LAW 130
(dated 31 December 2013)

That establishes the Prudential Regulatory Framework for Microfinance Entities and amends provisions of Law 10 of 2002 that establishes the rules for the Microfinance System

THE NATIONAL ASSEMBLY

DECREES:

Article 1. This Law governs the operations of credit entities that are not subject to prudential and accounting requirements.

Cooperatives are excluded from the regulation of this Law.

Article 2. For the purposes of this Law, the following terms will be understood as follows:

1. *Consumer loan.* A loan granted to an individual under agreed time and interest, destined to fund the acquisition of perishable and non-perishable consumer goods, payment of services or expenses not related to entrepreneurial activities, payable in successive installments and whose main source of repayment is the salary of that individual and/or the income from his/her economic activity.
2. *Restructured loan.* A loan that has any of the original conditions amended due to a real or potential deterioration of the debtor's payment capacity.

   The purpose of restructuring is to achieve the most favorable conditions for the entity to recover the debt and to postpone recognition of the deterioration.
3. *Refinanced loan. A loan in which* the terms and/or amount of the original contract are changed for reasons unrelated to real or potential difficulties in the debtor's payment capacity.
4. *Credit scoring.* A method for measuring credit risk.
5. *Microloan.* A small loan granted to an individual or legal entity borrower whose main source of income comes from production, marketing or services and who does not necessarily have formal support documentation, records of income or registered real collateral.

6. *Generic provision for additional risk.* The amount that entities operating microloans and consumer loans must create and maintain when their loan activities have non-collection risk factors besides delinquency.
7. *Voluntary generic provision.* The amount that entities operating microloans and consumer loans may freely create and that will be part of tier 2 capital with prior verification of the oversight body.

Article 3. Prior to granting a microcredit loan, the credit entity must conduct a comprehensive assessment of the borrower, including an analysis of payment capacity based on the applicant's income, his/her net equity, the amount of his/her obligations or liabilities, the quotas on the loan to be paid to the credit entity and the ratings given to the debtor in the rest of the financial system by the Panamanian Credit Association.

The assessment of borrowers will be made using loan technologies containing procedure manuals for credit risk management clearly defining the applied technology, as well as internal control manuals permitting controlling/monitoring the risks inherent in these operations.

For approval, creation, and disbursement of consumer loans, financial entities may use internal risk methods or measurement systems, such as *credit scoring, ratings* or other risk management methods and processes, and other procedures necessary for assigning availability and other loan conditions pursuant to the customers' profile and the entity's business strategy.

Internal control systems or methodologies implemented by entities referred to in the above paragraph must be certified in accordance to the instructions given by the Oversight Body for that purpose.

Article 4. Microfinance entities must have appropriate internal control systems according to the nature and scale of their business, including clear and defined provisions for the delegation of authority and responsibility, separation of duties, funds disbursement, operational accounting, safekeeping of assets, and appropriate independent internal and external auditing, as well as an administrative unit responsible for overseeing that the staff complies with these controls, laws, and applicable provisions.

Article 5. A maximum amount of fifty thousand balboas (B/.50,000.00) is fixed for microloans. The Oversight Body may modify this amount.

Article 6. Loans may be:

1. *Individual.* A loan granted by a credit entity to an individual and its guarantor, aimed at covering their funding needs, whether it is to fund business, service and/or production activities or to purchase consumer goods.
2. *Joint liability.* A loan granted by credit entities to a small group of people – between three and ten – jointly securing the return of the loan.
3. *Joint.* A loan granted by credit entities to a group of businessmen or neighbors in a community or neighborhood constituting a group to jointly manage and secure the loan. For that purpose, they must create a democratic organization, choose their own leaders, draft their own rules, register their operations, and manage their funds. The board of directors is wholly responsible for supervising the loans, including penalties for noncompliance.
4. *Associative.* A loan granted to economic organizations (associations) of farmers, miners and artisans, usually poor people living in rural areas with a low level of economic development and, consequently, financially excluded. The organization must continue to exist during the term of the loan and its members must share the same economic activity, which must be profitable, viable, and sustainable. The loan is usually granted as investment capital and seeks the growth and capitalization of its beneficiaries who are, at the same time, members of the organization.

The organization must have a credit record that is appropriate for mediating between the borrowing entity and the members of the organization. The organization must have a collateral fund, previously created by its members, that must be deposited in a bank.

Article 7. Financial system entities operating with microloans must request the information required by their own loan technology, which must consider the following, as a minimum:

1. The identity documents and the residential and business addresses.

2. The activity of the customer and his/her situation within the market in which he/she operates.
3. The source of income and its support, if any.
4. Payment records with suppliers and other creditors.
5. The loan application, in which the amount, terms and method of payment must be included.
6. The documentation proving real collateral is current and properly appraised, when applicable.
7. Any other documentation required by loan policy or technology, which will depend on the debtor's economic activity (business, service, agriculture or industrial) and his/her target market (export, domestic, wholesale or retail).

Article 8. Credit entities will freely fix interest rates, fees, and other charges to be applied to their operations and services. This interest rate will be applied to all balances due. In no case will service fees or expenses not related to services actually rendered or expenses incurred be charged.

The effective interest rate must include all charges and fees of all types. This rate must be announced to the public through the media and posted in a visible place at the agencies.

Entities must expressly indicate the equivalent annual effective rate in all financial contracts and inform the users of changes, if any.

Article 9. Credit entities will record the interest, fees and other additional charges using the accrual method, as long as the loan is still classified as current. These entities may not accrue any earned income on loans reclassified as delinquent or in liquidation.

Nor can loans granted to system debtors that have insolvent loans or loans in liquidation in the bank or any other entity in the system, including entities under liquidation, accrue income while these loans are not normalized, nor can interest be accrued on current loans of a borrower that has delinquent loans with the same entity. Similarly, at the moment in which the borrower's loan is classified in the D or E categories of the article below, receivable interests, fees, and other products must be written off and their accrual must be immediately suspended.

Consequently, they cannot be recorded in the profit statement of the financial entity until the interests, fees, and commissions are actually collected. While those are being collected, the relevant notation will be made in suspense accounts. The Oversight Body may order the suspension of these incomes when a loan has been restructured more than once.

Article 10. Credit entities must rate their microcredit portfolio and make the relevant provisions in accordance with the chart below:

Category	Delinquency	Provision
A. Normal	Up to 29 days	1%
B. Special Mention	Between 30 and 45 days	10%
C. Substandard	Between 46 and 60 days	20%
D. Doubtful	Between 61 and 90 days	50%
E. Unrecoverable	Over 90 days	100%

Banks under the supervision and regulation of the Superintendency of Banks of Panama must classify their microcredit portfolio and its relevant provisions pursuant to the regulatory rules issued by the Superintendency for that purpose.

Article 11. Any loan restructuring must be formalized by entering into any legal agreement that modifies the originally agreed conditions so that the debtor can properly meet the obligation. Before restructuring the loan, the financial entity must establish whether the loan can be recovered under the new conditions, i.e. the financial entity must make a new assessment of the debtor's payment capacity.

In any case, restructurings must be an exceptional recourse to guarantee the performance of the loan portfolio; they must not be made a general practice.

Debtor ratings must remain in the classification they had prior to restructuring or refinancing, with one exception: a loan previously ranked Doubtful may be upgraded to Substandard, as long as the debtor has proved his/her payment capacity for the new payment plan.

The payment capacity may be proven by the timely payment of agreed installments during two consecutive quarters, as well as meeting the refinancing or restructuring plan goals after a similar period has passed. However, if the debtor has failed to comply with the agreed installments, has failed to meet the goals agreed to for the quarter, and/or his/her payment capacity has deteriorated, the financial entity must reclassify the debtor in a higher-risk category. If the refinancing or restructuring operation covers a grace period, the provisions in the above paragraph will be applied beginning at the conclusion of that grade period.

Credit institutions must regularly follow up on the reclassified debtors. Entities must regularly inform the Oversight Body of the refinancings and restructurings granted to their debtors and all the reclassifications of categories made during the month no later than the fifth business day of the following month. This report must be included in the information reported to the Panamanian Credit Association.

Article 12. Loans whose amortization payments to capital and interest have not been fully paid to the entity within the fifteen days following the established payment date will be placed in the delinquent portfolio. For this purpose, the effective accounting date for this account will be the sixteenth day after the due date.

Any loan whose payment date for the amortization of capital and interest has been postponed for additional fifteen-day periods must be recorded as a delinquent portfolio.

Article 13. During the examinations visit, the Oversight Body will assess the loan activity of the financial system entity, in order to verify whether there are non-collection risk factors besides delinquency and, as a result, a need to create a generic provision for additional risk. The generic provision may only be decreased with the previous authorization of the Oversight Body.

For the purpose of determining the generic provision for additional risk, the Oversight Body will evaluate the policies, practices and procedures for granting and managing microloans and consumer loans, as well as credit risk controls, verifying they include, as a minimum:

1. The existence of an appropriate loan technology for the selection of the borrower, the determination of his/her payment capacity and the management and recuperation of loans, as well as an appropriate internal control system.
2. An adequate system for evaluating and classifying the portfolio and effective mechanisms for verifying their functioning, reviewed in a timely manner according to the situation.
3. Market and clientele prospects.
4. The existence of a computerized procedural system to follow up on microloan and consumer loan operations.

When it is determined that policy, practices and procedures for granting, managing, and controlling loans do not conform to the guidelines established herein, the financial system entity will be required to create and maintain a generic provision for additional risk factors of up to 3% of the microloan and consumer loan portfolio.

The generic provision for additional risk factors will be determined based on the review of a representative sample of borrowers, under statistical criteria, using computer procedures or other procedures oriented towards achieving a greater reach of the analysis, the frequency of cases where there are deviations or non-compliances with the established loan policies and procedures and/or best practices for granting and managing loans, among them, failure to comply with the following:

a. Verification of the residential and business addresses and the updated data sheet, including identity documents.
b. Verifying the source of income and a reasonable estimate of the payment capacity.
c. Verification of payment records with financial system entities and with other creditors, making sure that the customer does not have operations that are past due, in liquidation or written off.

d. Verification that the customer's guarantor has no past due debts with financial system entities or other creditors.

e. Verification, when applicable, of the currency of real collateral, its appropriate assessment, and the measures adopted for its protection.

f. Appropriate support for customers chosen and approved by automated procedures, including an appropriate historical database for those customers.

g. Documentation required by its loan policy for the application, approval, agreement, and collateral, if required.

h. Follow-up according to the provisions of its loan technology of the customer's domicile, situation and activity, which must be annotated by communication from the relevant loan officer.

i. Verification that the other aspects of the loan policy or technology have been complied with.

Article 14. For microloan and consumer loan operations, when the frequency of cases with deviations or non-compliances is higher than 10% of the sample, the financial system entity must create and maintain a generic provision for additional risk equivalent to 1% of the total loan balance relevant to the population or subpopulation that the sample comes from.

Based on the reports issued by the relevant credit bureau, an estimate will be made of the risk for customers that are also delinquent customers or customers with payment problems in other entities within the financial system, applying the following criteria:

1. The classification of the highest risk obtained by each customer in the rest of the system.
2. The classification of the highest risk obtained by each customer in the rest of the system, as long as the amount corresponding to that classification is higher than the amount granted by the entity itself.

The financial system entities whose main activity is oriented to granting consumer loans must submit their annual business plan in January of each year. If the portfolio growth for that type of operation is greater than 10%, they must constitute a generic provision of 1% on the pending balance at the closing of the year, for the purpose of covering the potential losses expected.

Credit entities regulated by this Law may constitute voluntary generic provisions.

Article 15. Article 5 of Law 10 of 2002 shall read:

Article 5. Organization of microfinance banks. Microfinance banks must be established as corporations and must have a minimum paid-in capital of three million balboas (B/.3,000,000.00).

The Superintendency of Banks of Panama is authorized to modify the minimum paid-in capital by means of a Rule.

Article 16. Article 6 of Law 10 of 2002 shall read:

Article 6. Obligations of microfinance banks. Microfinance banks are required to maintain a loan portfolio in which no less than seventy-five percent (75%) of the loans are granted to micro and small enterprises.

Article 17. This Law amends Articles 5 and 6 of Law 10 dated 30 January 2002.

Article 18. This Law shall take effect the day after its promulgation.

FOR COMMUNICATION AND ENFORCEMENT.

Bill 666 of 2013 approved at the third reading in Palacio Justo Arosemena, Panama City, on the sixteenth (16th) day of December, two thousand thirteen (2013).

The President,

[Signed]
Sergio R. Galves Evers

The Secretary General,

[Signed]
Wigberto E. Quintero G.

NATIONAL EXECUTIVE BRANCH. PRESIDENCY OF THE REPUBLIC. PANAMA, REPUBLIC OF PANAMA, 31 DECEMBER 2013.

[Signed]
RICARDO MARTINELLI BERROCAL
President of the Republic

[Signed]
LUIS EDUARDO CAMACHO G.
Minister of Commerce and Industry, in charge