of money, repayable on demand or otherwise, accepted by a MFB from the public for the purpose of providing microfinance services.
- e. **“Documents”** include vouchers, bills, promissory notes, bills of exchange, securities for advances, claims by or against microfinance bank (MFB) and other record supporting entries in the books of the MFB.
- f. **“Equity”** means and includes paid-up capital, share premium, general reserves and un-appropriated profits of the MFB.
- g. **“Exposure”** means investments and financing facilities provided by the MFB including both fund based and non-fund based.
- h. **“Family member”** of a person means his/her spouse, dependent, lineal ascendants and descendants and dependent brothers and sisters.
- i. **“Independent Director”** means such a person who is not linked directly or indirectly with the MFB or its sponsor. For the purpose of such determination, an "independent director" is a director who:
 - i. Has not been employed by MFB within the last five years;
 - ii. Has not been an employee or affiliate of any present or former external auditor/consultant/legal advisor of MFB within the last three years;
 - iii. Has not been an executive officer or employee of parent, subsidiary or associate

- company of the MFB or where Directors of the MFB have substantial beneficial interest (20% or more shareholding of director's own or combined with family members);
- iv. Has not been employed by a company of which an executive officer of the MFB has been a director within the last three years;
 - v. Has/had no material business relationship with the MFB either directly, or as a partner, shareholder, director or key executive of a body that has/had such a relationship with the MFB within the last three years;
 - vi. Does not hold cross-directorships or have significant links with other directors such as association as partner or common director/major shareholder in other companies or entities;
 - vii. Has not served on the Board for more than six years from the date of his first election or appointment provided that such person shall be deemed "independent director" if re-elected after a lapse of three years.
- j. **"Key Executive"** includes the officials responsible for overseeing following functional responsibilities:
- i. Any executive, acting as second to CEO including Chief Operating Officer, Deputy Managing Director or by whatever name called;
 - ii. Chief Financial Officer/Head of Finance/Head of Accounts;
 - iii. Internal Audit;
 - iv. Risk Management;
 - v. Compliance;
 - vi. Credit;
 - vii. Operations;
 - viii. Human Resource;
 - ix. Information Technology;

The condition for hiring all key executives will become mandatory whenever deposit base or gross loan portfolio of an MFB exceeds Rs. 3 billion, or the MFB completes three years in operations whichever is earlier. Further, if a person is performing more than one of the above-mentioned functions, it shall be ensured that there is no conflict of interest. The same shall also be notified to State Bank of Pakistan.

- k. **"Microfinance Banks - MFBs"** shall mean companies incorporated in Pakistan and licensed by the State Bank of Pakistan as microfinance banks for the purpose of providing microfinance services, especially mobilizing deposits from the public and providing credit to poor persons and micro-enterprises.
- l. **"Microenterprises"** shall mean projects or businesses in trading, manufacturing, services, or agriculture that lead to livelihood improvement and income generation. Moreover, these projects/businesses are undertaken by micro entrepreneurs who are either self-employed or

employ few individuals not exceeding 10 (excluding seasonal labor).

Microenterprises may include carpentry, electrical works, food stalls, farms (crops & non-crops), lathe machine workshops etc; which have traditionally lacked access to formal financial services.

- m. **“Poor Person”** means an individual who has meager means of subsistence but is involved in a livelihood activity and has an ability to repay debt from an annual income (net of business expenses) up to Rs. 500,000/-.
- n. **“Records”** include ledgers, daybooks, cash books, supporting documents and all other manual or magnetic/electronic records used in the business of the MFBs;
- o. **“Specified area”** means the district, region (comprising up to five adjacent districts within the same Province or any other area where Microfinance Institutions Ordinance 2001 is applicable), province or the whole country for which an MFB is licensed to operate;
- p. **“Sponsor Shares”** mean 5% or more paid-up shares of a MFB, acquired by a person(s) individually or in concert with his family members, group companies, subsidiaries, and affiliates/associates.
- q. **“Sponsor Shareholders”** mean all those shareholders of a MFB holding sponsor shares.
- r. **“Sponsor Director”** means the member of the Board of Directors of a MFB holding sponsor shares.
- s. **“State Bank”** means State Bank of Pakistan established under The State Bank of Pakistan Act, 1956.

Part-2: Customer Due Diligence and Anti Money Laundering (M)

- a. **“Beneficial Owner”** refers to the natural person(s) who ultimately owns or controls a customer and /or the natural person on whose behalf a transaction is being conducted.
- b. **“Beneficiary”** means the person to whom or for whose benefit the funds are sent or deposited in bank.
- c. **“Correspondent Bank”** means the MFB in Pakistan which provides correspondent banking services to bank or financial institution situated abroad and vice versa.
- d. **“Correspondent Banking”** means provision of banking services by one bank (correspondent) to another bank (respondent) including but not limited to opening and maintaining accounts, fund transfers, cheque clearing, payable through accounts, permissible foreign exchange services or similar other banking services.
- e. **“Currency Transaction Report”** means as defined under AML Act 2010.
- f. **“Customer”** means a person having relationship with the MFB which includes but not limited to holding of deposit/deposit certificate/ or any instrument representing deposit/placing of money with a MFB, availing other financial services, locker facility, safe deposit facility, or custodial services from the MFB.
- g. **“Customer Due Diligence or CDD”** in broader terms includes;
 - i. Identifying the customer and **verifying the customer’s identity** on the basis of documents, data or information obtained from customer or through reliable and independent source.
 - ii. Identifying, where there is a beneficial owner who is not the customer, the beneficial owner and taking adequate measures to verify his identity so that the MFB is satisfied that it knows who the beneficial owner is, including, in the case of a legal person, trust or similar legal arrangement, measures to understand the ownership and control structure of the person, trust or arrangement.
 - iii. Understanding and, as appropriate, obtaining information on the purpose and intended nature of the business relationship; and
 - iv. Monitoring of accounts/transactions on ongoing basis to ensure that the transactions being conducted are consistent with the MFB’s knowledge of the customers, their business and risk profile, including, where necessary, **the source of funds and, updating records and data/ information to take prompt action when there is material departure from usual and expected activity through regular matching with information already available with MFB.**
- h. **“FATF Recommendations”** means the Recommendations of Financial Action Task Force as

amended from time to time.

- i. **“FMU”** means the Financial Monitoring Unit established under the AML Act 2010.
- j. **“Money Laundering and Financing of Terrorism or ML/TF”** has the same meaning as ascribed to them in AML Act 2010.
- k. **“Online transaction”** means deposit or withdrawal of cash using different branches of a MFB through electronic means.
- l. **“Person”** has the same meaning as ascribed to it under the AML Act 2010.
- m. **“Politically Exposed Persons or PEPs”** are individuals who are entrusted with prominent public functions either domestically or by a foreign country, or in an international organization, for example Heads of State or of government, senior politicians, senior government, judicial or military officials, senior executives of state owned corporations/departments/autonomous bodies. This does not intend to cover middle ranking or more junior individuals in the foregoing categories.
- n. **“Risk”** refers to risk associated with money laundering and financing of terrorism.
- o. **“Suspicious Transaction Report or STR”** as ascribed in AML Act 2010.
- p. **“Walk-in-customer”** means the person conducting occasional transactions and is not a customer having relationship with the MFB.

Risk Management (R)

Regulation R – 1: Minimum Capital Requirements

Microfinance Banks (MFBs) shall maintain a minimum paid up capital (free of losses) of not less than:

- i. **One billion rupees if licensed to operate at national level.**
- ii. Five hundred million rupees if licensed to operate in a specified province;
- iii. Four hundred million rupees if licensed to operate in a specified region; and
- iv. Three hundred million rupees if licensed to operate in a specified district;

The MFBs shall also maintain Capital Adequacy Ratio (CAR) equivalent to at least 15% of their risk weighted assets. Instructions on calculation of CAR based on risk weighted assets are provided in Annexure - A. For the purpose of maintaining minimum CAR, MFBs are also allowed to raise sub-ordinate debt in local currency, subject to obtaining prior written approval from the SBP. The terms and conditions for raising sub-ordinate debt are provided in Annexure - A.

Regulation R – 2: Exposure against Contingent Liabilities

The contingent liabilities of the MFB for the first three years of its operations shall not exceed three times of its equity and thereafter shall not exceed 5 times of the MFB's equity.

Regulation R – 3: Maintenance of Cash Reserve and Liquidity

A. Cash Reserve Requirement:

- i. The MFB shall maintain a cash reserve equivalent to not less than 5% of its deposits (including demand deposits and time deposits with tenor of less than 1 year) in a current account opened with the State Bank or its agent.
- ii. Time deposits with tenor of 1 year and above will not require any cash reserve.

B. Statutory Liquidity Requirement:

- i. The MFB shall maintain statutory liquidity reserve equivalent to at least 10% of its total demand liabilities and time liabilities with tenor of less than 1 year, in the form of liquid assets i.e. cash, gold, unencumbered Treasury Bills, Pakistan Investment Bonds and Government of Pakistan Sukuk Bonds. The MFB shall, however, not account for the Treasury Bills and Pakistan Investment Bonds held

under depositor protection fund for the purpose of calculating statutory liquidity reserve.

- ii. Time liabilities with tenor of 1 year and above will not require any SLR.

MFBs shall submit their CRR and SLR statements along with bi-weekly (fortnightly) statement of affairs to 'Off-Site Supervision & Enforcement Department (OSED) – State Bank' within seven days of the close of the period to which it relates. The format of bi-weekly statement of affairs, statement of CRR, and statement of SLR are prescribed at Annexure - B, B1 and B2 respectively.

Regulation R – 4: Statutory Reserve

The MFB shall create a reserve fund to which shall be credited:

- i. An amount equal to at least 20% of its annual profits after taxes till such time the reserve fund equals the paid-up capital of the MFB.
- ii. Thereafter, a sum not less than 5% of its annual profit after taxes.

Regulation R – 5: Maximum Loan Size and Eligibility of Borrowers

A. Housing Loans:

Maximum Loan size is up to Rs. 500,000/- to a single borrower with annual income (net of business expenses) up to Rs. 600,000/-. However, at least 60% of housing loan portfolio of a MFB should be within the loan limit of Rs. 250,000/- or below.

B. General Loans (Other than housing loans):

The maximum Loan size for general loans is up to Rs. 150,000/- to a poor person with annual income (net of business expenses) up to Rs. 500,000/-

C. Loans to Microenterprises:

Loans to microenterprises shall be up to a maximum of Rs. 500,000/-. The MFB shall extend the enterprise loan only in the name of micro entrepreneur to ensure traceability and reduce the incidence of multiple borrowing.

The aggregate exposure against the enterprise loans in excess of Rs. 150,000/- shall not exceed 40% of the MFB's gross loan portfolio. MFBs shall ensure to have in place appropriate mechanism for monitoring the aggregate exposure limits on enterprise lending.

Only those MFBs that are fully compliant with Minimum Capital Requirement (MCR) and Capital Adequacy Ratio (CAR) shall be eligible to undertake microenterprise lending. The interested MFBs shall develop related institutional capacity (products, credit risk management and monitoring system, trainings etc.) and submit its

detailed business plan of microenterprise lending to SBP for seeking necessary approval for a pilot program. The SBP shall evaluate the plan along with operational/financial performance, funding plan, supervisory assessment, and credit rating of the MFB, and accordingly grant permission for launching pilot program to the applicant MFB. The final approval for enterprise lending shall be granted subject to satisfactory evaluation of pilot program.

Regulation R – 6: Maximum Exposure of a Borrower from MFBs / MFIs / Other Financial Institutions

The maximum limits of the borrowers' aggregate exposure shall not exceed Rs. 150,000/- for general loans, Rs. 500,000/- for housing loans, and Rs. 500,000/- for microenterprise loans. The aggregate exposure of the borrowers who are eligible to avail both general and microenterprise loan shall not exceed Rs. 500,000/-.

The MFBs shall develop an internal mechanism to monitor the overall exposure of their borrowers so as to manage credit risk and also minimize the borrowers' over indebtedness risk. At the time of granting facility, MFBs shall obtain a written declaration on the prescribed format attached as Annexure – C from the borrower divulging details of various facilities already obtained from other MFBs / MFIs / Banks / other Financial Institutions. The MFBs shall ensure that total exposure of their clients does not exceed their total repayment capacity as determined under the criteria laid-out in the MFBs' credit policy.

Regulation R – 7: Credit Report Check

Before allowing any credit facility, the MFBs shall obtain a credit report from the Credit Information Bureau (CIB) of State Bank of Pakistan, or from any other appropriate Credit Information Bureau of which they are a member. However, if credit facility exceeds Rs. 30,000, it will be mandatory for MFBs to obtain credit report from Credit Information Bureau of State Bank of Pakistan.

MFBs shall assign due weightage to the CIB reports in addition to their approved criteria while undertaking credit appraisal of the prospective borrower. Credit applications, however, may not be turned down solely on the basis of overdue amount reported in the CIB report.

Regulation R – 8: Classification of Assets and Provisioning Requirements

A. Specific Provisioning

The outstanding principal and mark-up of the loans and advances, payments against which are overdue for 30 days or more, shall be classified as Non- Performing Loans (NPLs). The unrealized interest / profit / mark-up / service charges on NPLs shall be suspended and credited to interest suspense account. Further the NPLs shall be divided into following categories:

Category	Determinant	Provisioning Requirement
Other Assets Especially Mentioned (OAEM)	Loans (principal/mark-up) is overdue for 30 days or more but less than 60 days	NIL
Substandard	Loans (principal/mark-up) is overdue for 60 days or more but less than 90 days	25% of outstanding principal net of Cash collaterals and Gold (ornaments and bullion) realizable without recourse to a Court of Law
Doubtful	Loans (principal/mark-up) is overdue for 90 days or more but less than 180 days	50% of outstanding principal net of Cash collaterals and Gold (ornaments and bullion) realizable without recourse to a Court of Law
Loss	Loans (principal/mark-up) is overdue for 180 days or more	100% of outstanding principal net of Cash collaterals and Gold (ornaments and bullion) realizable without recourse to a Court of Law

In addition, MFBs shall maintain a watch list of all accounts overdue for 5 – 29 days. However, such accounts may not be treated as NPL for the purpose of Classification / Provisioning.

B. General Provisioning

The MFB shall maintain a General Provision equivalent to 1.0% of the net outstanding advances (advances net of specific provisions). However, general provision shall not be required in cases where loans have been secured against gold or other cash collateral with appropriate margin.

Regulation R – 9: Rescheduling/Restructuring of Loans

In order to restructure/ reschedule NPLs, MFBs shall have in place a policy duly approved by their Board of Directors (BOD). The policy shall take following into account:

- i. Rescheduling/restructuring is not done to break timeframe or allow un-warranted improvement in classified category of loans/advances.
- ii. A mechanism is in place, to identify and verify the genuineness of circumstances of the concerned borrowers before rescheduling/ restructuring.
- iii. The rescheduled/restructured loans shall remain classified unless serviced regularly for 6 months excluding grace period (if any) or at least 40% of the outstanding amount principal along with accrued mark-up is recovered in cash.

- iv. In cases where rescheduled / restructured loans are not recovered on revised maturity date, they shall be classified directly as 'losses'.
- v. Envisage steps to provide relief to borrowers adversely affected by natural calamities. MFBs may grant appropriate relaxation either on case-to-case basis or en-block to the borrowers in the affected area. Further, MFBs are encouraged to develop risk mitigation strategies such as availing crop loan insurance, for eligible crops, so as to reduce vulnerability in such situations.

Regulation R – 10: Charging-off Non-Performing Loans (NPLs)

All NPLs shall be charged off, one month after the loan is classified as "Loss". The intent of 'charge-off' is to clear the balance sheet of MFBs, and this shall in no way extinguish the MFBs' right of recovery of such loans.

Note: Charge-off means reducing the value of the loans in 'loss' category to zero through offsetting the provisions, thus, removing such loans from the balance sheet.

Regulation R – 11: Classification of Investments and Other Assets

The MFBs shall categorize their investments into three categories viz. 'Held for Trading', 'Available for Sale' and 'Held to Maturity'. The securities should be categorized at the time of their acquisition and the decision to this effect shall be recorded in the deal ticket.

The MFB shall classify a security as Held-To-Maturity (HTM) if it has intent and ability to hold such investments till their maturity. Securities categorized as HTM shall be valued at amortized cost. However, in case of impairment, they will be subject to revaluation and the impaired amount shall be charged to Profit and Loss Account.

The investments once categorized will not be shifted to or from 'HTM'. The investments in 'Held for Trading' may be shifted to 'Available for Sale' category only under exceptional circumstances and after approval of MFB's Asset and Liabilities Committee (ALCO) with the reasons recorded in writing. While shifting the securities, the same will have to be valued at lower of cost/book or market value at that date and any diminution shall be fully provided for through profit and loss account.

The securities categorized as 'Held for Trading' shall be disposed off within 90 days from the date of their acquisition.

Investment portfolio in 'Held for Trading' and 'Available for Sale' shall be evaluated for the purpose of their valuation and classification keeping in view various subjective and objective factors given as under:

a) Quoted Securities:

Government Securities will be valued at PKRV (Reuter Page). Debt securities such as TFC and mutual funds shall be valued at their market value. The difference between the market value and book value will be treated as surplus/deficit.

b) Un-quoted Securities:

TFCs and mutual funds shall be carried at amortized costs. These securities will be tested for any impairment and classification on the evaluation date on the basis of both objective and subjective criteria (aging of default, future payment capacity, project/company's financial condition, business conditions etc;).

c) Treatment of Surplus/Deficit:

The measurement of surplus/deficit shall be done on portfolio basis. The surplus/deficit arising as a result of revaluation of 'Held for Trading' securities shall be taken into Profit & Loss Account. The surplus/deficit on revaluation of 'Available for Sale' category shall be taken to "Surplus/Deficit on Revaluation of Securities" through statement of comprehensive income. Impairment in the value of 'Available for Sale' securities will be provided for by charging it to the Profit and Loss Account.

Classification of 'Other Assets' and provision required there-against shall be determined keeping in view the risk involved and the requirements of the International Financial Reporting Standards (IFS).

MFBs are required to take appropriate measures to comply with the above conditions within six months of the issuance of these regulations.

Regulation R – 12: Investments of Funds

MFBs may invest their surplus funds in Government Securities, 'A' rated debt securities like TFCs and units of those mutual funds which maintain their investment portfolio in fixed income securities or money market instruments.

In addition, MFBs may acquire or hold shares of any corporate body, the objective of which is to provide microfinance services, technical, vocational, educational, business development and allied services to the poor and micro enterprises. The maximum investment in such a company or security shall not exceed 10% of paid-up share capital of that company or 5% of MFBs' own equity free of losses, whichever is less. For making investment in excess of the 5% limit, prior permission from SBP shall be obtained. The aggregate investments in such corporate bodies shall not exceed 10% of MFBs' equity, free of losses.

Regulation R – 13: Payment of Dividends

MFBs shall not pay any dividends on their shares until:

- i. They meet the MCR and CAR as laid down by the State Bank from time to time;
- ii. All the provisions/appropriations laid down in MFI Ordinance 2001 and the Prudential Regulations for Microfinance Banks have been made.

CORPORATE GOVERNANCE (G)

Regulation G – 1: Size and Composition of the Board

MFBs shall ensure that the skill mix of the Board is compatible with the objectives, plans and functions of the MFB and that the board is in a position to give direction to the executive management and steer the MFB in the desired direction. The board shall have:

- i. Minimum of seven members.
- ii. Not more than 25% of the members from the same family.
- iii. At least 2 independent members.
- iv. No more than 25% of the members as paid executives of the MFB.
- v. Chairman who is not the CEO of the MFB.

Further, MFBs are encouraged to have adequate female representation on their Board of Directors. MFBs are required to comply with the above conditions within six months of the issuance of these regulations.

MFBs shall also ensure that no member of the Board of Directors of a MFB holding 5% or more of the paid-up capital of the MFB either individually or in concert with his/her family members or concerns / companies in which he / she has the controlling interest, shall be appointed in the MFB in any capacity save as the Chief Executive of the MFB.

Regulation G – 2: Remuneration to Directors

No payment shall be made or perquisites provided to the non-executive directors and chairman other than reasonable fees, in addition to traveling and lodging expenses (on actual basis), for attending meetings of the Board of Directors or its Committees. MFBs may determine a 'reasonable fee' but not exceeding Rs. 25,000 per meeting. If meetings of the Board of Directors and its Committees are scheduled on the same day, the MFB shall not pay a separate fee for each meeting. Further, the scale of fee shall be approved by the shareholders on pre or post facto basis in the Annual General Meeting (AGM). However, if a MFB intends to pay above the prescribed ceiling of Rs. 25,000, it would require prior permission from SBP. The executive directors will only be paid usual TA/DA as per MFB's standard rules and regulations.

Regulation G – 3: Responsibilities of the Board of Directors

The Board of Directors of MFBs shall:

- i. Define vision & mission and set strategic goals & objectives.
- ii. Approve annual business plan, and monitor its progress on regular basis.

- iii. Undertake and fulfill their duties & responsibilities keeping in view their obligations under the applicable laws and regulations.
- iv. Ensure that the MFB maintains high standards of disclosure, transparency, fair treatment with consumers, and compliance with rules and regulations.
- v. Attend training program(s) on corporate governance preferably at least 1 week within first year of their directorship to be able to play effective role as a director on the board of MFB. However, those Directors who have already attended such programs or have served on the board of any foreign corporate body shall be exempted from such training programs.
- vi. Induct appropriately qualified and experienced CEO and management, and assess their performance. Recommend re-appointment of Chief Executive Officer/President and members of the board on the basis of their performance, and ensure appropriate skill-mix in the board composition.
- vii. Ensure that succession policy is in place for key management positions.
- viii. Clearly define the authorities and key responsibilities of both the Directors and the Senior Management without delegating its policy-making powers to the Management and shall ensure that the Management is in the hands of qualified personnel.
- ix. Approve and ensure implementation & compliance of internal policies relating to business and operations. Moreover, existing policies shall be reviewed and updated periodically or whenever circumstances justify.
- x. Hold frequent/regular meetings (not less than once every quarter). The individual directors of an MFB shall attend at least half of the meetings held in a financial year. The board should ensure appropriate MIS for receiving sufficient information from management on the agenda items well in advance of each meeting to be able to effectively participate in and contribute to each meeting.
- xi. Form specialized committees with well-defined objectives, authorities and tenure. These committees, preferably comprising of 'Non-Executive' Board members, shall oversee areas like audit, risk management, compensation etc. The Audit Committee of the board shall be chaired by the Independent Director. These committees of the board shall not indulge in day-to-day affairs/operations of the MFB and shall apprise the board of their activities, findings, and recommendations on regular basis.
- xii. Ensure that permanent committees of the board have charters approved by the board as a whole.
- xiii. Ensure that the audit committee of the board shall not include membership from the management. The audit committee must include an expert on accounting and financial analysis. It must meet with the external auditors in the absence of management.
- xiv. Inform State Bank of Pakistan (SBP) at least two months ahead of implementing its decision to remove its President/Chief Executive Officer (CEO) before the expiration of his/her term of office, through the defined statutory process along with reasons recorded in writing for the same. The Chairman of the Board of Directors of the MFB shall be responsible for submission of the requisite information to SBP.
- xv. The President/CEO, whenever, decides to tender resignation before completion of his/her term in office, he/she must inform SBP at least two months before tendering resignation.

Board of Directors is required to undertake measures, within six months of the issuance of these regulations, to meet its newly prescribed responsibilities.

Regulation G – 4: Fit and Proper Test

The Board Members and President/Chief Executive are custodians of public savings deposited with the MFBs. Thus, they should not only be persons of established integrity and track record, but should also have necessary capacity, qualification and experience to effectively undertake their respective responsibilities and functions in order to lead and steer the MFB as a commercially viable and socially responsible financial institution.

State Bank of Pakistan has, formulated “Fit & Proper Test” for selection/appointment, re-appointment/renewal, and interim appointment of the Board Members and President/Chief Executive of Microfinance banks, which prescribes the minimum qualifications, experience and integrity standards, etc. for the MFBs’ Board Members and President/Chief Executive. The criterion is given at Annexure - D.

For appointment of key executives, SBP’s prior approval is not required; however, MFBs shall furnish information of their key executives to SBP. MFBs shall provide FPT particulars of all key executives within six months of issuance of these regulations. The MFBs shall submit information about the Board Members and/or President/Chief Executive Officer and key executives to State Bank as per Annexure - E, E – 1, E – 2 and E – 3, respectively.

Fit & Proper Test prescribed in these regulations is continuous in nature. Therefore, all persons subject to FPT shall immediately submit any change in the information already submitted (at the time of clearance) either through their Company Secretary or Human Resources Department to Banking Policy and Regulations Department and copy to Agricultural Credit and Microfinance Department of State Bank. Violation of the instructions, circumvention, concealment, misreporting and delay in submission of information to SBP may result in withdrawal of SBP approval.

Regulation G – 5: Restriction on Certain Types of Transactions

The MFBs shall not:

- i. Allow any facility for speculative purposes.
- ii. Take any exposure on its sponsors, directors or employees including their spouses, parents, and children. The rule shall not apply on deposit services offered by the MFB and loans given to employees under staff loan policy of the MFB.
- iii. Offer preferable treatment to the deposit accounts of its sponsors, directors or employees including their spouses, parents, and children.
- iv. Enter into leasing, renting and sale/purchase of any kind with their directors, officers, employees or such persons who either individually or in concert with family members beneficially owns 5% or more

of the equity of the MFB. This restriction does not apply in case of purchase of vehicles, laptops, mobile phone devices and iPads by the paid directors, officers or employees of the MFBs which remained in their own use, provided such sale is covered under the employees service rules duly approved by the Board of Directors of the MFB and is effected by the MFB at least at book value at the date of such transaction.

- v. Hold, deal or trade in real estate except for use of MFB itself.

Regulation G – 6: Internal Audit

The MFBs shall have an Internal Audit Department manned preferably by professionals/persons having prior audit experience in MFBs/Banks/Financial Institutions. The Head of the Department shall report directly to the Board of Directors or to an Audit Committee of the Board which shall inter alia evaluate his/her performance annually. However, Head of Internal Audit may report administratively to the President/CEO.

Regulation G – 7: Policy Frameworks

The MFBs shall formulate policies for all functional areas of operations including but not restricted to risk management, micro-credit, deposit operations, investments, internal audit, human resources, and rescheduling / restructuring / write-off of loans / advances etc. These policies shall be duly approved by the Board of Directors. The Board shall also be responsible to review and update existing policies periodically and whenever circumstances justify it. The Board shall develop and implement newly prescribed policies within six months of issuance of these regulations.

Regulation G – 8: Guidelines on Internal Controls and Risk Management

The MFBs shall follow at minimum the instructions and standards given in the guidelines on i) Risk Management ii) Internal Controls iii) IT Security and iv) Business Continuity Management. The guidelines are given at Annexure - F. MFBs shall ensure implementation of these guidelines within six months from the date of issuance of these regulations.

Regulation G – 9: Credit Rating

The MFBs shall get themselves rated by any of the rating agencies on the approved panel of State Bank of Pakistan or any international microfinance rating agency, with prior approval of SBP, within three years of grant of license by State Bank of Pakistan to operate as MFB or within one year of commencement of deposit

mobilization services whichever is earlier.

The credit rating shall be an ongoing process and updated on a regular basis from year to year within four months of the close of financial year after the first rating as stated in the first paragraph. The rating report shall be submitted to Agricultural Credit & Microfinance Department, and Offsite Surveillance and Enforcement Departments of State Bank of Pakistan within 7 days of notification of the latest rating. The rating shall also be disclosed to the public within 15 days of the notification of the latest rating by the rating agency.

Regulation G – 10: Declaration of Fidelity and Secrecy

Every member, director, auditor and staff member of the microfinance bank shall, before entering upon his office and performance of duties, make a declaration of fidelity and secrecy in the form as prescribed in Annexure - G.

Regulation G – 11: Contributions and Donations for Charitable, Social, Educational and Public Welfare Purposes

MFBS shall strictly observe the following rules in the matter of making any donation/contribution for charitable, social, educational or public welfare purposes:

- i. The MFBS shall develop policy/guidelines duly approved by their Board of Directors for making donations/contributions.
- ii. The total donations/contributions made by the MFBS during the year shall not exceed such amount as approved by their Board of Directors. MFBS making these donations/contributions shall already have met provisioning and capital adequacy requirements.
- iii. All donations or contributions to be made during the year must be specifically approved by the Board of Directors on pre or post facto basis.
- iv. MFBS shall expressly disclose in their annual audited financial statements the total donation/contribution made during the year along with names of donees, to whom total donations/contributions during the year were made in excess of Rs 100,000/. In case of donations where any director or his family members have interest in the donee, the names of such directors, their interest in the donee and the names and addresses of all donees, shall also be given.

MONEY LAUNDERING, TERRORIST FINANCING AND OTHER UNLAWFUL ACTIVITIES (M)

To safeguard Microfinance Banks (MFBs) from the threat of Money Laundering, Terrorist Financing and other related unlawful activities, the following minimum standards are required to be followed by all the MFBs. Microfinance banks are free to take additional measures as per risk involved in line with Financial Action Task Force (FATF) recommendations. MFBs shall ensure to develop and implement following policies within six months of issuance of these regulations.

Regulation M - 1: Customer Due Diligence (CDD)

- 1) Know Your Customer/ Customer Due Diligence Policy:** All MFBs shall formulate a comprehensive KYC/CDD policy duly approved by their Board of Directors. The policy shall be communicated down the line to relevant officers / staff. Copies of the KYC/CDD policy shall be submitted to the Agricultural Credit and Microfinance Department (AC&MFD) of the State Bank of Pakistan. Any change in policy shall also be conveyed to SBP within seven (07) days of its approval from the Board of Directors.

MFBs shall apply customer due diligence measures including identification and verification of customers before opening a new account or extending any credit facility or establishing new business relationships. MFBs shall take all reasonable measures to perform due diligence of their existing and prospective customers to establish their identity and to confirm that the customer is not exploiting microfinance banking channel for any criminal activity, money laundering or terrorist financing.

- 2) Systems, Controls and Procedures:** MFBs shall put in place systems, controls and procedures for combating money laundering and terrorist financing which may include but not limited to;
 - i. Compliance setup under the supervision of a well qualified, senior and independent official who shall be responsible to ensure compliance with AML/CFT policies and procedures.
 - ii. Adequate screening procedures to ensure high standards when hiring employees.
 - iii. **An ongoing employee training program for relevant staff/officers.**
 - iv. Audit function to assess the adequacy of the policies & procedures and to evaluate the effectiveness of risk management process.
 - v. **Appropriate policies and procedures on internal controls.**
- 3) Identity of Individual Customers:** Identity of all the prospective customers shall be established with all reasonable efforts. Before establishing any banking relationship with the client, MFBs shall inter alia obtain copy of Computerized National Identity Card (CNIC), Passport, National Identity Card for Overseas Pakistanis (NICOP), Pakistan Origin Card (POC) or National Alien Registration Authority (NARA) Card of the prospective customer. **The copy of identity document so obtained shall be stamped as “original seen” after comparing it with the original document.**

In case of a salaried person, MFBs shall obtain copy of his/her service card, or any other acceptable evidence of service in addition to the attested copy of CNIC.

In case of an illiterate person, MFBs shall take additional measures such as recent photograph of the new account holder besides taking his/her right and left thumb impression on the specimen signature card.

In case of joint account, CDD measures on all the joint account holders shall be performed as if each of them were individual customers of the MFB.

MFBs may open account on the basis of attested copy of NADRA receipt/token for new CNIC, provided all other requirements of account opening under Prudential Regulations for Customer Due Diligence are complied with. MFBs shall, however, obtain copies of CNICs of such customers within three months of the opening of account.

- 4) Documents Required for Other than Individual Accounts:** For all accounts other than individuals' accounts, list of the required documents is given in Annexure – H.
- 5) Verification of the Identity:** Before opening of accounts or starting operation in the accounts, MFBs shall verify CNIC /NICOP/ POC from the Verisys of NADRA. Where the identity documents are other than CNIC/NICOP/ POC, MFBs shall make all efforts to verify the identity document from the concerned issuing authority /from reliable, independent source documents, database or information.

MFBs are allowed to provisionally open accounts (restricting debits) during the verification process of CNIC subject to;

- i. Completion of verification within five (05) working days from the date of application of account opening, and
- ii. Management of related risks effectively during the period.

Where it is difficult to establish identity of the prospective customer or verification of their identity, MFBs should not operate the account.

- 6) Micro-Saving Accounts:** These are privileged savings accounts offered only to low income and poor persons who are traditionally excluded from formal financial system. These accounts can be opened after establishing identity of customer only, and upon approval of the branch manager. Balance limits for such accounts shall, however, not exceed Rs. 100,000.

MFBs shall ensure proper systems and controls to avoid misuse of this relaxation. MFBs shall also conduct regular internal audit to review and assess effectiveness of the relevant controls. If there arise any doubt on the identity of the micro-saving account holder or a suspicion of money laundering and/or terrorist financing, MFB shall verify identity document of such account holders from NADRA.

MFBs shall also encourage women in remote areas to open accounts for saving and other purposes. If women in remote areas do not possess identity cards, MFB shall guide them for obtaining their own

Computerized National identity Cards (CNIC). Meanwhile, MFBs may open their micro-saving accounts, on the basis of attested copy of CNIC of her father/husband, for six months only. MFBs shall also obtain any document related to account holder e.g., Nikah Nama, Birth Certificate, Driving License, Educational Degree/ Certificate, Pension Book or Insurance Certificate.

- 7) **Identification and Verification of Beneficial Owner:** MFBs are required to identify the beneficial owner and take all reasonable measures to verify the identity of the beneficial owner during the course of establishing a business relationship or conducting transaction.
- 8) **Anonymous Accounts:** MFBs shall not allow opening of anonymous or numbered accounts or accounts in the names of fictitious persons.
- 9) **Purpose of Account / Relationship:** MFBs shall obtain from the customer intended purpose of account and likely sources of fund before starting any business relationship or opening of an account. Personal / individual accounts shall not be allowed to be used for charity purpose / collection of donation.
- 10) **On-Going Customer Due Diligence:** Ongoing Customer Due Diligence is an essential aspect of effective KYC/CDD procedures and applies to all customers to whom the MFB is offering any type of service(s). Ongoing due diligence includes monitoring and scrutiny of transactions undertaken throughout the course of business relationship to ensure that the transactions being conducted are consistent with the institution's knowledge of the customer, purpose of account, their business and risk profile, and where necessary, the source of funds. MFBs shall keep on conducting customer due diligence at reasonable periodic intervals or on significant occasions throughout the business relationship, e.g.;
 - i. Nature of product and services requested by the customer changes.
 - ii. Significant transaction or series of transactions take places.
 - iii. Significant change occurs in the way customer operates his account.

MFBs shall ensure that the documents, data or information collected under CDD process is kept up-to-date and relevant by undertaking reviews of existing records.

- 11) **Enhanced Due Diligence:** It is possible that certain customers/transactions may pose high risk to MFBs. The high risk factors must be defined in the KYC/CDD policy which may include the description of such customers, products, transaction channels and geographic elements. In particular, following shall also be considered for enhanced due diligence;
 - i. Having suspicion of money laundering or terrorist financing.
 - ii. Customers belong to countries where KYC and money laundering regulations are lax, or those with links to offshore tax haven.
 - iii. Customers are in cash based businesses and deal in high-value items and where customers have high net worth with no clearly identifiable source of income, etc.
 - iv. MFBs have reason to believe that the customer has been refused banking facilities by another bank / DFI / MFB.

- v. While establishing business relationship with politically exposed persons (PEPs), their family members and close associates.
- vi. While establishing business with Non-Governmental Organizations (NGOs) / Not-for-Profit Organizations (NPOs) and Charities.
- vii. Opening of correspondent banks' accounts, and taking appropriate measures to obtain all relevant information about the correspondent bank.
- viii. The customer resides in a country which does not comply with FATF Recommendations.

In case of PEPs and correspondent banking, MFBs are required to obtain senior management approval for establishing or continuing business relationship.

12) Walk in Customer:

- i. MFBs shall obtain copy of CNIC (regardless of threshold) for online deposits/fund transfers conducted by walk-in-customer.
- ii. MFBs shall obtain CNIC from walk-in customers conducting cash transactions above Rupees one million whether carried out in a single operation or in multiple operations that appears to be linked.
- iii. For rest of transactions, identification requirements may be defined above an appropriate limit by MFBs themselves in their KYC/CDD policies.

13) Government Accounts: MFBs shall not allow opening of Government accounts in personal names of individuals. The Government account shall be opened on production of special resolution/authority from the concerned department duly endorsed by the Ministry of Finance (MoF) or Finance Department of the concerned (Provincial, Federal etc.) Government. This requirement is not applicable on institutions which do not fall under the purview of MoF. Further, Government accounts shall be operated by the designated officer(s) only.

14) Public Awareness Campaign on Requirement of CNIC: MFBs shall encourage customer services officers/tellers and other MFB staff, directly in touch with the customer, to create awareness on requirement of CNIC and shall facilitate/guide them to obtain CNIC.

15) New Technology: MFBs shall pay special attention to any money laundering threat that may arise from new technologies that might favor anonymity and take measures, if required, to prevent their use in money laundering schemes. Measures for managing risks should include specific and effective CDD procedures that apply to non-face-to-face customers. In particular, MFBs should have policies and procedures in place to address anonymity risk associated with non-face-to-face customers/business relations/transactions. These policies and procedures should apply when establishing customer relationship and when conducting ongoing due diligence.

16) Non-Satisfactory KYC / CDD: In case, MFB is not able to satisfactorily complete the required CDD measures, account shall not be opened or any service provided and consideration should be given if the circumstances are suspicious so as to file an STR. If CDD of an existing customer is found unsatisfactory,

the relationship should be treated as high risk and reporting of suspicious transaction be considered as per law, and circumstances of the case.

Regulation M - 2: Record Retention

The records of transactions and identification data should be maintained by MFBs in systematic manner with exactness of period of preservation. For the purpose, following minimum requirements shall apply;

- i. **Identification Record:** MFBs shall keep record on the identification data obtained through the Customer Due Diligence (CDD) process, account files and business correspondence for at least Ten (10) years following the termination of the business relationship.
- ii. **Transactions Record:** MFBs shall maintain all necessary records on transactions, both domestic and International, for at least Ten years following completion of the transaction. Such record must be sufficient for reconstruction of individual transactions so as to provide, if necessary, evidence for investigation or prosecution of criminal activity.

The examples of the necessary components of transaction record may include: customer's name (beneficiary's name), address, nature and date of transaction, type and amount of transaction, currency involved, type and identification of any account involved in the transaction.

The identification and transactions record shall be made available to SBP or other domestic authorities that are competent, under law, to obtain this information and record.

MFBs shall, however, retain records for longer period where transactions and / or relationship relate to any investigation, litigation or required by the court of law or by any other competent authority.

Moreover, the transactions record may be maintained in paper or electronic form or on micro film, being admissible as evidence in a court of law.

Regulation M - 3: Reporting of Currency/Cash Transactions (CTR)

All MFBs shall adhere to the provision of Currency/Cash Transactions Report under the Anti-Money Laundering Act, 2010 and report currency/cash transactions to the Director General of the Financial Monitoring Unit (FMU). The Currency/Cash Transactions Guidance Notes and Reporting Form are available on the official website of FMU.

Regulation M - 4: Reporting of Suspicious Transactions (STR)

If an MFB suspects or have reasonable grounds to suspect that funds are the proceeds of a criminal activity, or are related to terrorist financing, it shall report within seven days its suspicions to the Director General, Financial Monitoring Unit (FMU). The report should be on the format prescribed by FMU.

MFBs, their Directors, Officers and Employees are strictly prohibited from disclosing (tipping-off) the fact that an STR or related information is being filled with the FMU.

The red flag indicators are available in AML/CFT Regulations for Banks / DFIs at http://www.sbp.org.pk/l_frame/aml.htm

Regulation M - 5: Implementation of obligations under UNSC Resolutions

MFBs shall ensure strict compliance of legal and regulatory requirements including freezing actions and prohibition of dealing with designated persons and entities as per the Statutory Notifications issued by Federal Government from time to time under United Nations (Security Council) Act, 1948 to apply certain measures for giving effect to the decisions of the relevant United Nations Security Council resolutions, and, notifications issued under Anti Terrorism Act, 1997.

OPERATIONS (O)

Regulation O – 1: Cash Payments Outside the Authorized Place of Business

The MFBs shall not undertake any business of cash payments at any place other than the authorized place of business. However, this rule shall not apply in case of mobile banking and branchless banking where permission has been obtained from the State Bank.

Regulation O – 2: Reconciliation/Settlement of Account Entries

The entries booked in the Inter-Branch Accounts and/or Suspense Account must be reconciled/cleared and taken to the proper heads of accounts within a period of 30 days from the date entry is made in the aforementioned accounts.

The above instruction shall not apply on the entries related to outstanding amount of the following, which may either be recorded in their respective head of accounts (1-7) or classified in other assets (8-9);

- i. Entries made on account of tax at source.
- ii. Advance tax paid.
- iii. Tax recoverable.
- iv. Advance expense on new branches.
- v. Advance rent paid.
- vi. Legal expenses.
- vii. Mark-up/service charge recoverable.
- viii. Premium on Crop Loan Insurance Scheme (CLIS) receivable from Government of Pakistan (GoP). The outstanding amount shall, however, be reconciled/cleared immediately on reimbursement of premium amount from the GoP.
- ix. Frauds and forgeries, cash theft and looted, payments against equity, and contributory payments of capital nature to be capitalized at a later stage. The exclusion of entries relating to frauds and forgeries, cash theft and looted will, however, be subject to the condition that the same are cleared immediately on receipt of insurance claims.

MFBs shall institute an effective internal control system for the operations of Inter-Branch and Suspense Accounts, which ensures reconciliation/clearing of the entries in shortest possible time and also clearly fixes the responsibilities on the official(s) for neglecting the timely reconciliation and clearance.

Regulation 0 – 3: Deposits

MFBs shall develop appropriate products for attracting deposits and encouraging savings, especially small savings from low-income groups. They shall facilitate both existing depositors for convenient/smooth operations of their accounts and potential depositors at the time of account opening. MFBs shall also ensure adequate training of their concerned staff to improve the quality of their deposit services. MFBs shall ensure to meet requirements stipulated for deposit operations within six months of issuance of these regulations.

A. Basic /Micro Savings Account

In order to mobilize savings especially from low income individuals, all MFBs shall offer a basic or micro savings account.

B. Opening of Deposit Accounts

- i. MFBs shall entertain all requests to open deposit accounts by persons who meet the requirements laid out in these Prudential Regulations, other instructions issued by the State Bank, and MFBs' own policies.
- ii. MFBs must apprise potential depositors with the different types of accounts and options available to them.

C. Service Charges and Minimum Balance Requirements

For all types of profit and loss deposit accounts (except those with added services):

- i. MFBs shall not levy service charges for their deposit services.
- ii. There shall be no minimum balance requirements. However, MFBs may require an initial balance not exceeding Rs. 100/- to open an account.

D. Statement of Account

MFBs shall provide at least half yearly statements of account for all accounts having an average daily balance of Rs. 10,000/- and above. MFBs may issue statements of account either through surface mail (registered or courier) or other appropriate means. For accounts below average daily balance of Rs. 10,000/-, MFBs shall develop an appropriate policy for issuing statements of account to the concerned depositors.

MFBs shall make all reasonable efforts to update the customers' records including CNIC of their account holders if statements of account are returned / undelivered.

Regulation O – 4: Consumer Protection

MFBs are required to implement following provisions within six months of issuance of these regulations.

A. Financial Literacy

Since the customers of MFBs often lack awareness about their rights and obligations, each MFB shall therefore develop a mandatory basic financial literacy program for them. The program at minimum shall cover charges/fees, interest rate calculation, repayment schedules, customers' obligations and other terms and conditions of all financial services (loan, deposit, insurance, payments etc.) that MFB offers. In addition, the program will also educate customers about how to lodge a complaint and track the resolution of complaints.

B. Transparency and Disclosure

While extending any service to a customer, the MFBs shall lay out detailed terms and conditions which must:

- i. Encompass the repayment schedule, if establishing a lending relationship, which discloses the period and amounts to be paid as principal, mark-up, and fees. The schedule must clearly disclose the Annualized Percentage Rate (APR).
- ii. Be drawn up in English and Urdu or any other regional language considered to be appropriate in view of clients' ability to understand.
- iii. Be displayed at a prominent place such as the entrances or windows of branches.
- iv. Include details of potential factors that may induce changes in fees and service charges.
- v. Be read-out, copied and provided to customers after they are signed.
- vi. Not be discriminatory on the basis of gender.

In addition, MFBs shall regularly disclose the expected APR on deposits to their customers.

C. Complaint Redressal Cell

Each MFB shall establish a customer complaint cell with effective internal processes for logging, acknowledging, assessing, and taking timely action in response to complaints received from customers. While defining the scope and activities of the cell, the MFB shall give due consideration to factors such as the complexity of its business, its range of products, the nature and size of its operations, the profile of its customers, and so forth.

MFBs shall define timelines for the resolution of complaints. Moreover, management shall make a quarterly review of the complaints processed (outstanding and settled) by the cell. If a complaint remains unresolved beyond the standard time, the MFB shall periodically report to its CEO about the nature of the unresolved complaint along with reasons for the delay. Furthermore, MFBs shall identify complaints of a recurring nature for immediate corrective action.

To facilitate the customers in lodging complaints, MFBs shall place a complaint box in each branch that is located at place which is easily identifiable and accessible to all customers, e.g. on a main customer service counter.

D. Collection Practices

Each MFB shall develop a code for debt collection practices duly approved by its BoD. The code shall be inclusive of at least the following:

- i. Customers must be pre-informed in writing about the consequences of non-repayment including legal remedies available to the MFB.
- ii. Only lawful and acceptable business language and professional attitude should be adopted in establishing contact with clients.
- iii. MFBs should not harass customers' family members. However, necessary information could be obtained from family, friends, or third parties if the customer is not in contact.

Regulation 0 – 5: Submission of Quarterly Returns

The MFBs shall submit their quarterly data online on prescribed Quarterly Data File Structure (DFS) under Reporting Chart of Accounts (RCOA) through Data Acquisition (DAP) Portal maintained at State Bank of Pakistan as per laid down instructions.

Regulation 0 – 6: Window Dressing

MFBs shall refrain from adopting any measures or practices whereby they would either artificially or temporarily show an ostensibly different position of MFBs' accounts as given in their financial statements. Particular care shall be taken in disclosing their deposits, minimum capital requirement, non-performing loans/assets, provisioning, profit, inter-branch and inter-bank accounts, etc.

Regulation 0 – 7: Permission Regarding Receipt of Grants

MFBs shall ensure obtaining prior permission from SBP before receiving any type of grants. Any such requests and /or clarifications shall be addressed to Director, Agricultural Credit and Microfinance Department, State Bank of Pakistan, Karachi.

Regulation O – 8: Reporting to Credit Information Bureau (CIB)

MFBs shall:

- i. Provide factual and accurate data to SBP on the format prescribed from time to time. The said data /information shall be submitted to SBP on a monthly basis but not later than 10th of every month following the month to which the CIB data relates.
- ii. Sign an agreement with SBP on the prescribed format, in order to avail online facility to obtain credit worthiness reports, the specimen of which can be obtained from concerned SBP department, MFBs shall be required to. The applicant MFB will be connected online after signing of the agreement and payment of prescribed joining fee to SBP. After completion of above formalities, SBP shall inter alia provide necessary guidelines, software, user IDs for authorized persons to the MFBs. The State Bank does not entertain manual requests for issuance of credit reports.
- iii. Submit CIB data of their borrowers on the prescribed formats online through their authorized persons.
- iv. Invariably report in writing to CIB the subsequent clearance of overdues/defaults within three working days from the date of such repayment/settlement.
- v. Reflect the detail of re-payment/settlement of overdues/defaults made subsequent to the reporting date in the CIB report by way of following notes in the remarks column of the CIB report on the basis of a written letter from the concerned MFB confirming that the overdues/defaults amount has been cleared by the borrower on a specific date: “The “MFB’s Name” has subsequently reported clearance of overdues/defaults of Rs. on (date).”
- vi. Share their customers’ data with private CIB(s) subject to development of comprehensive customer protection and confidentiality guidelines duly approved by their Board of Directors. Further, express customer consent is mandatory for sharing customer data with other institutions/ CIB and the duty of maintaining confidentiality will remain with the Microfinance Bank.

ANNEXURES

Instructions on Calculation of Capital Adequacy Ratio (CAR)

1. Requirements as to calculation of CAR:

- 1.1. MFBs shall categorize their capital as Core Capital and Supplementary Capital. The components of core & supplementary capital and the risk weights are provided in the annexed Table A and B respectively.
- 1.2. The inclusion of supplementary capital for calculating Capital Adequacy Ratio shall be limited to 50% of the Core Capital.

2. Computation of Supplementary Capital

- 2.1. General Provisions or General Reserves for loan losses shall include only such provisions which are not created against identified losses and are as such freely available to meet unidentified losses. These provisions or reserves will be limited to maximum of 1.25% of total Risk Weighted Assets.
- 2.2. Revaluation Reserves shall be the Reserves created by revaluation of fixed assets and equity instruments held by the MFB. The assets and investments must be prudently valued fully taking into account the possibility of price fluctuations and forced sale. Revaluation reserves reflecting the difference between the book value and the market value will be eligible up to 50% for treatment under Supplementary Capital subject to the condition that the reasonableness of the revalued amount is duly certified by the external auditors of the MFB.
- 2.3. Sub-ordinate debt shall qualify for inclusion in the Supplementary Capital after obtaining prior written approval from the SBP. Such approval will be granted by SBP on case to case basis subject to fulfillment of the following conditions:
 - a) Sub-ordinate debt can be raised from any person or entity, preferably from the sponsors, in local currency only.
 - b) Rate of profit will be decided by the MFBs, subject to SBP's clearance.
 - c) The loan should be un-secured, plain vanilla and sub-ordinate as to payment of principal and profit to all other indebtedness of the MFB including deposits.
 - d) The loan should have original fixed term to maturity of minimum 5 years. The loan should not be repayable before the agreed repayment date without approval of the SBP. Neither the interest nor the principal may be paid even at maturity if such payments mean that the MFB falls below or remain below the capital adequacy ratio.
 - e) Any other restrictions imposed by the State Bank of Pakistan.

MICROFINANCE BANK

CAPITAL ADEQUACY RATIO AS ON XX.XX.XXXX

Table-A

Sr. No.	ITEMS	AMOUNT
1	<u>Core Capital</u>	
	1.1 Fully Paid-up Capital	xxx
	1.2 Balance in Share Premium Account	xxx
	1.3 Reserve for Bonus Shares	xxx
	1.4 General Reserves	xxx
	1.5 Un-appropriated Profit/(Loss)	xxx
	1.6 Sub-Total (1.1 to 1.5)	xxxxxx
	Less:	
	1.7 Intangible Assets	xxx
	1.8 Shortfall in Provision required against Classified Assets.	xxx
	1.9 Sub-Total (1.7 to 1.8)	(xxxx)
	1.10 Eligible Core Capital (1.6-1.9)	
2	<u>Supplementary Capital</u>	
	2.1 Freely available General Provisions or reserves for loan losses – up-to maximum of 1.25% of Risk Weighted Assets	
	2.2 Revaluation reserves – eligible up-to 50%	
	2.3 Sub-ordinated debt (up-to 50% of core capital)	
	2.4 Sub-Total (2.1 to 2.3)	
3	Total Capital (1.10 + 2.4)	
4	<u>Capital Adequacy Ratio</u>	
	4.1 Risk Weighted Assets (as per Table B)	xxxx
	4.2 Minimum Capital Requirement (15% of Total Risk Weighted Assets as per item 4.1)	xxx
	4.3 Total Capital Held (As At Item 3 Above)	xxx
	4.4 Capital Surplus/(Shortfall) – (4.3 - 4.2)	xxx
	4.5 Capital Adequacy Ratio (4.3 / 4.1x 100)	xxx

RISK-WEIGHTED ASSETS ON-BALANCE SHEET ITEMS

Table-B

S.No.	ITEMS	BOOK VALUE	RISK WEIGHT%	ADJUSTED VALUE
1	Cash		0%	
2	Balances with Central Banks:			
	2.1 With State Bank of Pakistan		0%	
3	Balances with Banks			
	3.1 With Scheduled Banks in Pakistan		20%	
4	Investments in:			
	4.1 Treasury Bills		0%	
	4.2 Federal / Pakistan Investment Bonds		0%	
	4.3 Other securities of Federal Government		0%	
	4.4 Marketable Securities (TFCs / Mutual Funds)		100%	
	4.5 Other Investments (TDRs of Banks/MFBs)		20%	
5	Loans & Advances			
	(Less Cash margin and Govt. Securities held)			
	5.1 Loans guaranteed by Federal Govt./ SBP		0%	
	5.2 Microcredit		100%	
	5.3 Loans fully secured by mortgage of residential or commercial property		50%	
	5.4 Staff loans		0%	
6	Fixed Assets (net of accumulated depreciation)		100%	
7	Assets deducted from capital:			
	7.1 Intangible assets		0%	
	7.2 Unconsolidated investment in subsidiary companies engaged in micro financing activities		0%	
8	Other Assets			
	8.1 Advance tax		0%	
	8.2 Deposits & prepayments		100%	
	8.3 Accrued income on Advances		100%	
	8.4 Accrued income on deposits accounts		100%	
	8.5 Accrued income on investments - PIBs/T-Bills		0%	
	8.6 Accrued income on investments – Others		100%	
	8.7 Other receivable		100%	
	TOTAL			

Annexure - B

MICROFINANCE BANK

*Bi-Weekly Statement of Affairs as at Close of Business on -----

Rupees in '000

LIABILITIES:

AMOUNT

1) Demand Liabilities

a) Deposits (General)	XXXX	
b) Deposits From Banks & Financial Institutions	XXXX	
c) Borrowings From Banks And Financial Institutions (Other Than Call Money)	XXXX	
d) Other Demand Liabilities	<u>XXXX</u>	XXXX

2) Time Liabilities

a) Deposits (General)	XXXX	
b) Deposits From Banks And Financial Institutions	XXXX	
c) Borrowings From Banks And Financial Institutions	XXXX	
d) Other Time Liabilities	XXXX	XXXX

3) Borrowings From The State Bank Of Pakistan

a) Against Promissory Notes	XXXX	
b) Against Approved Securities	XXXX	
c) Other Borrowings	XXXX	XXXX

4) Money At Call And Short Notice

XXXX

5) Borrowing from Banks Abroad

XXXX

6) Borrowings From Government of Pakistan

XXXX

7) Capital (Paid Up)/Capital Fund And Reserves

XXXX

8) Other Liabilities (Excluding Contra Items)

XXXX

Xxxx

9) Total Liabilities

XXXX

Assets:

1) Cash

XXXX

2) Balance With

a) State Bank of Pakistan

XXXX

b) National Bank Of Pakistan

XXXX

c) Other Financial Institutions

XXXX

XXXX

3) Money At Call And Short Notice

XXXX

4) Advances

XXXX

5) Bills Purchased And Discounted		XXXX
6) Investment In Securities And Shares		XXXX
a. PIBs	XXXX	
b. T-Bills	XXXX	
c. Other Approved Securities	XXXX	
d. Shares	XXXX	
e. Others (Specify)	<u>XXXX</u>	
7) Other Assets (Excluding Contra Items)		XXXX
8) Total Assets		<u>XXXX</u>

Note: The Unencumbered approved securities held for liquidity purposes were:

a. PIBs	XXXX
b. TBs	XXXX
c. Others (specify)	<u>XXXX</u>
d. Total	<u>XXXX</u>

Authorized Signature
Name and Designation

* To be prepared once in every two weeks as at close of business on alternate Friday/Saturdays (close of week)

Annexure – B - 1

Bi-weekly (Fortnightly) Statement of Cash Reserve Requirement(CRR)

as at Close of Business on -----

Rs. In '000'

1. Demand Deposits, and Time Deposits of Less than One Year	<u>Amount</u>
1.1 All current deposits including customers, banks and other financial institutions	xxx
1.2 All savings deposits including customers, banks and other financial institutions	xxx
1.3 Special notice/call deposits including customers, banks and other financial institutions	xxx
1.4 Fixed deposits including customers, banks and other financial institutions with tenor of less than one year	xxx
1.5 Overdue fixed deposits including those of customers, banks, other financial institutions	xxx
1.6 All other deposits payable to public on demand	xxx
1.7 Mark- up/ Interest accrued on all above accounts	xxx
2. Total Deposits (1.1 to 1.7)	xxxx
3. Required CRR (5% of Total Deposits as per item # 2)	xxx
4. Actual Cash Reserve as of -----	xxx
5. Surplus / (Deficit)	xxx

Annexure – B - 2

Bi-weekly (Fortnightly) Statement of Statutory Liquidity Requirement (SLR)

as at Close of Business on -----

Rs. In '000'

1. Demand Liabilities, and Time Liabilities of Less than One Year	<u>Amount</u>
1.1 All current deposits including customers, banks and other financial institutions	xxx
1.2 All savings deposits including customers, banks and other financial institutions	xxx
1.3 Special notice/call deposits including customers, banks and other financial institutions	xxx
1.4 Fixed deposits including customers, banks and other financial institutions with tenor of less than one year	xxx
1.5 Overdue fixed deposits including those of customers, banks, other financial institutions	xxx
1.7 All other deposits payable to public on demand	xxx
1.8 All loans and borrowings with tenor of less than one year (except money at call & short notice, other interbank borrowings, and the loans exempted under section 18 of the Microfinance Institutions Ordinance, 2001)	xxx
1.9 Mark- up/ Interest accrued on all above accounts	xxx
1.10' Other Liabilities:	
i Unclaimed dividend/dividend payable	xxx
ii Sundry deposit accounts	xxx
iii Bills payable	xxx
iv Any other miscellaneous liabilities payable on demand	xxx
Sub Total (i to iv)	xxx
2. Total Liabilities (1.1 to 1.10)	xxxx
3. Required SLR (10% of total liabilities as per item # 2)	xxx
4. Actual Liquidity Reserve as of ----	xxx
5. Surplus / (Deficit)	xxx

UNDERTAKING

I ----- S/O, D/O, W/O ----- holder of CNIC -----, undertake that the detail of my existing exposure from the "Entire Banking & Microfinance Sector" as on----- is as under:

Details of Loans:

Sr. #	Name of the MFB/MFI/Bank /other financial Institutions	Type of Loan	Outstanding Amount
Total Exposure			

Signature: _____

Name of Applicant: _____

CNIC # _____

Date: _____

Fit & Proper Criteria for Members of Board of Directors, President / Chief Executive Officer and other Key Executives of Microfinance Banks (MFBs)

The competence of the Board Members and President/CEO is critically important for success of any corporate entity generally and financial institutions, being highly leveraged outfits, particularly. The Board Members and the President/CEO of banks and financial institutions are custodians of not only the shareholders' money but also the public funds placed with them as deposits. The Microfinance Banks are formal financial institutions eligible to extend a variety of financial services to the poor including savings and deposits. The MFBs' Board Members and the President/CEO should therefore, be persons of established integrity and track record and have the necessary capacity, experience and exposure to manage the bank and public funds. The following criteria has therefore, been developed for MFBs' Board Members and the President/CEO to ensure that the skill mix of the Board is compatible with the mission, vision and objectives of the MFBs and that the President/CEO has requisite background/expertise and relevant experience to run and manage the MFBs:

1. Integrity, Honesty and Reputation

The MFBs while selecting/recommending a person as Board Member shall ensure that he/she:

- i) Has not been convicted of any criminal offence, involved in any fraud/forgery, financial crime etc.
- ii) Has not been associated with any illegal activity especially relating to banking business.
- iii) Has not been in default of payment of dues owed to any financial institution and / or default in payment of any taxes in an individual capacity or as Proprietor of a firm, Partner in a partnership firm, Director, President or Chief Executive in any private or public limited company which has defaulted in payment of its dues to financial institutions/tax authorities.
- iv) Has not been subject to any adverse findings or any settlement in civil/criminal proceedings particularly with regard to investments, financial/business misconduct, fraud, formation or management of a corporate body etc.
- v) Has not contravened any of the requirements and standards of regulatory system or the equivalent standards or requirements of other regulatory authorities.
- vi) Has not been involved with a company/firm whose registration/license has been revoked or cancelled or that has gone into liquidation.
- vii) Has not been debarred from being the Chief Executive, Chairman or Director of a company.

2. Experience & Qualification

This section shall apply separately for President/Chief Executive and Directors:

2.1. For President / Chief Executive of MFBs:

The President/Chief Executive shall be a person having at least 10 years experience as a senior micro-finance practitioner or as a senior banker, preferably below 55 years of age at the time of his appointment. The minimum qualification for President/Chief Executive shall be graduation. MFBs, however, are encouraged to engage persons having professional and advanced qualifications in banking, finance, economics, information technology etc.

2.2. For members of Board of Directors of MFBs:

While selecting/recommending the Board Members, the MFBs shall ensure that their Board Members have necessary competence, qualification and experience to effectively undertake their responsibilities as Board Members. The Boards shall comprise of persons having extensive experience in Microfinance, Banking & Finance, Micro and Small Enterprises, Social Intermediation, Poverty Alleviation, Information Technology etc. The appropriate skill mix may include:

- a. Microfinance Practitioner(s) having at least 5 years experience in managing and administering microfinance/ micro credit programs, social intermediation, women empowerment programs etc. and; or
- b. Senior banker(s) having at least 5 years experience at senior level in credit, operations, audit, treasury etc and; or
- c. Finance professional(s)/Business/Management Consultant(s) having at least 5 years post qualification experience with reputed audit/business consulting firms etc. or
- d. Development economist(s) having at least 5 years experience as an economist / program / project officer in reputed national or international firms etc. and has managed/coordinated different poverty alleviation programs/projects/research assignments and; or
- e. Lawyer(s) with at least 10 years experience as an advocate in High Court or Supreme Court. He/She shall not be associated with any microfinance bank as legal counsel/adviser or on the payroll of a microfinance bank and; or
- f. IT Professional(s) having at least 5 years experience with a reputed IT firm and /or experience of developing/administering/managing IT systems in banks/microfinance banks/other financial institutions and; or
- g. Micro/small entrepreneur(s) having at least 10 years experience of successfully managing an enterprise.

The above list, however, is not exhaustive and persons from other professions and fields, business and industrial concerns, academia etc. may also be on MFB Board provided the overall skill mix of the Board remains compatible with the objectives and functions of the MFB.

The minimum qualification for Board Members shall preferably be graduation or equivalent. However, for persons having extensive and successful experience in microfinance, poverty alleviation, social

mobilization and development, women development, micro entrepreneur, business and industrial concerns etc. the minimum qualification limit may be relaxed.

3. Track Record

- i) The person selected must have an impeccable track record in the companies he/she has served either in the capacity of an employee or Director/Chief Executive or as Chairman
- ii) Has not been terminated or dismissed in the capacity of employee or Director/Chairman of a company.

4. Conflict of Interest

- i) The Directors on the MFBs' Board shall not be Director of any other Microfinance Bank. He/She shall also not act as consultant, adviser or an employee of any other MFB.
- ii) He/She shall avoid conflict of interest in his/her activities with, and commitments to, other organizations.

5. Others

No member/office bearer of any political party or member of Senate, National/Provincial assembly/assemblies, and local bodies shall be appointed / recommended for appointment as Member of Board of Director and/or President/Chief Executive Officer of MFBs.

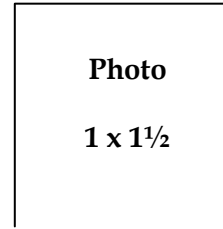
6. Prior Clearance

The MFBs shall submit information about the Board Members and/or President/Chief Executive Officer to State Bank, as per the proforma enclosed as Annexure - C, C-1 and C-2, for clearance before selection/appointment or re-appointment/renewal of term of Directors and President/Chief Executive Officer.

The appointment of other key executives will not require prior clearance of SBP. However, the MFBs while appointing key executives must themselves ensure that the incumbent(s) qualify on the basis of (i) Integrity, Honesty & Reputation, and (ii) Track record as laid down in Fit & Proper Test criteria of these regulations for President/CEO and Board Members in letter and spirit. The information on appointment of key executive is required to be forwarded to SBP on prescribed format at Annexure – C-3 within seven days of assumption of the charge of the post by the incumbent. The information submitted may be checked during inspection by Onsite Inspection Department of SBP.

Annexure - E

PROFORMA - FITNESS & PROPRIETARY OF CEO & BOARD MEMBERS



1. Full Name _____

2. If you have changed your name, state previous name and reasons for change _____

3. Parents and Spouse's Names

Father's Name: _____

Mother's Name: _____

Spouse's Name: _____

4. Date & Place of Birth: _____

5. Religion: _____

6. N.I.C. Number-Old: _____

C.N.I.C Number-New: _____

Passport Number: _____

7. N.T.N.: _____

8. Education: _____

9. Relationship with other Sponsor Directors: _____

10. Status of Directorship (shareholder or nominee): _____

11. Subscribed Amount: _____

12. Personal Net Worth (Certified copy of Wealth Statement may be enclosed): _____

13. Occupation / Profession / Trade: _____

14. Present Designation, Department and official Address

15. Telephone Numbers: Res. _____ Off: _____ Mobile: _____

16. Appointments held during the last five years (with dates): _____

17. List of Companies / firms and their bankers in which sponsor directors and their family members viz. spouses, children and parents serve(d) as directors, chief executive, partner, proprietor or major shareholders holding 5% or more shares as per following format:

Name of the Sponsors Director and his / her family Members	Occupation/ Profession/ Trade	National Tax Number	NIC & Passport Number	Name of Associated Company / Firm position held & % of Shareholding	Name of the Financial Institution along with the name of the branch (account number) with which firms / companies (as per column 5) have dealings with:
1	2	3	4	5	6

National Tax Number of the Corporate Bodies	Nature of Business	Asset Base as reflected in the latest Audited Accounts of the Corporate Bodies	Dividend declared in the immediately preceding three years
7	8	9	10

18. Declaration certificate pronouncing integrity, honesty, reputation and track record of the director as per guidelines given in Annexure –B

19. Present Residential Address:

20. Permanent Residential Address:

21. Names & Addresses of three respectable persons (not relatives) who have been closely acquainted with you during last five years: _____

Signature

QUESTIONNAIRE FOR ASSESSING “FIT & PROPER TEST”

Please answer the following questions by entering a tick (✓) in the appropriate box. If answer of any of these questions is in YES and need explanation, use a separate sheet with proper reference to the question.

	Yes	No
1. Have you ever been convicted/ involved in any fraud/forgery, financial crime etc, in Pakistan or elsewhere, or are being subject to any pending proceedings leading to any conviction?	<input type="checkbox"/>	<input type="checkbox"/>
2. Have you ever been associated with any illegal activity concerning banking business, deposit taking, financial dealing and other business?	<input type="checkbox"/>	<input type="checkbox"/>
3. Have you ever been subject to any adverse findings or any settlement in civil/criminal proceedings particularly with regard to investments, financial/business, misconduct, fraud, formation or management of a corporate body etc by SBP, other regulators, professional bodies or government bodies/agencies?	<input type="checkbox"/>	<input type="checkbox"/>
4. Have you ever contravened any of the requirements and standards of regulatory system or the equivalent standards or requirements of other regulatory authorities?	<input type="checkbox"/>	<input type="checkbox"/>
5. Have you ever been involved with a company or firm or other organization that has been refused registration/license to carry out trade, business etc?	<input type="checkbox"/>	<input type="checkbox"/>
6. Have you ever been involved with a company/firm whose registration/license has been revoked or cancelled or gone into liquidation or other similar proceedings?	<input type="checkbox"/>	<input type="checkbox"/>
7. Have you ever been debarred for being Chief Executive, Chairman, Director or Sponsor shareholder of a company, especially financial institutions?	<input type="checkbox"/>	<input type="checkbox"/>
8. Have you ever been dismissed/ asked to resign/resigned in Pakistan or elsewhere in order to avoid legal or disciplinary action?	<input type="checkbox"/>	<input type="checkbox"/>
9. Have you ever resigned from a professional or regulatory body in Pakistan or elsewhere in order to avoid legal or disciplinary action?	<input type="checkbox"/>	<input type="checkbox"/>
10. Have you ever been disqualified/ removed by regulators/Government bodies/ agencies?	<input type="checkbox"/>	<input type="checkbox"/>
11. Have you ever been in default of payment of dues owed to any financial institution in individual capacity or as proprietary concern or any partnership firm or in any private unlisted/listed company?	<input type="checkbox"/>	<input type="checkbox"/>
12. Have you ever been in default of taxes in individual capacity or as proprietary concern or any partnership firm or in any private listed/unlisted company?	<input type="checkbox"/>	<input type="checkbox"/>

- | | | |
|---|--------------------------|--------------------------|
| 13. Have you ever been associated as director and/or chief executive with the corporate bodies whose corporate and tax record, including custom duties, central excise and sales tax has been unsatisfactory? | <input type="checkbox"/> | <input type="checkbox"/> |
| 14. Have you entered into any agreement with any other person (natural or legal) which will influence the way in which you exercise your voting rights or the way in which you otherwise behave in your relationship with the authorized entity? | <input type="checkbox"/> | <input type="checkbox"/> |
| 15. Are you a director on the Board of Directors of any other Financial Institution(s)/MFB (or its parent MFI, if any)? | <input type="checkbox"/> | <input type="checkbox"/> |
| 16. Are you a Chairman, Chief Executive, Chief Financial Officer, Chief Internal Auditor, Research Analyst or Trader (by whatever name/designation called) of an Exchange Company (firm or sole proprietorship), member of a Stock Exchange, Corporate Brokerage House? | <input type="checkbox"/> | <input type="checkbox"/> |
| 17. Are you owning/controlling any Exchange Company or Corporate Entity? | <input type="checkbox"/> | <input type="checkbox"/> |
| 18. Have you been or are you working as consultant or adviser of the MFB (or its parent MFI, if any) in which you intend to become a director? | <input type="checkbox"/> | <input type="checkbox"/> |
| 19. Are you employee of the MFB (or its parent MFI, if any)? | <input type="checkbox"/> | <input type="checkbox"/> |
| 20. Are you employee of a company/entity/organization where sponsor shareholders of the MFB have substantial interest? | <input type="checkbox"/> | <input type="checkbox"/> |
| 21. Are you a member/office bearer of any political party or member of Senate/National/Provincial Assembly/Local Body? | <input type="checkbox"/> | <input type="checkbox"/> |
| 22. If independent director, have you enclosed declaration in this behalf? | <input type="checkbox"/> | <input type="checkbox"/> |
| 23. Any other information that is relevant for the purpose of SBP and needs to be mentioned? | <input type="checkbox"/> | <input type="checkbox"/> |

Signature _____

Name _____

Position _____

Date _____

AFFIDAVIT

(On Non-Judicial Stamp Paper)

I, _____ son/daughter/wife of _____ adult, resident of _____ and holding CNIC/Passport No. _____ do hereby state on solemn affirmation as under:-

- a. that the deponent hereby confirm that the statement made and the information supplied in the attached questionnaire and the Annexure-C1 and the answers thereof are correct and that there are no other facts that are relevant for “Fit and Proper Test”
- b. that the deponent undertake that the State Bank of Pakistan may seek additional information from any third party it deems necessary in view of assessing “Fit and Proper Test”
- c. that the deponent undertake to bring to the attention of the State Bank of Pakistan any matter which may potentially affect my status as being someone fit and proper as and when it arise; and
- d. that whatever is stated above is correct to the best of my knowledge and belief and nothing has been concealed therefrom.

DEPONENT

The Deponent is identified by me

Signature _____

ADVOCATE

(Name and Seal)

Solemnly affirmed before me on this _____ day of _____ at _____ by the Deponent above named who is identified to me by _____, Advocate, who is known to me personally.

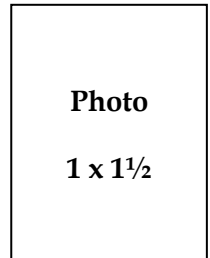
Signature _____

OATH COMMISSIONER FOR TAKING AFFIDAVIT

(Name and Seal)

Annexure – E - 3

PROFORMA – FITNESS & PROPRIETARY OF KEY EXECUTIVES



Position and Grade held by the Executive		
Date of assumption of current position (dd/mm/yyyy)		
Full Name		
Father's Name		
Date of Birth	Place of Birth (City and Country)	
Nationality (ies)	NTN Number	
C.N.I.C. No	N.I.C. No (Old)	
Passport No.		
Telephone Number(s)	Mobile Number	
Academic Qualification		
Qualification	Name & Address of Degree Awarding Institution	Date of Completion
Professional Qualification		
Qualification	Name & Address of Degree Awarding Institution	Date of Completion
Training(s); if any		
Previous Employment(s) (date-wise)		
Designation	Department	
Official Address		
Telephone Number (s)		
Has ever been convicted of any offence?	Yes	No
If yes, nature of offence and penalty imposed		
Has ever been censured or penalized by any financial regulator (local or foreign)?	Yes	No
If yes, reasons for adverse findings and amount of penalty imposed (if any)		
Has ever been dismissed from employment?	Yes	No
If yes, name of the employer and reason for dismissal		

(Signature of the concerned official)

(Signature and Stamp of Employer)

Guidelines on Internal Control and Risk Management

MFBs are exposed to several types and degree of risks depending on factors such as their size, complexity of business activities, scale etc. Like other financial institutions, MFBs face credit, market, liquidity, operational, compliance / legal /regulatory and reputational risks. To strengthen MFBs and increase their resilience to resist financial and economic shocks, they shall ensure to have in place appropriate mechanisms/frameworks for Business Continuity Management, Internal control, Risk Management and IT Security which commensurate with their needs.

A – INTERNAL CONTROLS

These Guidelines on Internal Controls provide a minimum set of best practices for establishing and implementing effective internal controls in Microfinance Banks (MFBs).

Internal Control refers to policies, plans and processes which are approved by the board and performed on continuous basis by the senior management and all levels of employees within the MFB. Internal controls are used to provide reasonable assurance regarding the achievement of organizational objectives. Effective and well-designed operations are prone to risk and even well trained personnel with the best of intentions can become distracted and negligent. MFBs shall therefore design and review their internal control policies and procedures taking into account the following;

- MFBs shall have in place an effective internal control system, duly approved by their board, clearly laying out the control environment and structure, recognizing risks and assessment, control activities, accounting, information & communication, and self-assessment or monitoring and correcting deficiencies.
- MFBs shall ensure implementation of internal controls mechanism and its integration into daily operations.
- MFBs shall ensure effective communication of their internal control processes and system among their employees.
- Monitoring of key risks should be part of the daily activities of the MFBs as well as periodic evaluations by the business lines and internal audit.
- MFBs shall conduct an effective and comprehensive internal audit of the internal control system.

The following ‘Controls Principles’ need to be applied by all MFBs, irrespective of size, nature and complexity of their business, while developing framework of internal controls;

- Regular feature: Control activities should be an integral part of the daily activities of a MFB in such a manner that it becomes ingrained in their ongoing processes rather than a year-end “fire drill” to satisfy documentation requests from auditors and supervisors.

- Separation of Duties: Duties should be divided so that no one person has complete control over a key function or activity.
- Authorization and Approval: All transactions should be authorized before recording and execution.
- Custodial and Security Arrangements: Responsibility for custody of assets needs to be separated from the related record keeping.
- Review and Reconciliation: Records should be examined and reconciled to regularly determine that transactions are properly processed, approved and booked.
- Physical Controls: Equipment, inventories, cash and other assets should be secured physically, counted periodically and compared with amounts shown on control records.
- Training and Supervision: Qualified, well-trained and supervised employees always help ensure that control processes function properly.
- Documentation: Documented policies and procedures promote employee understanding of duties and help ensure continuity during employee absences or turnover. Therefore, policies and procedures (in the form of operations manuals and desk instructions) should exist in all MFBs.
- Communication of importance of Internal Controls: Setting standards of professional integrity and work ethics and ensuring that all levels of personnel in their organization know the importance of internal controls and understand their role in the internal controls process and be fully engaged in the process.
- Cost/Benefit: It is for the MFBs to assess that the costs associated with control processes commensurate with the expected benefits.

B – RISK MANAGEMENT

These Guidelines on Risk Management provide a minimum set of best practices for establishing and implementing effective risk management in Microfinance Banks (MFBs). MFBs, like other financial institutions, are exposed to a spectrum of risks, which include credit risk, interest rate risk, liquidity risk, operational risk, and legal and reputation risk. Managing these risks is essential for their survival and sustainability. In this regard, MFBs shall design and review their risk management policies and procedures in light of the following:

- The MFBs shall prepare a comprehensive Risk Management and Reporting Framework (RMRF) covering all of their business activities and circumstances under which they operate and have flexibility to accommodate any changes thereof. The RMRF shall be duly approved by the Board.
- The RMRF shall outline role and responsibilities of board and senior management to identify, measure, monitor report and control relevant categories of risks especially credit, market, liquidity, operational and reputational risks.
- The MFBs shall ensure establishing clear lines of authority and responsibility for managing responsibilities for dissemination, implementation and compliance of the approved policies and procedures.
- The MFBs shall develop a system for testing and analyzing their aggregate loan portfolio on continuous basis. The MFBs in particular shall have in place mechanism to identify and correct portfolio concentration in geographies, products, economic segments, branches, and loan officers. The MFBs shall also record the risks identified through the portfolio testing and related corrective actions, and report these to their senior management.
- The BOD shall review the effectiveness of the risk management activities periodically and make appropriate changes as and when necessary. The risk review function shall be independent of those who approve and take risk. The review may use stress tests exposing the portfolio to unanticipated movements in key variables or major systemic shocks.
- The MFBs shall have in place an Asset-Liability Management Committee (ALCO) to undertake following responsibilities;
 - Oversee the structure /composition of MFB's assets and liabilities and decide about product pricing for deposits and advances.
 - Decide on required maturity profile and mix of incremental assets and liabilities.
 - Articulate interest rate view of the bank and deciding on the future business strategy.
 - Review and articulate funding policy.
 - Discuss strategies and risks in obtaining debt/loans from local and foreign lenders.

C – BUSINESS CONTINUITY MANAGEMENT (BCM)

These Guidelines on Business Continuity Management (BCM) provide a minimum set of best practices for establishing a holistic management process to identify and respond to potential events regarding operating disruptions that threatens MFBs. The quick recovery of business, after major operational disruption, is crucial in maintaining confidence in MFBs and protecting the interest of key stakeholders.

MFBs shall therefore take following actions:

- MFBs shall have in place a comprehensive plan, for BCM, duly approved by their board to ensure its ability to operate as going concerns and minimize losses in the event of severe business disruptions.
- The BCM plan shall clearly define/segregate responsibilities of board and senior management, identify critical staff and senior management, critical and time sensitive functions, location & suitability of operations back-up site and availability of necessary facilities, accessibility/movement plan, and critical documents / data.
- The MFBs shall allocate sufficient resources and knowledgeable personnel to accomplish the tasks contained in its BCM plan. MFBs shall provide training sessions and awareness programs for their staff to familiarize them with their roles, accountabilities, responsibilities and authority in response to a disruptive event.
- The MFBs shall carry out a thorough business impact analysis identifying the potential impact of uncontrolled, non-specific events on MFBs' business processes and their customers; consideration of all departments and business functions, not just data processing; and estimation of maximum allowable downtime and acceptable levels of data, operations, and financial losses.
- The MFBs shall carry out an assessment of potential business disruptions and critical business lines based upon severity and likelihood of occurrence in order of priority; a gap analysis comparing the MFBs' existing BCM, if any, to what is necessary to achieve recovery time and point objectives; an analysis of threats based upon their impact on MFBs and their customers and recovery time targets.
- The MFBs shall conduct an independent audit of their BCM plan.
- The MFBs shall make arrangements for review of their BCM plan, and are encouraged to conduct mock exercises on periodic basis.

D – INFORMATION TECHNOLOGY (IT) EFFECTIVENESS/SECURITY

These Guidelines on IT security provide a minimum set of best practices for establishing and implementing effective IT security in Microfinance Banks (MFBs). MFBs shall design and review their IT security policies and procedures in light of the following:

- The MFBs shall prepare a comprehensive IT policy, duly approved by the Board. It shall entail the process for reviewing current and future IT needs in terms of resources (hardware, software and technical expertise), ensuring effective use of existing IT resources, identifying IT related risks and adopting strategies to cope with these risks.
- The MFBs shall put in place a **Disaster Recovery Plan and maintain a disaster recovery site**. Disaster recovery planning shall ensure availability of resources and required technological support to businesses in an event of disaster. The plan must then be maintained, tested and audited by auditors to ensure that it remains appropriate to the needs of the MFB.
- The MFBs shall maintain a team of experienced technical and business human resources with a thorough understanding of IT Security issues. The team would streamline the IT security related process and procedures, including incident response and management and should report to the senior management / BoDs.
- The MFBs shall perform IT risk assessment on periodic basis to determine physical, environmental, administrative, and technical vulnerability as well as the potential threats (and their consequences). Risk re-assessment should be a continuing process.
- The MFBs shall conduct regular workshops/ training programs to create users' awareness.
- The MFBs shall have in place a dashboard utility for accessing information frequently required by auditors / SBP inspectors during their engagement. The requisite information includes statements of account of (GL, deposit or loan accounts), branch / bank wise affair & profit & loss, review of transactions etc.
- Those MFBs which are using alternative delivery channels (including ATMs, PoS machines, and branchless banking agents) shall opt for a third party IT security audit to ensure the adequacy of the adopted security plan and procedures and the effectiveness of the implemented controls.

DECLARATION OF FIDELITY AND SECRECY

I, **(insert name)** on becoming **(President/ Chairman of the Board/ Director on the Board/auditor/staff)** of the **(insert name of Microfinance Bank)** in terms of Section 26-A of the Microfinance Institutions Ordinance, 2001 do hereby solemnly & sincerely confirm/declare that I shall observe strict fidelity, secrecy and usage customary among bankers and all matters relating thereto and in particular shall not divulge or communicate any information relating to the affairs of its customers, which may come to my knowledge in discharging my duties directly or indirectly, except in circumstances in which it is in accordance with law, practice and usage customary among bankers.

Dated: Signature: _____ **Designation:** _____

DOCUMENTS TO BE OBTAINED FROM VARIOUS TYPES OF CUSTOMERS/ACCOUNT HOLDERS

1	Sole-proprietor	<ul style="list-style-type: none"> i). Attested copy of CNIC of the sole-proprietor ii). Declaration of Sole Proprietorship (if available, on business letter head) iii). Account opening requisition letter (if available, on business letter head)
2	Partnership	<ul style="list-style-type: none"> i). Attested copies of CNICs of all partners. ii). Attested copy of 'Partnership Deed' duly signed by all partners of the firm. iii). Attested copy of Registration Certificate with Registrar of Firms. In case the partnership is unregistered, this fact should be clearly mentioned on the Account Opening Form. iv). Authority letter, in original, in favor of the person authorized to operate on the account of the firm.
3	Joint Stock companies	<p>Certified copies of:</p> <ul style="list-style-type: none"> i). Resolution of Board of Directors for opening of account specifying the person(s) authorized to operate the company account. ii). Memorandum and Articles of Association. iii). Certificate of Incorporation. iv). Certificate of Commencement of Business. v). Attested copies of identity cards / passports of all the directors. vi). List of Directors on Form A/Form B as issued under Companies Ordinance, 1984
4	Clubs, Societies and Associations	<p>Certified copies of:</p> <ul style="list-style-type: none"> i) Certificate of Registration. ii) By-laws/Rules & Regulations. iii) Resolution of the Governing Body/Executive Committee for opening of account authorizing the person(s) to operate the account and attested copy of the identity card of the authorized person(s). iv) An undertaking signed by all the authorized persons on behalf of the institution mentioning that when any change takes place in the persons authorized to operate on the account, the banker will be informed immediately. v) MFBS should obtain copies of CNICs of all the members of Governing and Executive Bodies of DHA or ask for delegation of power to Administrator under section (7) & (8) of the Pakistan Defence Housing Authority Order, 1980 and accept copy of CNIC of

		Administrator as well as authorized signatories for the purpose of opening accounts of DHA or similar other authorities subject to the condition that all other requirements laid down under relevant regulations shall be complied with in letter and spirit.
5	Agents Accounts	<ul style="list-style-type: none"> i). Certified copy of 'Power of Attorney'. ii). Attested copy of identity card of the agent.
6	Trust Account	<ul style="list-style-type: none"> i). Attested copies of identity cards of the persons authorized to operate the account along with their mandate as given by Resolution of the Governing Body / Executive Committee for opening of account and authorizing the said person(s) to operate the account. ii). Certified copy of 'Instrument of Trust' or Trust Deed.
7	Executors and Administrators	<ul style="list-style-type: none"> i). Attested copies of identity cards of the Executor / Administrator. ii). Certified copy of Letter of Administration or Probate.
8	NGOs/NPOs/Charities	<ul style="list-style-type: none"> i). Certified copies of: <ul style="list-style-type: none"> a. Registration documents / certificates b. By-laws / Rules & Regulations ii). Resolution of the Governing Body/Executive Committee, if it is the ultimate governing body, for opening of account and authorizing the person(s) to operate the account. iii). Attested photocopies of valid CNICs of the authorized person(s) and members of Governing Body/Executive Committee, if it is the ultimate governing body. iv). Any other documents as deemed necessary including its annual accounts/ financial statements or disclosures in any form which may help to ascertain the detail of its activities, sources and usage of funds in order to assess the risk profile of the prospective customer.
9	Minor Account	<ul style="list-style-type: none"> i). Form B, Birth Certificate or Student ID Card (as Appropriate) of the minor ii). Photocopy of identity document of the guardian of the minor.