

**SMART LENDING: CLIENT PROTECTION IN THE GROUP LENDING PROCESS:**  
**An Overview for Incorporating Client Protection Practices into  
Group Lending by Microfinance Institutions**

[www.smartcampaign.org](http://www.smartcampaign.org)



Keeping clients first  
in microfinance

## INTRODUCTION

“Smart Lending: Client Protection in the Group Lending Process”<sup>1</sup> is a tool for MFIs that want to incorporate good client protection practices into their group lending process. The tool is applicable to a wide range of credit methodologies, and can be adapted for use by MFIs employing village banking methodology, Grameen-style “group of groups” methodology, and other forms of group lending.

The group lending process is segmented into five key phases: (1) Client Recruitment & Group Preparation, (2) Evaluation, (3) Group Loan Approval, (4) Disbursement, and (5) Customer Service and Collections.

Like other Smart Tools,<sup>2</sup> this tool is structured as follows:

- The tool identifies distinct “**Service Points**” (SP’s)—points of interaction between the client and the institution. For each Service Point, the tool:
  - demonstrates how an MFI can model **good practice** in client protection in:
    - their policies, and
    - their operations; and
  - identifies which **Client Protection Principles** are affected; and

The document provides recommendations for the use of **client protection tools** that could help MFIs improve client protection practices at each service point. These recommendations are listed in the Annex. Some of these tools have already been developed by the Smart Campaign, but for those not listed on our website, we encourage you to share your tools and/or tool ideas with us ([info@smartcampaign.org](mailto:info@smartcampaign.org)).

**THE CLIENT PROTECTION PRINCIPLES** (short form listed below; for complete description, see [www.smartcampaign.org](http://www.smartcampaign.org)).

- |  |   |
|--|---|
| 1. Avoid Client Over-indebtedness      | 4. Ethical staff behavior               |
| 2. Transparent and responsible pricing | 5. Mechanisms for redress of grievances |
| 3. Appropriate collections practices   | 6. Privacy of client data               |

<sup>1</sup>Special thanks to: ACCION India, Hema Bansal, Amit Gupta, Ujjivan, Grameen Koota, Victoria White, and Leah Nedderman.

<sup>2</sup>The Smart Campaign offers a wide range of tools for improving client protection practices among MFIs, networks, and investors. Among these are: “Smart Lending: Client Protection in the Individual Loan Process;” and “Smart Savings: Client Protection in the Savings Process.” Visit [www.smartcampaign.org](http://www.smartcampaign.org) to download these tools, at no cost.

## PHASE 1. CLIENT RECRUITMENT & GROUP PREPARATION

SERVICE POINT (SP)	SP1	SP2	SP3	SP4
	<p><b>PROMOTIONS</b> Institution promotes its savings product(s) to potential clients.</p>	<p><b>PRODUCT DESCRIPTION</b> Institution provides specific product information to interested clients.</p>	<p><b>GROUP FORMATION</b> Clients are instructed to form groups and given guidance for good selection.</p>	<p><b>TRAINING</b> Institution ensures groups have full information needed to succeed with loan product.</p>
<p><b>GOOD CLIENT PROTECTION POLICIES</b></p>	<ul style="list-style-type: none"> <li>• Institution publicly discloses product terms, conditions, fees, and interest rates.</li> <li>• Institution complies with all local legal requirements for marketing of financial services.</li> <li>• Staff incentives balance portfolio growth with portfolio quality to discourage recruitment of over-indebted clients.</li> <li>• Staff book of rules defines acceptable client recruitment policies, incl. whether staff may recruit clients from other institutions.</li> <li>• Internal audit checks staff interactions with clients for ethical behavior and compliance with client recruitment policies.</li> </ul>			
<p><b>GOOD CLIENT PROTECTION PRACTICES</b></p>	<p><b>Clear communication with clients always includes:</b></p> <ul style="list-style-type: none"> <li>• Use of local language(s)</li> <li>• Plain terminology</li> <li>• Verbal explanation for illiterate clients</li> </ul> <p><b>For marketing materials specifically:</b></p> <ul style="list-style-type: none"> <li>• Do not oversell benefits of credit.</li> <li>• Marketing materials should include: <ul style="list-style-type: none"> <li>• Basic eligibility requirements for taking a loan;</li> <li>• Contact information for the institution; and</li> <li>• Instructions for registering a complaint or question.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Follow guidelines on clear communication—see <b>SP #1</b>.</li> <li>• Describe all costs associated with the product(s): price—including total cost of the loan--the interest rate, and all associated fees.</li> <li>• Describe all loan terms and conditions, incl.: necessary documentation, eligibility criteria, conditions, any compulsory programs (e.g. insurance, savings), the use of client savings in the case of credit default, and how client data is used.</li> <li>• Explain group guarantee mechanism, incl. the rights and responsibilities of each group member; responsibilities in the case of a client death; and mandatory group/center requirements (attendance, group behavior, etc).</li> <li>• Describe process for loan recovery in case of late payments.</li> </ul>	<ul style="list-style-type: none"> <li>• Offer guidance on “how to select your group members”—esp. guidance on assessing peer willingness and capacity to repay.</li> <li>• Provide an overview of the institutional Code of Ethics and (if used), the Client Pledge. Pledge can include a commitment to borrow only within one’s payment capacity.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Training for group leaders:</b> collecting installments; cash handling; group conflict resolution; addressing client grievances; and the institution’s policy on multiple borrowing.</li> <li>• <b>Training for all clients:</b> consequences of over-indebtedness; the collections process; how to address unethical practices by staff; and financial literacy (optional).</li> <li>• Repeat group guarantee requirements.</li> <li>• Emphasize the importance of demanding receipts for all transactions and maintaining current passbook entries.</li> <li>• Encourage clients to raise questions and concerns.</li> </ul>
<p><b>CLIENT PROTECTION PRINCIPLES</b></p>	<p>Transparency; Ethical Staff Behavior; Mechanisms for Redress of Grievances</p>	<p>Transparency; Appropriate Collections Practices; Ethical Staff Behavior; Data Privacy</p>	<p>Avoid Over-indebtedness; Appropriate Collections; Ethical Staff Behavior; Redress of Client Grievances</p>	<p>Avoid Over-indebtedness; Appropriate Collections; Ethical Staff Behavior; Redress of Client Grievances</p>

## PHASE 2: EVALUATION

SERVICE POINT (SP)	SP5	SP6	SP7
	<p><b>GROUP LOAN APPLICATION</b> Institution guides groups through process of applying for a loan.</p>	<p><b>DATA COLLECTION: FINANCIAL AND NON-FINANCIAL</b> Institution collects client information for eligibility &amp; loan size analysis.</p>	<p><b>DATA PRIVACY &amp; MANAGEMENT</b> Institution explains and ensures the security of client data through strong internal controls.</p>
<p>GOOD CLIENT PROTECTION POLICIES</p>	<ul style="list-style-type: none"> <li>The group loan amount is a unanimous decision among group members.</li> <li>Staff refrains from judgmental questioning during application and data collection processes.</li> <li>The institution collects sufficient personal and financial information to make accurate decisions on appropriate loan amounts.</li> <li>Institutional policy dictates how the institution maintains the security and privacy of client data.</li> <li>Loan officers are trained in data management and how to explain data protection to clients.</li> <li>Clients receive copies/duplicates of any and all signed documents.</li> </ul>		
<p>GOOD CLIENT PROTECTION PRACTICES</p>	<ul style="list-style-type: none"> <li>Follow guidelines on clear communication—see <b>SP #1</b>.</li> <li>Allow any client to bring a third party to assist the client in reading/understanding forms.</li> <li>Explain the client consent form and what a signature implies for the client &amp; group.</li> <li>Include institution's contact information on the application.</li> <li>Explain how application data will be used and stored.</li> <li>If an additional signature is required on the application, explain the responsibilities and limitations for the signatory.</li> <li>Include any assets used as collateral on the application.</li> </ul>	<ul style="list-style-type: none"> <li>Ask clients for specific information about their outstanding debt, and ask group members to verify.</li> <li>Explain why assets are being recorded (e.g., for loan size evaluation &amp; collateral) and what can happen to these assets in case of default.</li> <li>Explain what demographic and business information is needed for evaluation, and how it will be stored and used.</li> <li>Explain process for how clients can update their personal information if it changes (e.g. change of address).</li> </ul>	<ul style="list-style-type: none"> <li>Explain how to protect: individual passbooks, client account numbers, savings cards, debit cards, and PIN numbers.</li> <li>Explain how client photos will be used and who will have access to them.</li> <li>Explain institution's policy on sharing an individual client's personal and financial information with the group.</li> <li>Disclose if the institution will use client information for marketing or cross-selling products.</li> <li>Prevent staff misuse of client information through use of strong internal controls.</li> <li>Strong data security means: <ul style="list-style-type: none"> <li>Internal controls/ IT management;</li> <li>Clearly-defined user access and hierarchy; and,</li> <li>Frequently changing passwords.</li> </ul> </li> <li>Include standards for client data protection in agreements with contracted third parties.</li> <li>Obtain authorization from clients before sharing financial information with third parties.</li> </ul>
<p>CLIENT PROTECTION PRINCIPLES</p>	<p>Transparency; Redress of Grievances; Privacy of Client Data</p>	<p>Avoid Over-indebtedness; Transparency; Ethical Staff Behavior, Privacy of Client Data</p>	<p>Ethical Staff Behavior, Privacy of Client Data</p>

### PHASE 3: GROUP LOAN APPROVAL

SERVICE POINT (SP)	SP8
	<p style="text-align: center;"><b>FINANCIAL ANALYSIS</b></p> <p style="text-align: center;">Institution analyzes personal and financial information and determines group eligibility and (if accepted) loan size.</p>
<p>GOOD CLIENT PROTECTION POLICIES</p>	<ul style="list-style-type: none"> <li>• The institution does not lend more than group members request or are capable of repaying.</li> <li>• Loan approval does not rely solely on group guarantee mechanism. All lending decisions incorporate some capacity to repay analysis. As loan size increases, this analysis is increasingly thorough.</li> <li>• Loan officers know the explicit guidelines for client debt thresholds and acceptable levels of debt from other sources.</li> <li>• Internal audit routinely checks loan officers' use of financial analysis, and follows up with a sample of delinquent clients to check for over-indebtedness.</li> </ul>
<p>GOOD CLIENT PROTECTION PRACTICES</p>	<ul style="list-style-type: none"> <li>• Capacity to pay analysis should be as rigorous as possible, given the institution's time and resource constraints, and should include at minimum, a calculation of the client's assets, liabilities, and household surplus.</li> <li>• Collect data on other loans the client may have. This can be done through an interview, a credit bureau, or an information exchange between institutions.</li> <li>• Invest in acquiring available data so that the institution can make the best credit decision.</li> <li>• The threat of client over-indebtedness should be continually monitored by the institution and by group members--e.g. an analysis of client over-indebtedness at the start of each new loan cycle.</li> <li>• Debt guidelines may vary based on geographic area, business sector, and other relevant factors.</li> <li>• Consider limits on amount clients must pay when a group member is in default (if using group guarantee mechanism). This could be a percentage of the original loan amount.</li> <li>• After rejecting a loan application, inform the client as to the reason(s).</li> <li>• Shortly after disbursement, conduct a loan utilization check to verify appropriate use of loan by clients.</li> </ul>
<p>CLIENT PROTECTION PRINCIPLES</p>	<p>Avoid Over-indebtedness</p>

## PHASE 4. DISBURSEMENT

SERVICE POINT (SP)	SP9	SP10
	<b>DISBURSEMENT SPEECH</b> Institution verbally reviews important account information before opening account.	<b>DOCUMENTATION</b> Institution provides client with a summary document to take home.
<b>GOOD CLIENT PROTECTION POLICIES</b>	<ul style="list-style-type: none"> <li>• Ensure that a sufficiently trained staff member is responsible for assembling all relevant information on the group's account.</li> <li>• Allow sufficient time in the disbursement process for clients to ask questions and address concerns.</li> </ul>	
<b>GOOD CLIENT PROTECTION PRACTICES</b>	<p><b>General:</b></p> <ul style="list-style-type: none"> <li>• Follow guidelines on clear communication—see SP #1.</li> <li>• Verbally review each loan document with the group, including the repayment schedule.</li> <li>• Read the summary sheet to the group (see SP #10, at right).</li> <li>• Consider a poster on the wall near where the disbursement occurs to remind staff and clients of their rights and responsibilities.</li> </ul> <p><b>Key Elements of Disbursement Speech:</b></p> <ul style="list-style-type: none"> <li>• Explain all costs (e.g. stamp duty, margin money, insurance, any other linked products, etc.). Advise clients not to pay additional fees or commissions to staff, beyond what is explained in disbursement speech.</li> <li>• Explain impact of fees on amount disbursed, when deducted upfront.</li> <li>• If the group shares liability, explain that individual clients control their own portion of the group loan. If other personal guarantors, explain their liability. If collateralized loans, review process.</li> <li>• Advise clients to always ask for a receipt for all transactions.</li> <li>• Explain what happens at the end of a loan term (e.g. repeat loans, closing the account), as well as how the group is renewed/maintained.</li> <li>• Provide clients with the time and opportunity to ask questions and to choose not to continue with the loan disbursement, based on their careful consideration of the above information.</li> </ul>	<ul style="list-style-type: none"> <li>• Provide the client with a short summary sheet that includes:             <ul style="list-style-type: none"> <li>• The rights and duties of the client, the group, and the institution.</li> <li>• The group/client repayment and amortization schedule.</li> <li>• Complaints information, including the institution's contact information and information about how to complain to any existing regional or national complaints agencies.</li> <li>• Collections practices, consequences, and procedures in case of non-repayment.</li> <li>• Information on how to request account information.</li> </ul> </li> <li>• Explain the summary sheet in non-legal terms and ask the group if they have questions or concerns.</li> <li>• Ensure that each group member receives a signed copy of the summary sheet.</li> </ul>
<b>CLIENT PROTECTION PRINCIPLES</b>	Avoid Over-indebtedness, Transparent and Responsible Pricing; Ethical Staff Behavior	Transparent and Responsible Pricing; Ethical Staff Behavior; Mechanism for Redress of Grievances

## PHASE 5. CUSTOMER SERVICE AND COLLECTIONS

SERVICE POINT (SP)	SP11	SP12	SP13
	<b>ONGOING CUSTOMER SERVICE</b> Institution continuously supports client satisfaction and product understanding.	<b>ON-TIME COLLECTIONS</b> Institution collects payments on scheduled day and in method outlined in loan contract.	<b>LATE REPAYMENT AND RECOVERY</b> Institution treats clients with dignity while collecting late installments.
<b>GOOD CLIENT PROTECTION POLICIES</b>	<ul style="list-style-type: none"> <li>• Institutional Code of Ethics spells out values and standards of conduct required by all staff, and clearly defines sanctions for unethical behavior.</li> <li>• Institutional debt collections policy details acceptable and unacceptable collections practices to prevent subjective decision making by collections staff.</li> <li>• Institutional loan recovery policy outlines step-by-step procedures and timelines for late payment recoveries.</li> <li>• A robust internal audit and fraud control system detects client mistreatment, such as soliciting kickbacks or favors.</li> <li>• Staff is evaluated and/or incentivized on the quality of their interactions with clients.</li> <li>• Client complaints are taken seriously, investigated, and resolved in a timely manner.</li> <li>• Staff is trained on the institution's complaints handling process.</li> </ul>		
<b>GOOD CLIENT PROTECTION PRACTICES</b>	<ul style="list-style-type: none"> <li>• In all communications with clients, follow communication guidelines outlined in <b>SP#1</b>.</li> <li>• Honor account information requests in a timely way.</li> <li>• Provide verbal account information to illiterate clients.</li> <li>• Alert clients to upcoming changes in product terms, conditions, fees, or interest rates.</li> <li>• Document, investigate, and resolve client complaints in a timely manner.</li> <li>• Internal audit or other monitoring system should check that complaints are resolved satisfactorily.</li> <li>• Do not use or share client information or photos (for marketing, promotions, etc.) without client consent.</li> <li>• Include institution contact information on all materials, and post in service points such as branch offices.</li> </ul>	<ul style="list-style-type: none"> <li>• Code of Ethics should include guidelines specific to collections.</li> <li>• Check for regular passbooks updates if group leaders handle collections.</li> <li>• Use preventive recovery methods, such as reminders.</li> <li>• Always provide a receipt and give exact change.</li> <li>• Ensure that field collections happen on a specified day.</li> <li>• Collect money publicly and transparently.</li> <li>• Ensure internal audit monitors center meeting collections.</li> <li>• Ensure that any third party collections agents agree to the institution's Code of Ethics.</li> <li>• Prevent theft (including internal) by carefully monitoring cash collection and setting limits on cash collection.</li> </ul>	<ul style="list-style-type: none"> <li>• Recovery measures should be based on type of default: temporary vs. long-term repayment problem; client death; willful default; mass default, etc.</li> <li>• As a first step, the escalation policy should engage the client and her group in a problem-solving session. As a second step, engage other important stakeholders—center leaders, village leaders, local functionaries, etc.</li> <li>• Prohibit staff and group leaders from: use of force, coercion, assertion of excessive group pressure, lengthy center meetings, humiliation etc.</li> <li>• Recovery practices should be audited by branch managers and internal auditors and violations strictly sanctioned.</li> <li>• Ensure clients understand penalties, additional charges, and adjustments.</li> <li>• Ensure restructuring does not increase the debt levels of already indebted clients.</li> <li>• Do not charge interest after loans are written off.</li> </ul>
<b>CLIENT PROTECTION PRINCIPLES</b>	Transparency, Redress of Grievances, Privacy of Client Data	Appropriate Collections Practices; Ethical Staff Behavior	Appropriate Collections Practices; Ethical Staff Behavior

## **ANNEX: CLIENT PROTECTION TOOLS TO IMPROVE PRACTICE AT EACH SERVICE POINT**

Institutions can benefit from the many tools already available for download on the Smart Campaign website, at no cost. Tools include guides for client protection in the individual lending process and the savings process; mini case-studies; Excel-based tools for calculating appropriate loan size; guidelines on how to develop an institutional code of ethics; a client protection self-evaluation for MFIs, and many more.

In the chart below, each service point is listed alongside a list of client protection tools that can improve an institution's ability to protect clients at that particular service point. Where these tools already exist through the Smart Campaign, a link is provided to the website. Other tools have yet to be developed and we encourage MFIs to develop these on their own, and share these developments with the Smart Campaign ([info@smartcampaign.org](mailto:info@smartcampaign.org)).

<b>SERVICE POINTS.</b> The financial institution interacts with clients at the following service points:	<b>CLIENT PROTECTION TOOLS.</b> At each service point, the financial institution can improve its ability to protect clients by using the following tools:
SP#1. PROMOTIONS	Guide for the development of promotional materials; Sales dialogues for loan officers; Sample internal audit checklist for monitoring client recruitment.
SP#2. PRODUCT DESCRIPTION	Guide for describing products to clients (e.g. checklist of points to cover); Guide for describing the group guarantee mechanism.
SP # 3. GROUP FORMATION	Group rights and responsibilities checklist.
SP #4. GROUP TRAINING	Group training manual for loan officers; Group training materials for group leaders (in local language/ pictures for illiterate clients).
SP #5. GROUP LOAN APPLICATION	Guide on how to request information from a client; Sample plain-language application form.
SP #6. DATA COLLECTION: FINANCIAL AND NON-FINANCIAL INFORMATION	Guide for communicating eligibility criteria to groups; Guide for how to talk to clients about over-indebtedness.
SP #7. DATA PRIVACY AND MANAGEMENT	Data management protocol manual; Sample third-party contracts that include agreements on privacy of client data; Checklist for internal audit to verify institutional compliance with data security measures. <sup>3</sup>
SP #8. FINANCIAL ANALYSIS	Guidelines for financial evaluation; Financial evaluation worksheet/spreadsheet.
SP #9. DISBURSEMENT SPEECH	Sample “plain language loan contract;” <sup>4</sup> Guidelines for disbursement speech; Sample disbursement speech.
SP #10. DOCUMENTATION	Guidelines for documentation requirements; Sample summary page. <sup>5</sup>
SP#11. ONGOING CUSTOMER SERVICE	Guidelines for receiving and resolving client complaints; <sup>6</sup> Sample intake form; Guidelines for selling new products and renewing loans; Sample consent for use of client information/photos; Checklist for informing clients of term changes
SP#12. ON-TIME COLLECTIONS	Guidelines for collections practices; <sup>7</sup> Sample Code of Ethics; <sup>8</sup> Sample internal audit checklist for monitoring collections practices.
SP #13. LATE REPAYMENT & RECOVERY	Guidelines for recoveries; <sup>9</sup> Sample restructuring policy & process (rescheduling & refinancing); Sample scripts for recoveries (for staff and group leaders).

3. For more information on data security see “Smart Note: Customized IT at Caja Morelia safeguards client data,” here: <http://smartcampaign.org/tools-a-resources/2/248>
4. This resource is available through the Smart Campaign. Find an example of a plain language loan contract here: <http://smartcampaign.org/tools-a-resources/2/275>.
5. This resource is available through the Smart Campaign. Find an example of a loan contract summary here: <http://smartcampaign.org/tools-a-resources/2/276>.
6. The Smart Campaign offers resources on receiving and resolving client complaints, here: <http://smartcampaign.org/component/taxonomy/term/list/25/12>
7. For more information on collections strategies, see ACCION International’s “Best Practices in Collections Strategies,” here: <http://smartcampaign.org/tools-a-resources/2/83>.
8. Download the Smart Campaign’s “How to Develop an Institutional Code of Ethics” here: <http://smartcampaign.org/tools-a-resources/2/84>. View sample Codes from around the world, here: <http://smartcampaign.org/tools-a-resources/2/44>.
9. For more information on collections strategies, see ACCION International’s “Best Practices in Collections Strategies,” here: <http://smartcampaign.org/tools-a-resources/2/83>.