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# Trouble with Regulating Microfinance

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# The Trouble with Regulating Microfinance

Anita Bernstein\*

*In its short lifetime, the neologism “microfinance” has become central to several realms—among them philanthropy, social entrepreneurship, commercial banking, and economic development efforts underway in numerous nations—with no consensus on what the word includes and excludes. Indeterminacy makes microfinance resemble other abstract polysyllabic Latinate words like “nationalization,” “industrialization,” “privatization,” “globalization,” and “democracy.” Unlike these other nouns, however, microfinance has struck observers as amenable to unitary regulation.*

*Well-intentioned proposals start from the erroneous premise that a single statute, best-practices compendium, or set of governing principles can cover all of microfinance. These efforts are destined to fail until reformers pause to consider the goals they can pursue and the varied sectors they address. The word has its uses. Before microfinance can be regulated, however, it must be disaggregated.*

## TABLE OF CONTENTS

INTRODUCTION .....	2
I. “MICROFINANCE NEEDS REGULATION” .....	6
A. What Reformers Have Offered .....	7
1. Disaggregation and Reaggregation .....	7
2. Microfinance Understood as For-Profit Banking .....	8
3. Microfinance Commandments .....	8
4. Comprehensive National Laws .....	9
5. An Assessment .....	10
B. Crises That Invite More Responses .....	10
II. BUT WHAT IS MICROFINANCE? RECURRING CONFUSIONS .....	13
A. Definitional Uncertainty .....	13
B. Conventional Wisdoms .....	15
1. Optimism .....	15
2. Pessimism .....	18

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3.	Seeking the Center.....	20
C.	The Oxymoron of a “Double Bottom Line”.....	23
III.	DISAGGREGATION, FIRST PASS: MICROFINANCE AS BANKING FOR PEOPLE...24	
A.	Support For Savings.....	25
1.	Reconsidering Prudential Rules.....	26
2.	Linkages.....	26
3.	New Types of Savings Accounts.....	27
4.	Reaching Poor Depositors Where They Live and Work.....	28
B.	Enhanced Lending.....	29
1.	Consumer Protection.....	30
2.	Optimizing Loan Capital: Toward Sustainability.....	34
IV.	REGULATION DISAGGREGATED, SECOND PASS: A FOCUS ON OWNERS.....36	
A.	Pertinent Distinctions Among Providers.....	37
B.	Owner-Specific Attentions.....	40
1.	Microfinance as Mutual Aid.....	40
2.	Microfinance for Profit.....	42
3.	Microfinance as Instrumental to a Nonprofit Mission.....	43
4.	Fitting the Three Provider Categories Together.....	45
	CONCLUSION.....	47

## INTRODUCTION

Banking delivered in small-scale transactions to low-income clients, known since the mid-1990s as “microfinance,” appears to cry out for law-based controls. Even governments lacking the will or expertise to regulate other industries and sectors have paid heed to loans and other financial instruments offered to clients who are too poor to access traditional bank services.<sup>1</sup> Experts share this view: Microfinance Needs Regulation.<sup>2</sup>

Room for disagreement remains, of course. Discussions fill lively literatures in a variety of disciplines, especially on whether legal controls ought to encourage, or instead curb, lending to poor people.<sup>3</sup> While differences flourish, however, informed opinion unites in support of regulation.

<sup>1</sup> See *infra* Part III.A.1.

<sup>2</sup> Aneel Karnani, *Microfinance Needs Regulation*, 9 STAN. SOC. INNOVATION REV. 48 (Winter 2011), available at [http://www.ssireview.org/images/articles/2011WI\\_Feature\\_Karnani.pdf](http://www.ssireview.org/images/articles/2011WI_Feature_Karnani.pdf); see also Aaron Jones, Note, *Promotion of a Commercial Viable Microfinance Sector in Emerging Markets*, 13 GEO. J. ON POVERTY L. & POL’Y 187, 199-203 (2006) (noting that observers agree on the need to regulate microfinance but disagree on what this regulation should provide); Shelley Thompson, Note, *80 Simple Rules: The Effective and Sustainable 2009 Rwandan Microfinance Regulations*, 38 SYRACUSE J. INT’L L. & COM. 415, 420 (2011) (observing that regulation is salutary for microfinance institutions themselves).

<sup>3</sup> See *infra* Part II.

From this consensus, efforts to codify the definitive set of microfinance rules have escalated.<sup>4</sup> Each new statement of regulatory goals or ideals appears to inspire the next set of drafters to do it again and do it better. Although Microfinance Needs Regulation stays in place as a commitment, enthusiasts have not completed, and appear unable to complete, the project that they have deemed necessary.

When one considers the extraordinary talent and ample funding that underlie attempts to write the optimal rules for microfinance, this failure cries for an explanation. Drafters like the Consultative Group to Assist the Poor, the Basel Commission on Banking Supervision, and the World Bank have drawn on sophisticated data sets, years of experience, well-curated troves of national and local regulations, good will, good intentions, and the participation of researchers who enjoy international renown. These strengths having failed to achieve the goal—that is to say, no definitive regulation of microfinance having emerged—I raise in this Article the possibility that expertise in microfinance might impede rather than advance the undertaking.

The trouble with regulating microfinance is not the burden of regulation on microfinance providers or their stakeholders—like every other observer who writes in this field, I accept the need for legal rules—but, I argue, “microfinance” itself. The word has brought together constituents that for purposes of regulation ought to remain separate.<sup>5</sup> Microfinance is no more amenable to a best-practices regulatory recitation than any other broad-swatch Latinate noun that describes macroeconomic conditions.

Policymakers who would never have tried to summarize in one document a scheme to regulate “industrialization,” “globalization,” “privatization,” or “democracy” may have been misled by the “micro” in microfinance, which makes their target look small and well-cabined. It is no such thing. Because the term blurs lines that matter, any single set of regulatory considerations for microfinance will necessarily be either wrong (at least with respect to some entities or individuals in the cohort addressed) or vague to the point of meaninglessness. Accordingly the notion of Microfinance Needs Regulation, explained in Part I as resting on aggregations of crises that generate and accompany aggregations of recommendations, becomes a blueprint for the reiteration of failure.

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<sup>4</sup> See *infra* Part I.A.

<sup>5</sup> The linguistic term “polysemy,” referring to overlapping and multiple meanings present in a single word, is on point. See Charles J. Fillmore & B.T.S. Atkins, *Describing Polysemy: The Case of “Crawl,”* in POLYSEMY: THEORETICAL AND COMPUTATIONAL APPROACHES 91, 91 (Yael Ravin & Claudia Leacock eds., 2000) (noting what the verb “to crawl” can signify).

Readers will recall the distinction between what the biologist George Gaylord Simpson once called “lumpers” and “splitters”: When making classifications, lumpers focus on large units; splitters focus on smaller ones.<sup>6</sup> Microfinance as neologism is the work product of a lumper.

The coinage aptly brings together a cluster of deprivations, challenges, innovations, and opportunities faced by the unbankable poor.<sup>7</sup> “Microfinance” gathers into one word a set of needs and pursuits that could easily fill a paragraph. It has a place in policy: banking for poor people is, and ought to remain, vital in national and transnational debates. Yet because the label tells nothing about conditions that the law finds meaningful—such as those found in banking law and rules related to corporate governance—it unites what ought to receive analytically separate legal controls rather than a unitary response. Part II of this Article reviews some lexical difficulties inherent in the word.

Presenting a splitter-repair to fix a lumper source of confusion, this Article makes suggestions in broad-survey outline form. My starting point is to consider what legal controls might aspire to achieve. Here I presume that regulators want to improve the delivery of small-scale loans and savings.<sup>8</sup>

An alternative to Microfinance Needs Regulation emerges after microfinance is disaggregated. Exploring the question broached in Part II—just what is microfinance?—Part III offers an unglamorous answer: banking for low-income savers and borrowers.<sup>9</sup> Clearing away high-sizzle

<sup>6</sup> George G. Simpson, *The Principles of Classification and a Classification of Mammals*, 85 BULL. AM. MUSEUM NAT. HIST. 1, 23 (1945). For a recent reference to the dichotomy, see Peter H. Schuck, *Professor Rabin and the Administrative State*, 61 DEPAUL L. REV. 595, 611 (2012).

<sup>7</sup> “Unbankable” entered the financial-development literature with IBRAHIMA BACKHOUM, *BANKING THE UNBANKABLE: BRINGING CREDIT TO THE POOR* (1989). See also GERT VAN MAANEN, *MICROCREDIT: SOUND BUSINESS OR DEVELOPMENT INSTRUMENT* 17 (2004) (“In general, banks are for people with money, not for people without.”).

<sup>8</sup> Other motives might occupy regulators. See ROBERT BALDWIN & MARTIN CAVE, *UNDERSTANDING REGULATION: THEORY, STRATEGY, AND PRACTICE* 22 (1999) (reviewing regulatory capture and public choice, both of which ascribe self-interest to regulators’ decisions).

<sup>9</sup> “Microfinance” as neologism tacitly favors the perspective of wealthy providers over that of their clientele. “Micro” is a gradable adjective: a savings account or a loan is small only when compared to something bigger. See generally Paul Egré & Nathan Klinedinst, *Introduction: Vagueness and Language Use*, in *VAGUENESS AND LANGUAGE USE* 5 (Paul Egré & Nathan Klinedinst eds., 2011) (describing gradable adjectives). Billion-dollar undertakings are not called macrofinance to reference their large size; they are simply finance, and from the vantage point of poor borrowers or savers, microfinance is simply finance. A wordier phrase like “banking for low-income savers and borrowers” brings these people to the foreground.

jargon returns regulators to a familiar task. Part IV continues this disaggregation by assessing opportunities to save and borrow with reference to who owns provider institutions.<sup>10</sup>

Providers of microfinance, the entities that need to be regulated, fall into three groups. The first group consists of entities whose members share the benefits of safety and risk. These institutions hold, lend, and collect money for and by their members. Owners and clients are the same people. They pool their holdings in pursuit of mutual aid. The two other ownership-based categories of microfinance providers are for-profit and nonprofit entities. Though occasionally blurred rather than bright,<sup>11</sup> the line between the two is familiar and widely heeded around the world. Nations that have codified any corporation law at all recognize both types of firms. The universality and familiarity of the division between nonprofit and for-profit comport with regulatory priorities for microfinance.

Each category of microfinance provider has distinct pursuits. For individuals who pool their money in affiliations like rotating credit associations and credit unions, microfinance is a source of goods and opportunities in daily human lives. Managers and donors of nonprofit microfinance institutions, for their part, envision and practice microfinance as poverty reduction and other eleemosynary goals.<sup>12</sup> Commercial banks experience microfinance as a source of new markets; for banks, microfinance diversifies portfolios and expands sources of income to owners.<sup>13</sup>

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Regulators ought to bear in mind that these customers are poor, for at least two reasons. First, vulnerability—including information asymmetry, impediments to self-protection, externalities, and unequal bargaining power—is fundamental to regulation generally, *see* BALDWIN & CAVE, *supra* note 8, at 9-16 (“Why regulate?”), and poor people are exceptionally vulnerable. Second, this subcategory of banking is distinct because it includes transactions that are too small to be profitable on a per-unit basis. A provider has to deviate from banking practices used for prosperous customers—it might charge fees for savings accounts, impose interest rates that look usurious, or come up with substitutes for collateral like lending to a circle of borrowers—when offering financial services to the poor. *See* Lan Cao, *Rethinking Microfinance*, 33 U. PA. J. INT’L L. 971, 986 (2012). I thank Jeffrey Thomas for his insights on this point.

<sup>10</sup> Here I follow the convention that excludes from the microfinance rubric those entities and persons who hold or lend money without purporting to follow the law. “Loansharks” and “moneylenders” are providing microfinance, if microfinance is understood as financial transactions and services furnished to poor customers; but because these words bespeak an unwillingness to abide by financial regulation, such providers lie outside the scope of this Article.

<sup>11</sup> *See generally* Dana Brakman Reiser, *Charity Law's Essentials*, 86 NOTRE DAME L. REV. 1 (2011) (asking, with regulation in mind, what exactly characterizes a charity).

<sup>12</sup> Jonathan Morduch, *The Microfinance Schism*, 28 WORLD DEV. 617 (2000).

<sup>13</sup> BLUE ORCHARD MICROFINANCE INVESTMENT MANAGERS, *Microfinance: an*

Laws around the world authorize some nonprofit institutions, banks that pursue profit, and mutual-aid entities to offer credit or savings to low-income clients. Doing so gives these providers something in common. When holding or lending money, however, they pursue different ends. Charitable missions, earnings returned as profit to external owners, and earnings returned to internal owners in a mutual-aid scheme are fundamentally unlike.

Because these types of entities generate different opportunities and consequences, the job of regulating them calls for rules that are not monolithic, along with tailored combinations of encouragement and constraint. Treating the different providers of microfinance as a single industry or sector is a regulatory mistake. Polysemy is all very well in language—probably inevitable<sup>14</sup>—but when a word that encompasses so much divergence becomes the object of a unitary rulebook, disarray ensues.

### I. “MICROFINANCE NEEDS REGULATION”

Several conditions manifest in microfinance support the consensus about its needing regulation. First and most generally, microfinance is market activity of a type that has experienced considerable market failure.<sup>15</sup> Second, microfinance encompasses consumer banking, a domain long identified as suited to government oversight.<sup>16</sup> Third, as a technology of national economic development that has been credited and blamed for both prosperity and ruinous debt,<sup>17</sup> microfinance appears simultaneously too valuable to ban and too risky to leave unattended. Finally, microfinance is a sector in which inadequate education and economic stresses impede the ability of individual participants to know, assert, and safeguard their interests.<sup>18</sup>

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*alternative asset class*, <http://www.blueorchard.com/jahia/Jahia/pid/399> (last visited Oct. 24, 2012).

<sup>14</sup> See Fillmore & Atkins, *supra* note 5.

<sup>15</sup> See *infra* Part I.B.

<sup>16</sup> See generally Ronald J. Gilson, Henry Hansmann, & Mariana Pargendler, *Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the United States, and the European Union*, 63 STAN. L. REV. 475 (2011) (connecting this need with national development imperatives).

<sup>17</sup> See *infra* Part II.B.

<sup>18</sup> Anita Bernstein & Hans Dieter Seibel, *Reparations, Microfinance, and Gender: A Plan, with Strategies for Implementation*, 44 CORNELL INT'L L.J. 75, 90-94 (2011) (summarizing various disempowering conditions that impede micro-borrowers); Rashmi Dyal-Chand, *Reflections in a Distant Mirror: Why the West Has Misperceived the Grameen Bank's Vision of Microcredit*, 41 STAN. J. INT'L L. 217, 261-66 (2005) (reporting empirical findings about oppression in the Grameen model).

Mindful of these circumstances regulators, starting in the late 1990s, have been addressing the problem of how to regulate this sector. Comprehensive statements purporting to govern microfinance—drafted in the form of legislation, principles, guidelines, best practices, and other schemes—have proliferated. They continue to emerge.

### A. What Reformers Have Offered

Proposals to regulate microfinance have taken varying approaches that reflect an array of goals and priorities for rule-writers, surveyed here with examples of each.

#### 1. Disaggregation and Reaggregation

The World Bank, an international financial institution whose motto is “Working for a World Free of Poverty,”<sup>19</sup> published the first comprehensive proposal in 1998.<sup>20</sup> Emphasizing disaggregation, the *Framework for Regulating Microfinance Institutions* focused on risk management and “prudential”—i.e. bank-supervisory—considerations.<sup>21</sup> It divided microfinance providers into three categories and seven types.<sup>22</sup>

The Consultative Group to Assist the Poor (“CGAP”), an entity housed at the World Bank but established as “independent”<sup>23</sup> and funded by donor agencies and private foundations,<sup>24</sup> has offered an alternative set of recommendations for microfinance regulation.<sup>25</sup> Its description of

<sup>19</sup> THE WORLD BANK GROUP, *Working For a World Free of Poverty* (2006), available at <http://siteresources.worldbank.org/EXTABOUTUS/Resources/wbgroupbrochure-en.pdf>.

<sup>20</sup> Hennie van Greuning, Joselito Gallardo, & Bikki Randhawa, *A Framework for Regulating Microfinance Institutions*, FINANCIAL SECTOR DEVELOPMENT DEPARTMENT, THE WORLD BANK (1998), <http://elibrary.worldbank.org/docserver/download/2061.pdf?expires=1351231135&id=id&accname=guest&checksum=ABE46D1CB3B17EDAE0E1381024AE63C9> [hereinafter van Greuning et al., *Framework*]. “The term ‘World Bank’ refers only to the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA).” See THE WORLD BANK, *About The World Bank*, <http://web.worldbank.org/WBSITE/EXTERNAL/EXTSITETOOLS/0,,contentMDK:20147466~menuPK:344189~pagePK:98400~piPK:98424~theSitePK:95474,00.html#2> (last visited Oct. 25, 2012).

<sup>21</sup> van Greuning et al., *Framework*, *supra* note 20.

<sup>22</sup> *Id.* at ii.

<sup>23</sup> See CGAP, <http://www.cgap.org/about> (last visited Oct. 25, 2012).

<sup>24</sup> The World Bank provides this data at THE WORLD BANK, <http://siteresources.worldbank.org/INTDGF/DGFPrograms/21870033/CGAP.pdf> (last visited Oct. 25, 2012).

<sup>25</sup> Robert Peck Christen, Timothy R. Lyman, & Richard Rosenberg, *Microfinance Consensus Guidelines: Guiding Principles on Regulation and Supervision of Microfinance*, CGAP/THE WORLD BANK GROUP (2003), <http://www.cgap.org/sites/default/files/CGAP->



microfinance purports to cover all sources of this product: “non-government organizations (NGOs); cooperatives; community-based development institutions like self-help groups and credit unions; commercial and state banks; insurance and credit card companies; telecommunications and wire services; post offices; and other points of sale.”<sup>26</sup>

## 2. *Microfinance Understood as For-Profit Banking*

For the Basel Committee on Banking Supervision, a transnational entity formed in 1930 “to foster international cooperation” among national central banks “in their pursuit of monetary and financial stability,”<sup>27</sup> regulating microfinance is a subset of regulating banks. The Basel Committee published *Microfinance Activities and the Core Principles for Effective Banking Supervision* in 2010.<sup>28</sup> Celebrated among poverty-reduction activists as “the first paper ever by the Basel Committee on a financial inclusion topic,”<sup>29</sup> this proposal for comprehensive regulation focuses on deposit-taking institutions.

## 3. *Microfinance Commandments*

The European Commission published its take on microfinance regulation in 2007.<sup>30</sup> Unlike the World Bank, CGAP, and Basel documents, which all espouse universalism, *The Regulation of Microcredit in Europe* addresses only one (large and affluent) geographic region. It differs from the other three also in favoring description over prescription; its recitation of precepts appears at the end, in four quasi-commandments: “1. Allow for lending by non-banks. 2. Avoid setting interest rate caps too low. 3. Ensure minimum

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Consensus-Guidelines-Guiding-Principles-on-Regulation-and-Supervision-of-Microfinance-Jun-2003.pdf.

<sup>26</sup> See PI SLICE, *Microfinance*, <http://pi-slice.com/content.php?id=12> (last visited Oct. 25, 2012).

<sup>27</sup> See BANK FOR INTERNATIONAL SETTLEMENTS, *About BIS*, <http://www.bis.org/about/index.htm> (last visited Oct. 25, 2012).

<sup>28</sup> Bank For International Settlements, Consultative Document, *Microfinance Activities and the Core Principles for Effective Banking Supervision*, BASEL COMMITTEE ON BANKING SUPERVISION (2010), <http://www.bis.org/publ/bcbs167.pdf>.

<sup>29</sup> Denise Dias, *Basel Blesses Microfinance*, CGAP (Oct. 19, 2010), <http://www.cgap.org/blog/basel-blesses-microfinance>.

<sup>30</sup> European Commission, Expert Report, *The Regulation of Microcredit in Europe, ENTERPRISE AND INDUSTRY* (2007), [http://ec.europa.eu/enterprise/newsroom/cfi\\_getdocument.cfm?doc\\_id=538](http://ec.europa.eu/enterprise/newsroom/cfi_getdocument.cfm?doc_id=538).

legislative standards for non-banks. 4. Create a favourable general environment for microenterprise.”<sup>31</sup>

The nonprofit World Education Australia Limited, opining on microfinance, has also adopted a quasi-commandments presentation. Its 2006 *Principles of Sustainable Microfinance*<sup>32</sup> opts for eleven precepts instead of four and for less specificity than what the European Commission endorses. Among its Principles are generalizations like “Microfinance is a powerful instrument against poverty” and “Microfinance means building financial systems that serve the poor,”<sup>33</sup> along with more specific stances: World Education Australia Limited, like the European Commission, perceives interest rate caps as detrimental;<sup>34</sup> it recommends that governments only enable, rather than provide, financial services.<sup>35</sup>

#### 4. Comprehensive National Laws

Legislation enacted around the world has undertaken to regulate microfinance. The World Bank notes “legislation and regulation initiatives” in South Africa, Zambia, Uganda, Malawi, Nepal, Bangladesh, Bosnia, Georgia, Moldova, and Ukraine, all installed before 1999.<sup>36</sup> More recently, the Central Bank of Nigeria in 2011 updated its 2005 *Microfinance Policy Framework for Nigeria*;<sup>37</sup> the Microfinance Act, addressing deposit-taking institutions, brought comprehensive microfinance regulation to Kenya;<sup>38</sup> the government of Rwanda adopted a National Microfinance Strategy;<sup>39</sup> and draft legislation proposed to extend the reach of the Reserve Bank of India over microfinance.<sup>40</sup>

<sup>31</sup> *Id.* at 5.

<sup>32</sup> WORLD EDUC. AUSTR., *Principles for Sustainable Microfinance* (2006), <http://www.mdf.org.rs/pdf/MF-Principles.pdf>.

<sup>33</sup> *Id.* at 1-2.

<sup>34</sup> *Id.* at 2.

<sup>35</sup> *Id.* at 3.

<sup>36</sup> van Greuning et al., *Framework*, *supra* note 20, at 1 n.3.

<sup>37</sup> Central Bank of Nigeria, *Microfinance Policy Framework for Nigeria* (2011), available at <http://www.cenbank.org/Out/2011/pressrelease/gvd/Revised%20Microfinance%20Policy%20July%2012%202011.pdf>.

<sup>38</sup> The Microfinance Act, No. 19 (2006), KENYA GAZETTE SUPPLEMENT NO. 103 §§4-10, available at <http://www.idlo.int/MF/Documents/Regulations/KENYA1.pdf>.

<sup>39</sup> Thompson, *supra* note 2, at 426 (citing United Nations Development Programme & Ministry of Finance and Economic Planning, Republic of Rwanda, *Building an Inclusive Financial Sector in Rwanda* 3 (2009), available at [http://www.undp.org.rw/Prodoc\\_U\\_NCDF\\_P73948.pdf](http://www.undp.org.rw/Prodoc_U_NCDF_P73948.pdf)).

<sup>40</sup> *The Micro Finance Institutions (Development and Regulation) Bill*, Draft Legislation (2011), available at [http://financialservices.gov.in/banking/micro\\_finance\\_institution\\_bill\\_2011.pdf](http://financialservices.gov.in/banking/micro_finance_institution_bill_2011.pdf). For an analysis of this draft statute, see Lamar Dowling, *The Indian*

### 5. An Assessment

Disaggregation—the central notion of the first-published comprehensive principles—was the right idea: on that point this Article builds on well-grounded earlier work. The World Bank has long understood that microfinance cannot be regulated in monolithic terms. Its careful delineation of tiers and cohorts correctly focused on the activities of entities rather than the still-new neologism.<sup>41</sup> Its prudential rules for banks combined attention to safety in savings with the development goal of expanding branch banking. Yet instead of providing the last word, the *Framework for Regulating Microfinance Institutions* triggered new proposals. Experts apparently read this compendium as a first draft.

If the World Bank had hoped for acceptance and implementation of its ideas, in hindsight it harmed its chances when it gave its splitter rulebook a lumper title.<sup>42</sup> The term “microfinance,” which the World Bank chose in 1999 when “microcredit” was still ascendant, may have made the *Framework* appear modern, ahead of the jargon curve. Its unity nevertheless undermined the drafters’ thesis: Microfinance consists of divergent activities, not just one, and is furnished by entities with different priorities. An alternative title omitting the neologism—something like “Classifications to Regulate Banking for the Poor,” admittedly a duller option—would have described the document more accurately. Even if it had had a descriptively accurate title, however, the *Framework* would have looked ripe for revision eight or nine years after its publication, when observers started to ask whether better rules governing financial institutions could have ameliorated a collapse.

#### B. Crises That Invite More Responses

The global financial crisis that began in 2007 marked a turn for microfinance. Accounts of failures and alarms among microlending institutions followed reports of setbacks in the financial sector generally. The fall of microfinance in Andhra Pradesh, a state in central India that had received large infusions of loan capital from both state and national government sources and for-profit lenders doing business in the region,

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*Microfinance Institutions (Development and Regulation) Bill of 2011: Microfinance Beginnings and Crisis and How the Indian Government is Trying to Protect Its People*, 45 INT’L LAW. 1083 (2011).

<sup>41</sup> Dividing providers into seven types within three categories made for a confusing typology, however. See van Greuning et al., *Framework*, *supra* note 20, at ii.

<sup>42</sup> See *supra* note 6 and accompanying text (contrasting lumpers with splitters).

drew particular attention.<sup>43</sup> Headlined as “India’s Major Crisis in Microlending,”<sup>44</sup> the Andhra Pradesh experience circa 2010 showcased the fragility of banking for poor clients: calamities escalate.

Borrowers who defaulted on loans in Andhra Pradesh spurred more defaults. Widespread defaulting goaded lenders to pursue loan repayment more aggressively. Reports of suicides by borrowers fueled the perception of a crisis, and a legislative response by the state government, subjecting microfinance institutions to more scrutiny and limiting what these lenders could do, struck observers as understandable but counterproductive.<sup>45</sup> According to a publication by the Brooks World Poverty Institute at the University of Manchester, inadequate regulatory mechanisms deserve much of the blame for the Andhra Pradesh devastation.<sup>46</sup>

Accounts of microfinance failure in other nations during 2009 and 2010 gave further support to Microfinance Needs Regulation, as country after country reported crises in the sector. The acronym PAR, counting the percentage of a portfolio at risk, added a worrisome note to microfinance jargon.<sup>47</sup> When a large Moroccan microfinance institution announced in June 2009 that it would merge with a rival bank its alarming PAR, more than 30%, was part of the reason:<sup>48</sup> “The global financial crisis [was] not to blame,” wrote one researcher; instead, microfinance failed in Morocco because of oversupply, which in turn caused, *inter alia*, “lack of internal controls, and substandard governance.”<sup>49</sup> Defaults, informal bailouts, and contraction of the microloan market in Bosnia during the same year spurred

<sup>43</sup> See Dowling, *supra* note 40, at 1086-88.

<sup>44</sup> Eric Bellman & Arlene Change, *India’s Major Crisis in Microlending*, Wall St. J., Oct. 29, 2010, <http://online.wsj.com/article/SB10001424052702304316404575580663294846100.html>.

<sup>45</sup> Anurag Priyadarshie & Asad K. Ghalib, Working Paper, *The Andhra Pradesh Microfinance Crisis in India: Manifestation, Causal Analysis, and Regulatory Response*, BROOKS WORLD POVERTY INST. 1, 8 (2011), <http://www.bwpi.manchester.ac.uk/resources/Working-Papers/bwpi-wp-15711.pdf>; Micro-Credit Ratings Int’l Ltd., *M-CRIL’s Comments on the Draft Microfinance Bill: A Major Step Forward for Financial Inclusion?* 1 (2011), <http://www.m-cril.com/BackEnd/ModulesFiles/Publication/M-CRIL's-comments-on-the-draft-Microfinance-Bill-July-2011.pdf>.

<sup>46</sup> Priyadarshie & Ghalib, *supra* note 45.

<sup>47</sup> PAR of more than 10% indicates a repayment crisis. See Greg Chen, Stephen Rasmussen, & Xavier Reille, *Growth and Vulnerabilities in Microfinance*, CGAP 1, 4 (2010) <http://www.cgap.org/gm/document-1.9.42393/FN61.pdf>.

<sup>48</sup> Xavier Reille, *The Rise, Fall, and Recovery of the Microfinance Sector in Morocco*, CGAP 1, 2 (2010), <http://www.cgap.org/sites/default/files/CGAP-Brief-The-Rise-Fall-and-Recovery-of-the-Microfinance-Sector-in-Morocco-Jan-2010.pdf>.

<sup>49</sup> *Id.*

commentary that inadequate regulation coupled with a surfeit of foreign-originated cash had caused unsustainable lending.<sup>50</sup>

The experience of Nicaragua during this period pointed up another need for regulation: microcredit can give rise to risky politics.<sup>51</sup> In 2008, *Movimiento No Pago* revisited an old struggle between debtors and creditors in a poverty-stricken nation when the mayor of Jalapa, a northern town, delivered a fiery speech that urged farmers to stand up against microfinance institutions to which they owed high-interest debt.<sup>52</sup> Violence ensued: protesters attempted to burn down the headquarters of a regional microlender called La Fundación para el Desarrollo de Nueva Segovia.<sup>53</sup> “I don’t pay” soon morphed from slogan into political force in Nicaragua.

In 2010 the National Assembly acceded to several “no pago” demands, including a cap on interest rates for new loans, a suspension of asset seizures from delinquent borrowers and, central to the movement, what became known as a moratorium, which gave debtors partial respite by rewriting and amortizing loan terms.<sup>54</sup> Running for re-election to the presidency in 2011, Daniel Ortega won backing from the movement when he agreed that debtors ought to stand up to their microcreditors.<sup>55</sup> Whether *Movimiento No Pago* worsened—or instead merely accompanied, or perhaps even eased—effects of the global downturn for Nicaraguans is difficult to know, but credit became less available there after 2009. More than 100,000 clients lost microcredit, and the nation’s microloan portfolio dropped from US \$420 million in 2008 to \$170 million in April 2011.<sup>56</sup>

<sup>50</sup> William K. Black, *Microcredit Accounting Control Fraud Deepens Bosnia's Nightmare*, NEW ECON. PERSPECTIVES (Mar. 11, 2012, 10:23 PM), <http://neweconomicperspectives.org/2012/03/microcredit-accounting-control-fraud-deepens-bosnias-nightmare.html>.

<sup>51</sup> See Bhaskar Chakravorti, *Does Microfinance Forestall Political Upheavals? Or Does It Cause Them?*, THE FLETCHER SCH. OF LAW AND DIPLOMACY (2010), <http://fletcher.tufts.edu/MIB/Ten-Questions/Q3-Microfinance> (reporting an interview with Kim Wilson concluding that in Nicaragua, microfinance “exacerbated an aggressive platform that [Daniel Ortega’s] political party already had”).

<sup>52</sup> Elizabeth Minchew, *A Movement to Acknowledge: The Nicaraguan Movimiento No Pago*, MICROFINANCE FOCUS (Sept. 14, 2011), <http://www.microfinancefocus.com/movement-acknowledge-nicaraguan-movimiento-no-pago>.

<sup>53</sup> *Id.*

<sup>54</sup> Sergio Guzmán, *Ley Moratoria (Moratorium Law) Passes in Nicaragua*, CENTER FOR FINANCIAL INCLUSION BLOG (Mar. 23, 2010), <http://cfi-blog.org/2010/03/23/ley-moratoria-moratorium-law-passes-in-nicaragua/>.

<sup>55</sup> David Roodman, *Think Again: Microfinance*, FOREIGN POLICY (Feb. 1, 2012), [http://www.foreignpolicy.com/articles/2012/02/01/think\\_again\\_microfinance?page=0,4](http://www.foreignpolicy.com/articles/2012/02/01/think_again_microfinance?page=0,4).

<sup>56</sup> See *6 Microfinance Crises That the Sector Does Not Want to Remember*, MICROFINANCE FOCUS (Apr. 22, 2011), <http://www.microfinancefocus.com/6-microfinance-crises-sector-does-not-want-remember>.

## II. BUT WHAT IS MICROFINANCE? RECURRING CONFUSIONS

The regulation of microfinance has been confounded by three sources of fragmentation and disarray. The first and most basic difficulty is the absence of an accepted definition of the term. The second difficulty, three conventional wisdoms that coexist in contradiction to one another, destabilizes regulatory policy. The third difficulty is present in many though not all microfinance offerings: “the double bottom line,” a sloganish goal that purports to favor simultaneous economic and social returns. Though attractive to donors and investors, this constituent of contemporary microfinance impedes coherence in regulation.

### A. Definitional Uncertainty

Regulators who would write rules for microfinance need a working definition of this newish word. The development sociologist Hans Dieter Seibel has written that he invented “microfinance” in about 1990 to expand “microcredit,” an older term, into a broader set of financial services: he was especially interested in microsavings.<sup>57</sup> Because no other writers has claimed to have coined “microfinance” and no printed instances of the term predate the early 1990s,<sup>58</sup> we can start with what Seibel has said his noun means.

To Seibel, microfinance is “that part of the financial sector which comprises formal and informal financial institutions, small and large, that provide small-size financial services to the poorer sections of the population as well as larger-size financial services to agro-processing and other small and medium rural enterprises.”<sup>59</sup> Why Seibel includes “larger-size financial services to agro-processing and other . . . rural enterprises” in his understanding of the term is obscure, but the rest of his definition resembles other attempts to say what microfinance is.<sup>60</sup>

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<sup>57</sup> Hans Dieter Seibel, *Does History Matter? The Old and the New World of Microfinance in Europe and Asia*, UNIV. OF COLOGNE 1 n.1 (2005), [http://www.microfinancegateway.org/gm/document-1.9.29698/29667\\_file\\_Does\\_History\\_Matter.pdf](http://www.microfinancegateway.org/gm/document-1.9.29698/29667_file_Does_History_Matter.pdf).

<sup>58</sup> See generally MARGUERITE S. ROBINSON, *THE MICROFINANCE REVOLUTION: SUSTAINABLE FINANCE FOR THE POOR* xxx (2001) (recounting that the author “first heard the term microfinance revolution used . . . in 1993”); David Roodman, *What is Microfinance?*, CTR. FOR GLOBAL DEV. (Oct. 11, 2010), [http://blogs.cgdev.org/open\\_book/2010/10/what-is-microfinance.php](http://blogs.cgdev.org/open_book/2010/10/what-is-microfinance.php) (examining the word along with predecessors like “microprocessor” and “microenterprise”).

<sup>59</sup> Seibel, *supra* note 57, at 1 n.1.

<sup>60</sup> See, e.g., ROBINSON, *supra* note 58, at 9-10; *What is Microfinance?*, MICROFINANCE.ORG, <http://www.microfinancegateway.org/p/site/m/template.rc/1.26.12263/> (last visited Oct. 27, 2012).

None of these proffered definitions is clear enough to hold up a platform of regulation.<sup>61</sup> To illustrate the difficulty, consider the provisional definition chosen by the Basel Committee on Banking Supervision in 2009. The Committee declared that microfinance is “the provision of financial services in limited amounts to lower income households and small, informal businesses.”<sup>62</sup> This definition appeared in a survey questionnaire that the Committee distributed to supervisory authorities in thirty-two countries. The Basel definition resembles Hans Dieter Seibel’s understanding of the word,<sup>63</sup> but whereas Seibel had only described what interested him as a researcher, the Basel survey had ambitions for regulation. It set out to determine how well the Committee’s established *Core Principles for Effective Banking Supervision*, originally published in 1997 and revised in 2006,<sup>64</sup> apply to microfinance.<sup>65</sup> Its premise casts microfinance as a subset of banking generally that might differ enough from banking to warrant its own regulations.

With this divide in mind, drawing the line between microfinance and banking becomes critical: and yet the Basel provisional definition of microfinance avoids precision. What are “limited amounts”? Surely all financial transfers have some limit. To qualify, must customers be “households,” or can individuals also participate in microfinance? How low is “lower income”? Are “small, informal businesses” different from small businesses and informal businesses?

Other instances of obscurity obstruct microfinance regulation. Some published understandings of the word presume that a microloan or micro-transfer supports entrepreneurial activity and others perceive it as coming to the recipient with no inherent restrictions on use; some recognize individuals as potential clients of microfinance while others insist that microfinance is shared by groups of poor people; some focus on the intent

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<sup>61</sup> One authority on microfinance who pre-published a book in chapter-by-chapter posts online stated the definitional problem forthrightly on his blog. “I’m seen as an expert on microfinance,” David Roodman wrote. “I’m writing a book about microfinance. I blog about microfinance. I go to microfinance conferences. So you’d think I know what microfinance is. But I’m not sure I do.” Roodman, *supra* note 58. The book is DAVID ROODMAN, *DUE DILIGENCE: AN IMPERTINENT INQUIRY INTO MICROFINANCE* (2012).

<sup>62</sup> Bank For International Settlements, *Microfinance activities and the Core Principles for Effective Banking Supervision*, BASEL COMMITTEE ON BANKING SUPERVISION 1 (2010), <http://www.bis.org/publ/bcbs175.pdf>.

<sup>63</sup> See *supra* text accompanying note 59.

<sup>64</sup> Bank For International Settlements, *Core Principles for Effective Banking Supervision*, BASEL COMMITTEE ON BANKING SUPERVISION 1 (2006), <http://www.bis.org/publ/bcbs129.pdf> [hereinafter Basel Committee].

<sup>65</sup> *Id.* at 34.

of the provider; some associate microfinance with the amelioration of social distress.<sup>66</sup>

These divergent understandings and provisional definitions undermine microfinance regulation by sowing uncertainty about the identity of providers and clients, the transactions that fall under the aegis of a rule, and the benefits or goals that the regulatory scheme seeks to advance. Imprecision, self-refuting jargon, and inclusion of entities that may or may not align with governing legal categories come together in a *mélange*.

### B. Conventional Wisdoms

Attitudes about microfinance as a tool for enhancing economic and social development align with attitudes about its regulation. Three clusters of conventional wisdom have emerged in contemporary discussion. The first celebrates microfinance as a source of spontaneous wealth. Applied to regulation, this stance worries that too many rules will impede innovation and dampen the best hopes of the poor.<sup>67</sup> The second genre harbors an opposite worry, perceiving microfinance to be a source of dangerous debt, deeper poverty, or even violent upheaval. It favors more controls. Attempting to combine the optimism of the first with the pessimism of the second, the third genre of conventional wisdom on microfinance finds opportunity and danger combined.<sup>68</sup> The three genres swing in oscillation.

#### 1. Optimism

Microfinance reached its apogee of prestige when Muhammad Yunus and the bank he founded, Grameen, shared the Nobel Peace Prize in 2006.<sup>69</sup> The Norwegian Nobel Committee drew a novel connection between a for-

<sup>66</sup> See generally Roodman, *supra* note 58 (reporting multiplicity).

<sup>67</sup> See, e.g., Christen et al., *supra* note 25, at 4 (recommending “enabling” regulation to encourage new entrants into the microfinance market); B. Seth McNew, *Regulation and Supervision of Microfinance Institutions: A Proposal for a Balanced Approach*, 15 LAW. & BUS. REV. AMERICAS 287, 288 (2009) (worrying that regulation of microfinance providers “can easily become overbearing, and the cost of compliance may become so high as to defeat the ultimate goal of . . . giving the world’s poorest citizens access to financial services.”).

<sup>68</sup> I advert to the orientalist notion that “crisis” in Chinese combines the ideograms for danger and opportunity. See Cecil Adams, *Is the Chinese Word for “Crisis” a Combination of “Danger” and “Opportunity”?* THE STRAIGHT DOPE (Nov. 3, 2000), <http://www.straightdope.com/columns/read/2363/is-the-chinese-word-for-crisis-a-combination-of-danger-and-opportunity> (concluding that the suggestion is mostly inaccurate).

<sup>69</sup> *The Nobel Peace Prize for 2006*, NOBELPRIZE.ORG (Oct. 13, 2006), [http://www.nobelprize.org/nobel\\_prizes/peace/laureates/2006/press.html](http://www.nobelprize.org/nobel_prizes/peace/laureates/2006/press.html).



profit bank and world peace when it linked microcredit with the aim of its prize. "Lasting peace cannot be achieved," wrote the Committee, "unless large population groups find ways in which to break out of poverty. Microcredit is one such means."<sup>70</sup>

Microfinance had achieved acclaim before its 2006 triumph. Former U.S. President Bill Clinton remarked in 2002 that Muhammad Yunus "long ago should have won the Nobel Prize. I'll keep saying that until they finally give it to him."<sup>71</sup> The Consultative Group to Assist the Poor was formed in 1995 to expand access to financial services for so-called "unbankable persons" everywhere in the world.<sup>72</sup> In 2004, the United Nations announced that 2005 would be the International Year of Microcredit.<sup>73</sup> Scholarship in the field took off with the publication of *The Microfinance Revolution*,<sup>74</sup> documenting and celebrating microfinance as central to sustainable economic development.

For enthusiasts, microfinance has retained its 2006-vintage luster. When in 2009 Muhammad Yunus won the Presidential Medal of Freedom, the highest honor given to civilians in the United States, President Obama praised his Grameen Bank for "lifting millions of people from poverty with microloans."<sup>75</sup> Researchers continue to report that this category of banking builds wealth.<sup>76</sup> Microlending not only ameliorates poverty and spurs domestic economic development, the optimists declare, but also installs

<sup>70</sup> *Id.*

<sup>71</sup> William Jefferson Clinton, Former President of the United States, Speaker at the University of California, Berkeley (Jan. 29, 2002) (transcript available at <http://www.berkeley.edu/news/features/2002/clinton/clinton-transcript.html>).

<sup>72</sup> Edward Bresnayan, Case Study, *Addressing Challenges of Globalization: An Independent Evaluation of the World Bank's Approach to Global Programs*, THE WORLD BANK OPERATIONS EVALUATION DEPARTMENT vii (2004), [http://lnweb90.worldbank.org/oed/oeddoclib.nsf/24cc3bb1f94ae11c85256808006a0046/c29f384f74e0ec5785256f240050d440/\\$FILE/gppp\\_cgap\\_wp.pdf](http://lnweb90.worldbank.org/oed/oeddoclib.nsf/24cc3bb1f94ae11c85256808006a0046/c29f384f74e0ec5785256f240050d440/$FILE/gppp_cgap_wp.pdf).

<sup>73</sup> INTERNATIONAL YEAR OF MICROCREDIT 2005, <http://www.un.org/events/microcredit/> (last visited Oct. 30, 2012).

<sup>74</sup> ROBINSON, *supra* note 58; MARGUERITE S. ROBINSON, *THE MICROFINANCE REVOLUTION, VOLUME II: LESSONS FROM INDONESIA* (2002).

<sup>75</sup> President Barack Obama, Remarks By President Obama At The Medal Of Freedom Ceremony (Aug. 13, 2009) (transcript available at <http://www.muhammadyunus.org/In-the-Media/remarks-by-president-obama-at-the-medal-of-freedom-ceremony/>).

<sup>76</sup> Alan M. White, *Credit and Human Welfare: Lessons from Microcredit in Developing Nations*, 69 WASH. & LEE L. REV. 1093, 1095-96 (2012) (reporting on "[e]xtensive empirical research"); Inter-American Development Bank, *IDB Urges Microfinance Industry to Reach Out to Millions of Underserved People in Latin America and the Caribbean*, IADB.ORG (Oct. 1, 2009), <http://www.iadb.org/en/news/news-releases/2009-10-01/idb-urges-microfinance-industry-to-reach-out-to-millions-of-underserved-people-in-latin-america-and-the-caribbean,5697.html>.

ancillary gains: it opens philanthropy to a wider circle of donors;<sup>77</sup> enhances the education of youngsters in the United States;<sup>78</sup> keeps poor families together and helps prevent illegal border crossings;<sup>79</sup> and eases the ravages of malnutrition.<sup>80</sup> The Nobel Peace Prize citation praised microlending for making women better off;<sup>81</sup> numerous writers agree.<sup>82</sup>

The global financial crisis presented a challenge to optimism about microfinance that enthusiasts have found sobering but not daunting. If microfinance ameliorates poverty, then by hypothesis a world grown poorer following economic collapse needs more of it. Because loan capital becomes less available in a contracted economy, policymakers can ease the downturn by making lending and borrowing more available. Poorer borrowers benefit from lower interest rates; increases in supply lower prices; accordingly, the optimist prescription urges policymakers to invite more providers into the microloan market.<sup>83</sup>

<sup>77</sup> Tracy Turner, *Planting Seeds of Hope*, COLUMBUS DISPATCH, Apr. 13, 2007, at 1F.

<sup>78</sup> Sacha Pfeiffer, *Tale of Microloans Urges Kids to Generosity*, THE BOSTON GLOBE, Mar. 10, 2008, at 1D.

<sup>79</sup> Devon Roepcke, “Should I Stay or Should I Go?”: Preventing Illegal Immigration By Creating Opportunity in Mexico Through Microcredit Lending, 38 CAL. W. INT’L L.J. 455, 460 (2008); Lourdes Medrano, *Micro-lending Efforts in Mexico Helps Poor Families Stay Home*, Ariz. Daily Star, June 17, 2007, at A1.

<sup>80</sup> Jessica Deihl, *Microfinance in Emerging Markets: The Effects of the Current Economic Crisis and the Role of Securitization*, 6 AM. U. WASH. C. BUS. L. BRIEF 37, 38-39 (2009), available at [http://www.wcl.american.edu/blr/documents/Spring09\\_Microfinance.pdf](http://www.wcl.american.edu/blr/documents/Spring09_Microfinance.pdf) (reporting a study in Bangladesh).

<sup>81</sup> See source cited *supra* note 69.

<sup>82</sup> See Susy Cheston & Lisa Kuhn, *Empowering Women through Microfinance*, MICROCREDIT SUMMIT CAMPAIGN (2002), <http://www.microcreditsummit.org/papers/empowerment.pdf> (summarizing benefits); see also Anita Bernstein, *Pecuniary Reparations Following National Crisis: A Convergence of Tort Theory, Microfinance, and Gender Equality*, 31 U. PA. J. INT’L L. 1, 31 (2009) (noting praise for microcredit as a feminist instrument). Studies consistently report that female microborrowers are more likely than non-borrowers to practice contraception. Charlotte E. Lott, *Why Women Matter: The Story of Microcredit*, 27 U. PITT. J. L. & COM 219, 227 (2009) (summarizing findings). See generally Salil Tripathi, *Microcredit Won’t Make Poverty History*, GUARDIAN (Oct. 17, 2006), <http://www.guardian.co.uk/business/2006/oct/17/businesscomment.internationalaidanddevelopment?INTCMP=SRCH> (arguing that “to appreciate Grameen’s real worth, we need to look at its role in empowering women. That is its real success, and for achieving this in a conservative, largely rural society such as Bangladesh, where Islamic fundamentalism is on the rise, Dr. Yunus deserves his Nobel prize.”).

<sup>83</sup> See, e.g., Michael Schlein & Michael Chu, *Microfinance Goes Public*, FORBES.COM (Apr. 30, 2010, 5:40 AM), <http://www.forbes.com/2010/04/30/india-microfinance-sks-ipo-markets-emerging-markets-accion.html> (praising IPOs for microfinance institutions as a source of wealth).

## 2. Pessimism

“The idea of borrowing one’s way out of poverty is passing strange,” mused Judge Richard Posner in 2005,<sup>84</sup> joining a cohort of skeptics who expressed doubts well before the twenty-first century’s first global downturn. Borrowing in contrast to saving—or microcredit in contrast to microfinance—has received the brunt of criticism. One careful review of published studies circa 2002 found microcredit no better than “other poverty alleviation models. Providing money to a population through almost any means will ordinarily have a short-term positive impact on poverty[,]” but the effect dissipates “once the funds are expended.”<sup>85</sup> Other pre-downturn skeptics argued that microlending benefits only the richer poor,<sup>86</sup> that enthusiasts have overstated gains to women from microlending,<sup>87</sup> and that microcredit is best understood as a salve that eases the pain of “trade liberalization, deregulation and privatization” imposed on the world’s poor by foreign intervenors.<sup>88</sup>

A global financial crisis that reached full force only two years after Yunus and his bank shared the Nobel Prize strengthened a view among pessimists, parallel to that of optimists,<sup>89</sup> that they had been right all along. Critics who had spoken against microcredit before 2007 returned with more ammunition.<sup>90</sup> Whereas earlier objections had taken a mild tone—mostly

<sup>84</sup> See Bernstein & Seibel, *supra* note 18, at 89 n.71.

<sup>85</sup> Celia R. Taylor, *Microcredit as Model: A Critique of State/NGO Relations*, 29 SYRACUSE J. INT’L L. & COM. 303, 326 (2002).

<sup>86</sup> Thomas Dichter, *Hype and Hope: The Worrisome State of the Microcredit Movement*, MICROFINANCE GATEWAY (Mar. 24, 2006), <http://www.microfinancegateway.org/p/site/m/template.rc/1.26.9051> (“The microcredit paradox is that the poorest people can do little productive with the credit, and the ones who can do the most with it are those who don’t really need microcredit, but larger amounts with different (often longer) credit terms.”).

<sup>87</sup> Dyal-Chand, *supra* note 18, at 221 (objecting to the Grameen mode of collecting on its loans); Gina Neff, *Microcredit, Microresults*, 74 LEFT BUS. OBSERVER 1, 4-5 (1996), available at <http://www.leftbusinessobserver.com/Micro.html> (criticizing microcredit programs for encouraging borrowers to compete only with other women in low-wage entrepreneurial dead ends).

<sup>88</sup> Walden Bello, *Microcredit, Macro Issues*, THE NATION, Oct. 30, 2006, <http://www.thenation.com/article/microcredit-macro-issues> (referencing the World Bank).

<sup>89</sup> See *supra* note 83 and accompanying text.

<sup>90</sup> See, e.g., THOMAS W. DICHTER, WHAT’S WRONG WITH MICROFINANCE? (2007); Thomas W. Dichter, *Too Good to Be True*, 32 HARV. INT’L REV. (May 1, 2010), available at <http://hir.harvard.edu/women-in-power/too-good-to-be-true>; MILFORD BATEMAN, WHY DOESN’T MICROFINANCE WORK? THE DESTRUCTIVE RISE OF LOCAL NEOLIBERALISM (2010) (describing microfinance as advantageous to investors and international standard-setters). On doubts about microfinance in the context of trafficking, see Katherine Driscoll, *Microcredit: Not Yet a Panacea to End Trafficking in Women*, 13 U. PA. J. BUS. L. 275, 287

just skeptical that loans cure poverty and suggesting that claims of big effects were exaggerated—post-downturn critiques have found malfeasance in microfinance.<sup>91</sup> In this perspective, choices like awarding a big prize to a bank and declaring a calendar year of microcredit were not mere judgment-calls akin to admiring celebrities more than they deserve: they generated new harms.

Prestige from the 2006 award directly preceded the initial public offering of the controversial microfinance institution Banco Compartamos in Mexico in 2007, a launch that drew more than a billion United States dollars in market capitalization on its closing date.<sup>92</sup> Boosterish books published in 2005 and 2006 that bore optimistic titles—*Untapped, Make Poverty Business, The 86% Solution, The Fortune at the Bottom of the Pyramid*—preached microfinance as a tool for anyone, rich or poor, to gain wealth.<sup>93</sup> Because loans are more profitable than savings,<sup>94</sup> it is likely that that touting microfinance encouraged wealth-pursuers, providers and customers alike, to accrete unsustainable levels of debt. Increased economic vulnerability also makes it easier for lenders to get away with overcharging and otherwise injuring poor borrowers.<sup>95</sup>

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(2010), available at <https://www.law.upenn.edu/journals/jbl/articles/volume13/issue1/Dri%20scoll13U.Pa.J.Bus.L.275%282010%29.pdf>. See also Rebecca Farrer, *Exploring the Human Rights Implications of Microfinance Initiatives*, 36 INT'L J. LEGAL INFO. 447, 459 (2008) (reporting that women with HIV may be especially ill served by group-loan models of microfinance) (citations omitted).

<sup>91</sup> See, e.g., HUGH SINCLAIR, *CONFESSIONS OF A MICROFINANCE HERETIC: HOW MICROLENDING LOST ITS WAY AND BETRAYED THE POOR* (2012) (arguing that microfinance rapidly became a locus of gouging by commercial banks); BATEMAN, *supra* note 90.

<sup>92</sup> See Dragan Loncar, Christian Novak & Svetlana Cicmil, *Global Recession and Sustainable Development: The Case of Microfinance Industry in Eastern Europe*, MICROFINANCEGATEWAY.ORG (Sept. 2009), <http://www.microfinancegateway.org/gm/document-1.9.39138/MICROFINANCE%20PAPER-%20FINAL%20VERSION.pdf> (finding a connection between the two).

<sup>93</sup> Aneel Karnani, *Romanticizing the Poor*, 7 STAN. SOC. INNOVATION REV. 38 (2009), <http://www.ssireview.org/pdf/RomanticizingthePoor.pdf>.

<sup>94</sup> See *infra* Part III.

<sup>95</sup> Sebastian Strangio, *Is Microfinance Pushing the World's Poorest Even Deeper Into Poverty?*, THE NEW REPUBLIC (Dec. 14, 2011, 12:00 AM), <http://www.tnr.com/article/world/98499/microfinance-drive-poverty> (quoting an activist based in Dhaka: "Microcredit is discrimination against the poor, it doesn't empower. It's total nonsense."); Devinder Sharma, *Micro-finance Institutions on a Looting Spree: Making Profits From Poverty*, GROUND REALITY (Nov. 25, 2009, 11:52 AM), <http://devinder-sharma.blogspot.com/2009/11/micro-finance-institutions-on-looting.html> ("All that micro-finance institutions are doing now is [replacing] moneylenders. Micro-finance institutions are also extracting their pound of flesh.").

A milder expression of pessimism notes that microfinance appears neither necessary nor sufficient for the economic advancement of a nation. Anne Welle-Strand, Kristian

### 3. Seeking the Center

Valuable writings on microfinance have eschewed the extremes of cheerleading at one end and fretting at the other. These works include a celebrated book published in stages on the Internet, with opportunities for readers to weigh in on draft chapters;<sup>96</sup> explanations of how difficult it is to know whether microfinance initiatives have any effect and reviewing the small set of controlled studies;<sup>97</sup> and distinctions between microsavings and microcredit, the former type of microfinance being safer and more necessary.<sup>98</sup> These publications work in a middle ground that is different from a stance we may call centrism, which aspires to a middling level of enthusiasm for microfinance.

After optimists documented the problem of poor people cut off from access to banks and pessimists focused on various adverse consequences associated with microfinance, this hope for synthesis started to manifest in generalizations about microfinance in around 2009. Expand but add safeguards, said the newest conventional wisdom. Make more loans, but worry about abuses. Temper pessimism with optimism and optimism with pessimism.<sup>99</sup>

Two difficulties with centrism are pertinent to the challenge of regulating microfinance. First, there is no *a priori* reason to suppose that correctness necessarily lies midway between two policy positions perceived as polar

Kjøllesdal, & Nick Sitter, *Assessing Microfinance: The Bosnia and Herzegovina Case*, 8 *MANAGING GLOBAL TRANSITIONS* 145, 150-51 (2010) (noting that Vietnam and South Korea made significant economic progress with little microfinance, while Bangladesh, Bolivia, and Indonesia, which experienced an “influx of microcredit,” fared worse at alleviating poverty) (citation omitted).

<sup>96</sup> ROODMAN, *supra* note 61.

<sup>97</sup> *A Partial Marvel: Microcredit May Not Work Wonders But It Does Help The Entrepreneurial Poor*, *THE ECONOMIST* (July 16, 2009), [http://www.economist.com/node/14031284?story\\_id=14031284](http://www.economist.com/node/14031284?story_id=14031284); Robin G. Isserles, *Microcredit: The Rhetoric of Empowerment, the Reality of “Development as Usual,”* 31 *WOMEN’S STUD. Q.* 38 (2003).

<sup>98</sup> The Yale University economist Dean Karlan, acclaimed for empirical work on the effects of microfinance, told a journalist that concerns about “irrational exuberance” with respect to borrowing should not obscure the need to expand microsavings. See Strangio, *supra* note 95.

<sup>99</sup> See, e.g., VIKRAM AKULA, *A FISTFUL OF RICE: MY UNEXPECTED QUEST TO END POVERTY THROUGH PROFITABILITY* (2010) (defending for-profit microlending while condemning microlenders that charge the maximum interest rates that loan markets will bear); Beatriz Armendáriz & Marc Labie, *Introduction and Overview: An Inquiry Into the Mismatch in Microfinance*, in *THE HANDBOOK OF MICROFINANCE* 3 (Beatriz Armendáriz & Marc Labie eds., 2011) (“Microfinance . . . is seen by some as a magic wand against poverty that is supposed to solve it all. For others, microfinance is no more than a new wave of usurious practices reframed and glorified.”).

opposites.<sup>100</sup> The optimistic and the pessimistic view of microfinance could each be wrong in the sense of not going far enough, rather than going too far. Diluting one with the other would yield worse results than would hewing to the (correct) extreme. Second, neither in isolation nor as constituents of a dialectic do optimistic or pessimistic perspectives on microfinance answer the questions of which microfinance rules are best and whether regulation ought to discourage or encourage particular financial practices.

Debates about microfinance return to the oscillation between exuberance and worry found in debates about what might be called macrofinance, the larger environment of domestic and transnational consumer banking. Good-faith disagreement about consumer-finance regulation (good-faith, that is, in the sense of disinterested pursuit of socially optimal rules rather than a quest for personal or political advantage)<sup>101</sup> has also shuttled between laissez-faire and sterner controls. Leaving the market alone seems like a good idea until defaults and insolvencies mount. Regulating tightly seems like a good idea until lack of access to capital appears to oppress providers or customers. Centristism between optimism and pessimism seems like a good idea until constituencies demand to know what exactly the rules are trying to install while partisans of the polar stances—laissez-faire or sterner controls—perceive any middle ground as misguided appeasement. The problem of warring ideological cohorts is thus familiar from the larger debate about financial regulation.

In microfinance the problem has worse effects because comprehensive proposals to regulate microfinance are formed at a maximum distance from clients. Consumer banking in the United States may suffer from regulatory capture, excess influence by banks over Congress and state governments, or inadequate enforcement of existing regulation, but at least rule-writers live in the same country as consumers and thus face some accountability. Best-practices statements about microfinance of the CGAP or Basel stripe get written by remotely situated researchers who do not suffer when their recommendations fail. These authors might be disinterested in the research-centered sense of the adjectives “neutral” or “impartial”; but whereas disinterestedness is good for the assessment of interventions, it can make proffered new rules worse when it insulates initiators from consequences.

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<sup>100</sup> BO BENNETT, LOGICALLY FALLACIOUS: THE ULTIMATE COLLECTION OF OVER 300 LOGICAL FALLACIES (2012) (identifying the argument to moderation or *argumentum ad temperantiam* as synonymous with “middle ground, false compromise, gray fallacy, golden mean fallacy, fallacy of the mean, [and] splitting the difference”).

<sup>101</sup> See *supra* note 8.

Comprehensive national legislation avoids this infirmity because codifiers live with what they promulgate. Yet by addressing “microfinance” rather than financial institutions, these statutes exempt the middle-income and wealthy citizenry from what the rules deliver. Experiences with federal transfer payments in the United States—Medicare and Social Security for citizens in the mainstream and “welfare” and food stamps for the marginalized poor—point up the danger of stigma and isolation raised by provisions that affect only the very poor.<sup>102</sup> Once “microfinance” sticks as a label, this segment of consumer credit becomes a regulatory ghetto, outside the mainstream.

The lack of consequences for prosperous stakeholders makes microfinance more vulnerable to variations in exuberance and worry. Centrism also fails to mitigate extreme shifts because of the same problem: a gap between the prescribers and the prescribed-to. Separated from effects, centrist observers add mainly dilution and vagueness to a policy debate.

In sum, because regulators who draft provisions about microfinance live far from the results of their efforts, the tempering effects of lived experience are less available to ease the ideological extremes of optimism and pessimism and what may be the thoughtless compromises of centrism. For rule-writers who join the optimistic, pessimistic, or centrist teams, microfinance offers a playing field for predilections and ideologies. This distance helps to explain the proliferation of microfinance principles and compendia: the powerlessness that accompanies poverty means that people at risk of harm from interventions cannot silence an intervenor. Nor do they have much voice in the debate. In sectors of the consumer-credit economy that reach the middle class (credit cards, automobile financing), reformers would be more inhibited by modesty. Optimists, pessimists, and centrists who would normally have to negotiate with and learn from one another in ideological competition can remain separated when opining on microfinance. Relatively marginal perspectives face low barriers to entry.<sup>103</sup> Diversity in ideas may make for lively reading, but regulation that can be enacted and enforced needs a foundation in politics on the ground.

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<sup>102</sup> See generally Jennifer Stuber & Mark Schlesinger, *Sources of Stigma for Means-Tested Government Programs*, 63 SOC. SCI. & MED. 933 (2006) (noting an association between means-testing and stigma in U.S. transfer programs).

<sup>103</sup> The large majority of what is written about microfinance gets published only online. Peer review, editorial oversight, and the market of consumers who pay for what they read all hold relatively little sway in policy debates.

### C. The Oxymoron of a “Double Bottom Line”

Like “microfinance” itself, “the double bottom line” makes a useful point at the expense of clarity and coherence. This coinage refers to simultaneous pursuit by an entity of pecuniary earnings and social enhancements.<sup>104</sup> Terms like “social entrepreneurship” for newly formed, progress-minded entities and “cause marketing” for commercial promotions that promise to give returns to charity illustrate the double bottom line as propounded by for-profit businesses.<sup>105</sup>

Microfinance entities—banks and charities alike—have expressed fondness for this dual pursuit, emphasizing the microcredit subset of microfinance.<sup>106</sup> The notion that small loans to poor borrowers yield both earnings for the lender and gains for the nearby community is foundational to contemporary microfinance. It underlay the Nobel Peace Prize award divided in 2006 between a bank founder and the entity he started.<sup>107</sup> The two bottom lines really do have ground in common. Pecuniary earnings and social enhancements overlap whenever gains in wealth support positive cultural change in a community. As one scholar has argued, the two priorities come together in “microfinance organizations that affirmatively seek to change culturally-based attitudes that are antithetical to broad development principles.”<sup>108</sup>

Few would quarrel with doing good while doing well, and the truism that human actors pursue more than one goal at a time is not the problem with the double bottom line. The difficulty lies in an implicit commitment to precision that cannot be achieved. Traditional for-profit ledgers measure the financial side of a bottom line relatively easily by subtracting costs from revenues. The social-enhancement ledger is less amenable to quantification.

Measurement technologies do exist, to be sure. In her strong defense of social entrepreneurship, approving of undertakings by for-profit businesses to “harness[] innovation, people, and resources to develop an enterprise that

<sup>104</sup> Jerr Boschee, *Doing Good While Doing Well*, PITT. POST-GAZETTE, Oct. 19, 2008, at G1.

<sup>105</sup> Brakman Reiser, *supra* note 11, at 34-41.

<sup>106</sup> See Drew Tulchin, *Microfinance’s Double Bottom Line: Measuring Social Return for the Microfinance Industry*, SOCIAL ENTERPRISE ASSOCIATES 7 (2003), [http://www.microfinancegateway.org/gm/document-1.9.27273/13947\\_13947.pdf](http://www.microfinancegateway.org/gm/document-1.9.27273/13947_13947.pdf) (“Effectively gauging and then reporting financial and social activities—managing both as the Double Bottom Line (DBL)—positions microfinance institutions as a solution. Few fields in development or commerce emphasize both economic and social performance as strongly as microfinance.”) (emphasis in original).

<sup>107</sup> See *supra* note 69 and accompanying text.

<sup>108</sup> Cao, *supra* note 9, at 988.



is self-sustaining, makes money, and solves a social problem,”<sup>109</sup> Janet Kerr surveys the tools that can gauge social impact and finds them bounteous. Innovators, she notes, have come up with taxonomies of metrics, guidelines that a board of directors can apply to the socially minded entity it governs, and a framework for managers to use while pursuing social entrepreneurship.<sup>110</sup> It would no longer be fair to ascribe feel-good vacuity to the social half of the double bottom line now that experts have applied themselves to the task of measurement. Nevertheless, to date “no universal standard”<sup>111</sup> has emerged to gauge the social profit (or loss) of a double-bottom-line venture.

“The double bottom line” must remain an oxymoron. Even if measurements should improve to the point of consensus about how to quantify the social gains of an entity, a bottom line tolerates no bifurcation. It announces finality. For any enterprise there can be only one. Accounting standards may in the future evolve to measure the sustainability or social enhancements achieved by a for-profit business, and also to recognize that gains at one side of the ledger do not necessarily come at the expense of the other;<sup>112</sup> but it is hard to imagine how any measure might frame one conclusion about corporate health that matters just as much as a separate conclusion. Metrics amenable to counting social gains—which have not yet taken hold—necessarily differ from the ones that count pecuniary profit. They do not lie on the same axis.

### III. DISAGGREGATION, FIRST PASS: MICROFINANCE AS BANKING FOR POOR PEOPLE

Replacing “microfinance” with “banking for poor people” as an object of regulatory attention advances at least three ends. First, it disaggregates a dense Latinate term into pertinent constituents. Second, it makes the regulatory effort simpler and more intelligible. Third, it puts a vulnerable sector into the foreground for regulators.

As a label, “microfinance” distracts from the work of identifying risks, activities, and participants in the sector they are addressing. This Part substitutes a cumbersome phrase—“banking for poor people”—precisely because this alternative is too clunky to become jargon. “Banking for poor

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<sup>109</sup> Janet E. Kerr, *Sustainability Meets Profitability: The Convenient Truth of How the Business Judgment Rule Protects a Board's Decision to Engage in Social Entrepreneurship*, 29 CARDOZO L. REV. 623, 633 (2007).

<sup>110</sup> *Id.* at 644-53.

<sup>111</sup> Tulchin, *supra* note 106, at 7.

<sup>112</sup> Kerr, *supra* note 109.

people” also aids the task of disaggregation by inviting regulators to think about demand for, not just the supply of, the services they oversee.<sup>113</sup> One noun in the phrase refers to providers and the other to customers.

After “banking for poor people” becomes the object of regulatory effort, the desirability of simplicity becomes more apparent. Complexity is of course hard to avoid in rules governing banking. Other things being equal, however, these rules function better when they are relatively easy to follow.<sup>114</sup> At least at the preliminary level where this Article makes its recommendations, opportunities for more clarity emerge through inquiry into what customers want from banking for poor people.

Researchers know the answer. Foremost, poor people want a safe place to store their money.<sup>115</sup> They also want access to credit.

#### A. Support For Savings

“Portfolios of the poor,” a jocular-sounding title of a book whose point is not facetious,<sup>116</sup> notes the near ubiquity of private property. Although millions of people in the world are poor, few adults possess nothing. What the poor categorically lack are secure places to store what they own, and when surveyed they rank this need above others.<sup>117</sup> Savings that can be kept relatively safe can smooth fluctuations in income, provide continuity during emergencies or occasions of new opportunity, and allow individuals to share life-cycle events like funerals and weddings in their communities. People need credit only some of the time, savings all of the time.<sup>118</sup>

The global downturn that began in 2008, reckoning with loan money gone bad, harmed the relative prestige of microcredit within microfinance. Donors and governments turned their attention away from debt and toward savings. In early 2010, the Gates Foundation announced a \$38 million initiative to promote savings in 18 microfinance institutions.<sup>119</sup> In 2012

<sup>113</sup> See *infra* Part III.B.2.

<sup>114</sup> Joe Nocera, *The Simplicity Solution*, N.Y. TIMES, May 29, 2012, at A23 (applying this generalization to financial regulation).

<sup>115</sup> ROBINSON, *supra* note 58.

<sup>116</sup> DARYL COLLINS ET AL., PORTFOLIOS OF THE POOR: HOW THE WORLD’S POOR LIVE ON \$2 A DAY (2009).

<sup>117</sup> Joshua Haynes & Mariah Levin, *Debating the Future of Savings-Led Microfinance: A Summary Paper of the Microfinance From Below Conference* (2009), [http://fletcher.tufts.edu/CEME/research/~media/Fletcher/Microsites/CEME/newpdfs/CEME\\_MFSavingsConferenceReport\\_03-2009.ashx](http://fletcher.tufts.edu/CEME/research/~media/Fletcher/Microsites/CEME/newpdfs/CEME_MFSavingsConferenceReport_03-2009.ashx) (referencing the research of Marguerite S. Robinson).

<sup>118</sup> Marguerite Robinson & Graham A.N. Wright, *Mobilising Savings*, in SAVINGS—AN ESSENTIAL SERVICE FOR THE POOR 25, 26 (2009), [http://www.microsave.org/sites/files/technicalBriefs/briefingNotes/Savings\\_Booklet.pdf](http://www.microsave.org/sites/files/technicalBriefs/briefingNotes/Savings_Booklet.pdf).

<sup>119</sup> *A Better Mattress: Microfinance Focuses On Lending. Now The Industry Is Turning*

Oxfam, the British charity, declared on its blog: “Forget microcredit: microsavings work much better,” going on to describe the operations of its initiative Savings for Change.<sup>120</sup>

Regulators thus have an array of proposals, experiences, and pilot programs to draw on as they consider what to support through rule-based facilitating. Although challenges to safe savings will vary from region to region, a few points of common concern recur and provide a starting point for savings reform. Like other recommendations in this Article, savings-supportive regulatory priorities can be pursued and implemented without use of the word microfinance.

### 1. *Reconsidering Prudential Rules*

Financial institutions that seek to take deposits must comply with regulations focused on whether capital reserves are secure enough to let customers withdraw money at will. This posture regards deposit-taking as riskier than loan-making, and prudential regulation thus burdens savings banks more than lenders that dispense microcredit. This attention to safety is incomplete. Institutions that meet prudential standards are less likely to fail than those that do not, but when poor people face the danger of having no savings bank at all, aggregate-level safety diminishes.

Addressing this problem, reformers have offered suggestions to lower cash-reserve minimums to qualify for a bank charter while keeping savings accounts secure enough for poor customers.<sup>121</sup> The tradeoff is perilous—at the prudential level it treats poor depositors worse than prosperous ones—yet it warrants consideration as a source of welfare for a vulnerable cohort. At a minimum, rule-writers ought to ask whether existing prudential rules have made low-income prospective depositors better or worse off.

### 2. *Linkages*

Foreclosed from institutional accounts to hold their cash deposits, the unbankable poor resort to self-help, which at its most sophisticated takes the form of group-based saving. Unbankable persons who unite in these alliances know what they are missing: “security, convenience, liquidity, access to loans, choice of demand driven products, helpful and respectful

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*To Deposits*, THE ECONOMIST (Mar. 11, 2010), <http://www.economist.com/node/15663834> [hereinafter *A Better Mattress*].

<sup>120</sup> Duncan Green, *Forget Microcredit: Microsavings Work Much Better*, OXFAM (Apr. 5, 2012, 9:12 AM), <http://www.oxfamblogs.org/fp2p/?p=9489>.

<sup>121</sup> See McNew, *supra* note 67, at 288 (noting the tradeoff); Bernstein & Seibel, *supra* note 18, at 83-84 (noting recommendations made by the Alliance for Financial Inclusion).

service, confidentiality, and returns,” reported Marguerite Robinson, author of *The Microfinance Revolution*, summarizing her field work.<sup>122</sup> “None of us wants to bank with groups,” researcher Malcolm Harper has noted wryly, “but we are happy to promote that the poor should use them forever.”<sup>123</sup>

Linkage banking presents a partial solution to this fragility by enhancing connections between group-based savings and rotating credit associations and formal institutions. Pioneer initiatives, installed first in Indonesia and later in India, invented linkage banking when they identified small groups of savers (twenty or fewer people, predominantly women, in both countries) and helped them connect with banks, usually delivering advice as well as accounts in the name of the group.<sup>124</sup> Linkage banking in India, where these clusters of customers are called “self-help groups,” has fostered microcredit incidentally while emphasizing microsavings.<sup>125</sup> Researchers studying India report positive economic effects.<sup>126</sup> To the extent that self-help groups have fared worse since the global downturn,<sup>127</sup> these consequences originate in loans rather than savings; linkage banking remains promising as a source of enhanced savings.

Access to formal institutions increases the prospects of poor savers to earn interest on their money, reach additional capital in the form of credit, and gain formal legal protection of their holdings.<sup>128</sup> What regulators can do to support linkage banking ranges from engagement by a large national bank with or without the mediation of nonprofit organizations, as in India, to more modest innovations. For example, bank rules could be amended to permit a wider range of names on the account.

### 3. *New Types of Savings Accounts*

Lack of access to bank accounts is the major impediment to safe savings for the poor, but other obstacles diminish the quantity of money held by low-income depositors in banks. The poor are by hypothesis short of cash. Saving money precludes spending it, and so any commitment individuals may have to save their money means a reduction in whatever utility they obtain from consumption. The pleasure of corruption can be short-lived.

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<sup>122</sup> See Haynes & Levin, *supra* note 117, at 3.

<sup>123</sup> *Id.*

<sup>124</sup> Bernstein & Seibel, *supra* note 18, at 83-84.

<sup>125</sup> *Id.*

<sup>126</sup> *Id.* at 84 (reporting on findings by Seibel and the central bank of India).

<sup>127</sup> See *supra* notes 43-45 and accompanying text (noting the local collapse of microlending in 2010).

<sup>128</sup> See *supra* note 124 and accompanying text.

Tempted to spend money that they could otherwise deposit in the bank accounts they have, people might not save as much as they think they want to. That individuals desire to prevent themselves from consuming their spare cash is manifested by the popularity of voluntary barriers to spending.<sup>129</sup>

Depositors voluntarily accept—and even pay for—“commitment savings products” that make their holdings less liquid. This category offers options that bank regulators could encourage in an effort to enhance safe savings.<sup>130</sup> A review financed by the Asian Development Bank examined schemes that have been tried and show promise. Some of the constraints that were studied force deposits; others inhibit withdrawals. On the forced-deposit side, automatic transfers into investment accounts and automatic withholding from paychecks offer promise mainly to the relatively rich poor in prosperous countries. Other practices—such as bonuses awarded by financial institutions for saving, deposit collectors, and commitment-savings schemes for farmers—can benefit the relatively poor poor.<sup>131</sup> Restricted-use savings accounts, restricted timing of withdrawals, a (literal) lock box that holds cash, withdrawal fees, and peer monitoring are among the examples of schemes focused on the withdrawal side of commitment savings.<sup>132</sup>

#### 4. *Reaching Poor Depositors Where They Live and Work*

Geographic distances impede the access poor people might otherwise have to banks. Technology looks like a fix. “Much of the current buzz,” remarks a 2008 report on what CGAP has called transformational branchless banking, “is around mobile phones,”<sup>133</sup> of which several billion

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<sup>129</sup> Nava Ashraf, Nathalie Gons, Dean Karlan & Wesley Yin, *A Review of Commitment Savings Products in Developing Countries*, THE FINANCIAL ACCESS INITIATIVE AND INNOVATIONS FOR POVERTY ACTION 4-5 (2003), <http://financialaccess.org/sites/default/files/publications/a-review-of-commitment-savings-products-in-developing-countries.pdf> (noting, inter alia, the choice of U.S. taxpayers to overwithhold the income tax they owe to get a larger refund; the high proportion of U.S. wealth held in illiquid assets, and the willingness of individuals to accept inconveniences for the purpose of generating more savings).

<sup>130</sup> *Id.*

<sup>131</sup> *Id.* at 5-8.

<sup>132</sup> *Id.* at 8-11.

<sup>133</sup> Timothy R. Lyman, Mark Pickens & David Porteous, *Regulating Transformational Branchless Banking: Mobile Phones and Other Technology to Increase Access to Finance*, CGAP (Jan. 15, 2008), <http://www.cgap.org/publications/regulating-transformational-branchless-banking-mobile-phones-and-other-technology>.

are in use around the world.<sup>134</sup> The director of a Gates Foundation initiative aimed at enhancing financial access has argued that mobile phones and retail storefronts can combine as instruments for making savings more available to poor depositors, who can use their telephones to order transactions and familiar retail venues to pick up and leave their money.<sup>135</sup>

Inviting banks to reach low-income prospective savers with partnerships between mobile communication technology and retail agents necessarily reaches into several regulatory domains. Rules pertaining to telecommunication, competition, and consumer protection bear on feasibility. At the banking level, implementation of such a proposal necessarily touches on foreign exchange regulations, e-commerce rules, and provisions governing whether and how a bank's agent can work with customers at retail storefronts.<sup>136</sup> Regulators must also consider how to count, for the sake of prudential-rules compliance, sums in accounts that are available to depositors by electronic means.<sup>137</sup>

### B. Enhanced Lending

The downturn that had spread through the world by 2008 showcased both the presence and the absence of loan regulations. The American statutory response to this crisis, named Dodd-Frank for two committee chairmen in Congress and tellingly subtitled the Wall Street Reform and Consumer Protection Act,<sup>138</sup> covered most of the United States income spectrum. At the richer end, hedge funds, private equity funds, derivatives, investment banks, and other aggregations of wealth on Wall Street faced controls the likes of which had not been introduced since the Great Depression.<sup>139</sup> At the poorer end, Congress bestowed power over consumer-finance fundamentals on a new Consumer Financial Protection Agency.<sup>140</sup> Similar

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<sup>134</sup> See *Gartner Says Worldwide Mobile Connections Will Reach 5.6 Billion in 2011 As Mobile Data Services Revenue Totals \$314.7 Billion*, GARTNER NEWSROOM (Aug. 4, 2011), <http://www.gartner.com/it/page.jsp?id=1759714> (estimating 5.6 billion mobile connections worldwide in 2011).

<sup>135</sup> *A Better Mattress*, *supra* note 119 (quoting Robert Peck Christen).

<sup>136</sup> Lyman, Pickens & Porteous, *supra* note 133, at 5.

<sup>137</sup> *Id.*

<sup>138</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010). Christopher Dodd chaired the Senate Banking Committee and Barney Frank chaired the House Financial Services Committee. Jim Hawkins, *Regulating on the Fringe: Reexamining the Link Between Fringe Banking and Financial Distress*, 86 IND. L.J. 1361, 1380 n.100 (2011).

<sup>139</sup> Michael S. Barr, *The Financial Crisis and the Path of Reform*, 29 YALE J. ON REG. 91, 113 (2012).

<sup>140</sup> See *id.* (summarizing Dodd-Frank).

interventions arose outside the United States. The European Union moved in 2009 to centralize regulation of banking, securities, and the insurance sector,<sup>141</sup> while supranational entities took steps to strengthen prudential regulation.<sup>142</sup>

Re-regulating has proceeded. Going forward, the substitution of “banking for poor people” for “microfinance” would keep both customers and providers at the forefront of new lending controls. Consumer protection ought to be a priority for the regulation of loans made to low-income borrowers. Another priority, this one focusing on providers, is to optimize levels of loan capital.

### 1. Consumer Protection

Two ideas warrant attention in any discussion of consumer protection in microlending because they so pervade the literature on financial regulatory reform. The first is transparency: Advocates argue that consumers should receive intelligible accounts of how much they are borrowing, how much they will have to repay, how loans available in the borrowers' markets compare to one another, and the consequences of not repaying.<sup>143</sup> The second oft-proposed reform is a maximum interest rate.<sup>144</sup> Both ideas have promise and both call for caution before implementation.

Transparency offers something for two conflicting sectors in the politically binary debate, *pro* versus *contra*, on regulation. Because clarity about loan terms makes no sense unless borrowers can use disclosures to guide their decisions, transparency as policy necessarily embraces and extends consumer choice. This stance appeals to both admirers and opponents of regulation, the optimists and pessimists we met in the last Part. Pessimists appreciate transparency as a source of power for weaker parties. For optimists, transparency supports an attractive alternative to

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<sup>141</sup> Ian Traynor, *European Union Agrees Super-Regulator to Head Off Financial Crises*, THE GUARDIAN, Dec. 2, 2009, <http://www.guardian.co.uk/business/2009/dec/02/eu-financial-regulation-deal>.

<sup>142</sup> Kevin Davis, *Regulatory Reform Post the Global Financial Crisis: An Overview*, MELBOURNE APEC FINANCE CENTRE (2011), [http://www.apec.org.au/docs/11\\_CON\\_GFC/Regulatory%20Reform%20Post%20GFC-%20Overview%20Paper.pdf](http://www.apec.org.au/docs/11_CON_GFC/Regulatory%20Reform%20Post%20GFC-%20Overview%20Paper.pdf).

<sup>143</sup> Robin Ratcliffe, *An Industry Imperative: Enhancing Consumer Protection in Microfinance*, MICROFINANCE INSIGHTS (2009), available at <http://www.accion.org/Document.Doc?id=637>.

<sup>144</sup> Brigit Helms & Xavier Reille, *Interest Rate Ceilings and Microfinance: The Story So Far*, CGAP OCCASIONAL PAPER (2004), <http://www.cgap.org/sites/default/files/CGAP-Occasional-Paper-Interest-Rate-Ceilings-and-Microfinance-The-Story-So-Far-Sep-2004.pdf>.

command-and-control rules from bureaucrats. Neither side is completely satisfied, but a policy of transparency meets them halfway.<sup>145</sup>

Substituting “loans made to poor people” for the word microcredit or microfinance hones attention to a couple of basic problems with transparency as policy. A summary of transparency circulated by Oikocredit, an international organization founded by church leaders in 1975 to support fledgling enterprises with loan capital, notes the custom of microfinance analysts to estimate loan prices “by looking at institutional portfolio yields.”<sup>146</sup> Yields do not reveal the prices of loans when an institution offers multiple products at multiple prices.<sup>147</sup>

Lenders do not follow any unitary convention in articulating the price of a loan. Two popular metrics, annual percentage rate and total cost of credit, count the cost of borrowing differently and compete with other alternatives.<sup>148</sup> Even if regulators and lenders wanted to agree on criteria and terminology for loan disclosure, individual borrowers present divergent conditions for lenders: they present a range of credit histories, and market conditions can make the price of money labile in a region.<sup>149</sup> Prices vary in response to other conditions, including the sizes of loans, transaction costs that lenders associate with particular loans, inflation, taxes, and the maturity of the lending institution.<sup>150</sup>

And even if prices could be stated clearly and consistently, poverty impedes what individuals can learn about the terms banks offer them as customers. One expert on financial-literacy initiatives has concluded that “the gulf between the literacy levels of most Americans and that required to assess the plethora of credit, insurance, and investment products sold today—and new products as they are invented tomorrow—will not be

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<sup>145</sup> This midpoint gives transparency the appearance of transcending partisanship. See generally JACQUELINE BEST, *THE LIMITS OF TRANSPARENCY: AMBIGUITY AND THE HISTORY OF INTERNATIONAL FINANCE* (2006) (arguing that calls for transparency mask political struggles and that as policy, transparency is never just a simple corrective to shortfalls of information in a market).

<sup>146</sup> Alexandra Fiorillo, *Pricing Transparency in Microfinance: No Single Price for Microloans*, MFTRANSPARENCY.ORG (Oct. 24, 2011), <http://www.mftransparency.org/pricing-transparency-in-microfinance-no-single-price-for-microloans/>.

<sup>147</sup> *Id.*

<sup>148</sup> Interview by OIKO CREDIT with Chuck Waterfield, CEO of MicroFinance Transparency (Feb. 10, 2012) available at <http://www.mftransparency.org/pricing-transparency-in-microfinance-interview-with-chuck-waterfield-ceo-of-mftransparency/>.

<sup>149</sup> Alyssa Hansen, *The Interest Rate Debate: How is Oikocredit Protecting Clients?*, OIKO CREDIT (Aug. 9, 2011), <http://oikocreditusa.org/the-interest-rate-debate-how-is-oikocredit-protecting-clients/>.

<sup>150</sup> *Id.*



bridged.”<sup>151</sup> Poor people in the United States are relatively rich. In India, one study of micro-borrowers “found that only 17 percent of respondents were able to solve the arithmetic problem ‘divide 8,000 by 10’ and only three percent of respondents could multiply ‘4,500 by 18.’”<sup>152</sup> Borrowers typically misunderstand the interest rates they pay.<sup>153</sup>

In debates over the regulation of loans made to poor people, the other oft-mentioned reform idea, price controls, serves as a kind of complement to transparency. Transparency enjoys popularity among reformers and other observers but warrants concern. Limits on the amounts of interest that lenders can lawfully charge borrowers have generally been decried;<sup>154</sup> they may deserve more support.

Critics of interest rate caps emphasize the truism that poor people’s banking is a costly business. If limited to prices that would not shock observers who have ready access to loan capital, lenders to a poor clientele could not make money. They would cater to the well-banked sector, whose loans are cheaper to administer. In turn poor people, cut off from well-regulated credit, must resort to “moneylenders” or “loan sharks.” These epithets connote disrespect for the rule of law, predatory tactics to get loans repaid and, of course, interest rates even higher than the high prices a well-regulated lender would charge without caps.

Regulators might keep in mind the analogous critique of minimum wage legislation as a reform to enhance welfare for the poor. For market-modelers in the academy, it once was axiomatic that employment rates and minimum hourly wages are inversely correlated. Any employer, according to the axiom, would choose to do without labor—switching to machinery, perhaps, or offshore manufacture—unless that labor came cheap, and so policymakers could have robust domestic employment or good wages but not both. Experience refuted the hypothesis.<sup>155</sup>

<sup>151</sup> Lauren E. Willis, *Against Financial-Literacy Education*, 94 IOWA L. REV. 197, 201 (2008).

<sup>152</sup> See Karnani, *supra* note 2, at 50.

<sup>153</sup> Akhand Tiwari, Anvesha Khandelwal & Minakshi Ramji, *How Do Microfinance Clients Understand Their Loans?*, CENTRE FOR MICRO FINANCE (2008), [http://ifmr.ac.in/cmfp/publications/wp/2008/25\\_Ramji\\_Loan%20Contracts\\_Financial%20Literacy.pdf](http://ifmr.ac.in/cmfp/publications/wp/2008/25_Ramji_Loan%20Contracts_Financial%20Literacy.pdf).

<sup>154</sup> Priyadarshie & Ghalib, *supra* note 45, at 7-9 (summarizing the debate).

<sup>155</sup> The leading monograph on the minimum wage concludes that raising it does not harm employment. DAVID CARD & ALAN B. KREUGER, *MYTH AND MEASUREMENT: THE NEW ECONOMICS OF THE MINIMUM WAGE* (1995) (reporting empirical studies). See also Steven Greenhouse, *A Campaign to Raise the Minimum Wage*, N.Y. TIMES, Apr. 9, 2012, at B1 (reporting a suggestion that the minimum wage be raised as an economic stimulus: more wage income means more cash in the hands of spenders). Disagreement continues. On state and local data in the U.S., compare Debra Burke, Stephen Miller & Joseph Long, *Minimum Wage and Unemployment Rates: A Study of Contiguous Counties*, 46 GONZ. L. REV. 661

For loans made to poor people, experience within a domestic economy can serve a similar function, informing the to-cap-or-not-to-cap question.<sup>156</sup> Studies of microlending have yielded mixed results. Ecuador has fared well with limits on interest rates,<sup>157</sup> Vietnam poorly.<sup>158</sup> Regulators in a jurisdiction can consider how their setting resembles, or differs from, other places where interest rate caps have succeeded. Caps are likely to function better where microloan markets are dominated by monopoly providers, because restrictions on lenders' rents would invite in more entrants to compete with the monopolist and, at least in theory, drive loan prices down.<sup>159</sup> Loosening the clutch of monopoly power is a regulatory goal that interest rate caps can advance. Here policymakers have available the experience of South Africa, where legislation authorizes the government to impose interest rate controls in response to market data.<sup>160</sup>

Another consumer-regulatory direction that experience can guide is the prohibition of abusive repayment tactics.<sup>161</sup> Like transparency and interest rate caps, this reform can deliver only so much and implementers ought to remain aware of its limitations. Predatory lenders foreclosed by law enforcement from one type of predation would presumably try to shift to

(2010-2011) (finding an adverse effect on employment) with Scott D. Miller, *Atrophied Rights: Maximum Hours Labor Standards Under the FLSA and Illinois Law*, 28 N. ILL. U. L. REV. 261, 279 (2008) (observing that after Illinois raised its minimum wage, its employment rate went up).

<sup>156</sup> Compare Elin M. King, *Vietnam's Decree on Microfinance: A Flawed Attempt to Create an Enabling Legal Environment for Microfinance*, 17 PAC. RIM L. & POLY J. 187 (2008) (arguing that caps failed in Vietnam) with Megan Whittaker, *South Africa's National Credit Act: A Possible Model for the Proper Role of Interest Rate Ceilings for Microfinance*, 28 NW. J. INT'L L. & BUS. 561 (2008) (arguing that caps succeeded in South Africa).

<sup>157</sup> See Bill Payne & Gray Skinner, *Microfinance Regulation: Interest Rate Caps and Concept of Usury* 57 (2010) (unpublished manuscript), available at: [http://works.bepress.com/gray\\_skinner/1](http://works.bepress.com/gray_skinner/1) (reporting success in Ecuador). "I'm not in favor of interest rate caps," wrote the founder of MF Transparency in a comment left on the CGAP microfinance blog: but I would say that a main factor for forcing MFIs [microfinance institutions] to think harder about their pricing has been pricing caps. . . . When there isn't price competition, when there isn't pricing transparency, when there aren't pricing caps, MFIs—especially for-profit MFIs—don't have much incentive to really think hard about reducing the prices they are charging the poor.

Richard Rosenberg, *Competition Gets a Pat on the Back*, CGAP (Feb. 7, 2012), <http://www.cgap.org/blog/competition-gets-pat-back> (reporting a comment from Chuck Waterfield)

<sup>158</sup> King, *supra* note 156.

<sup>159</sup> See Karmani, *supra* note 2, at 50-51.

<sup>160</sup> Whittaker, *supra* note 156, at 580-81 (adverting to the National Credit Act of 2005, which allows a trade minister to set interest rate caps based on market data).

<sup>161</sup> See Dowling, *supra* note 40, at 1086 (describing predatory loan collection tactics in Andhra Pradesh).

another; regulators cannot expect that abusive lenders will live within decent means of obtaining repayment. It remains desirable, however, to remind lenders that loan payments may be pursued by some means and not others. Enforcement of legal controls on repayment tactics, in turn, returns to transparency. Enforcement tells borrowers which burdens of their repayment struggle must be endured and which are unacceptable because they violate the law.<sup>162</sup>

For regulators, the clearest guidance from experience is that it is desirable to prevent, or at least discourage, individual microdebtors from taking out several unsecured loans at the same time.<sup>163</sup> This regulatory stance—a frankly paternalistic intervention—constrains lending while keeping the vulnerability of individual debtors in mind. Legal interferences in voluntary transactions are always difficult to enforce: but this species of interference, with recent histories of default so fresh in mind, will likely warrant the necessary effort and cost. Experiments in securitization and other technologies that increase the pool of loan capital function more safely when regulators can thwart the making of multiple unsecured loans to the same low-income borrower. We now look more closely at this innovation.

## 2. *Optimizing Loan Capital: Toward Sustainability*

Researchers report, on one hand, a problem of too little loan cash available for the world's poor to borrow for microenterprises and, on the other, instances of crisis where too much money flooded a particular loan market too suddenly.<sup>164</sup> The word “sustainable” describes what regulators ought to pursue when they try to optimize loan capital. An increase in the supply of money will, when it is sustainable, permit poor people to borrow more at their election while at the same time not mire individuals in debts they cannot repay.

“Sustainability” is, to be sure, a conclusory term that tends to emerge only in its absence; when large numbers of borrowers default and portfolios go bad, observers condemn the initial lending in the aggregate as unsustainable. The term can nevertheless be applied to consider one technique, securitization, that sets out to enlarge microloan capital.

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<sup>162</sup> See Tiwari, *supra* note 153 (reporting findings that borrowers do not know which repayment tactics are permitted, and that they do not disapprove of some tactics prohibited by law as abusive).

<sup>163</sup> Multiple loans to the same borrower has been a common thread in microloan failure at the national level. See *supra* Part I.B.

<sup>164</sup> Deborah Burand, *Deleveraging Microfinance: Principles for Managing Voluntary Debt Workouts of Microfinance Institutions*, 27 J.L. & COM. 193, 194 (2009).

Corporate finance scholar Steven Schwarcz has expounded on the prospects of securitization, using “sustainable” in an article title.<sup>165</sup>

More microloan capital can be raised, Schwarcz argues, by the issuance to investors (not “donors”<sup>166</sup>) of shares in special-purpose entities established to lend money to low-income borrowers.<sup>167</sup> When buying the opportunity to collect on existing loans, this special-purpose entity would offer “regenerative securitization”; a bolder “transformative securitization” occurs when it moves beyond buying receivables and makes new loans.<sup>168</sup> This influx of investment capital could make microloans not only more available but cheaper.<sup>169</sup> Securitization means that no intermediary stands between investors and borrowers.<sup>170</sup> A loan price thus need not include any retail markup, which is the difference between the lower interest rate at which a bank borrows and the higher interest rate at which it lends.<sup>171</sup> The special-purpose entity does not borrow and so need not “buy low, sell high.”<sup>172</sup> At least in principle, securitization offers poor people cheaper loans than what commercial banks can provide. The proposal has been implemented.<sup>173</sup>

Securitization of loan receivables is risky, however. Investors, borrowers, and financial systems have felt its repercussions. Special-purpose vehicles are key constituents of the “shadow banking system,” which moves financial transactions out of the safety of prudential regulation.<sup>174</sup> Two other terms of popular alarm—“derivatives” and “collateralized debt obligations”—describe what Schwarcz praises as a source of new microloan capital. As one settlement of a notorious

<sup>165</sup> Steven L. Schwarcz, *Disintermediating Avarice: A Legal Framework for Commercially Sustainable Microfinance*, 11 U. ILL. L. REV. 1165 (2011).

<sup>166</sup> *Id.* at 1197.

<sup>167</sup> *Id.* at 1175.

<sup>168</sup> *Id.*

<sup>169</sup> *Id.* at 1176.

<sup>170</sup> *Id.* at 1171.

<sup>171</sup> *Id.* at 1169.

<sup>172</sup> *Id.*

<sup>173</sup> *Id.* at 1177. CGAP and the Grameen Foundation jointly published a guide for microfinance institutions considering securitization. Peter Humphreys & Alexandra Moosally, *Securitization: A Technical Guide*, CGAP (2010), <http://www.cgap.org/sites/default/files/CGAP-Technical-Guide-Securitization-Oct-2010.pdf>.

<sup>174</sup> This term was coined by Paul McCulley. See Bryan J. Noeth & Rajdeep Sengupta, *Is Shadow Banking Really Banking?*, THE REGIONAL ECONOMIST (2011), [http://www.stlouisfed.org/publications/pub\\_assets/pdf/re/2011/d/shadow\\_banking.pdf](http://www.stlouisfed.org/publications/pub_assets/pdf/re/2011/d/shadow_banking.pdf). See also PAUL KRUGMAN, THE RETURN OF DEPRESSION ECONOMICS AND THE CRISIS OF 2008 (2009) (depicting shadow banking as at the center of the financial crisis).

complaint has demonstrated, a special-purpose vehicle can injure investors who receive false information about the investments it holds.<sup>175</sup>

The dangers of special-purpose investment vehicles spread beyond investors, as indicated by the fall of home mortgages in the United States. Holders of securitized mortgages are less likely than mortgagees whose loans are not securitized to obtain loan modifications that allow them to stay in their homes, in part because of the different incentives for portfolio lenders and securitization servicers: a securitization servicer “does not care what the property brings in at a foreclosure . . . because the servicer is paid off the top. As long as there is just some land value left, the servicer will get paid.”<sup>176</sup> Wide-scale loss of homes worsens the consequences of economic reversal in a region. Residents are displaced, neighboring properties decline in value, and what had been collateral for a loan dissipates. At the institutional level, collapses of securitized vehicles can grow big enough to raise the prospect of a government bailout—“too big to fail” makes ironic reference to what is in fact a catastrophic failure, with costs borne by nonparticipants—and a bailout in turn deepens perceptions of collapse.

Should regulators choose to reject or discourage securitization of microloan capital, however, “transformative”<sup>177</sup> shifts in how borrowers reach this money are relatively unlikely to emerge. Conventional banking for poor people—furnished by commercial banks, nonprofits, and aggregations of customer-owners<sup>178</sup>—keeps the supply of loan cash more constant, but this constancy may be inadequate. Microloan cash supplies unenlarged by the dramatic increases that securitization can bring is too limited to meet the needs of both low-income individuals and low-income national economies, whereas too much cash encourages lenders to make multiple loans to the same borrower. Optimizing loan capital thus calls for care in rulemaking, as the perils of both under- and over-supplying money have been well documented.

#### IV. REGULATION DISAGGREGATED, SECOND PASS: A FOCUS ON OWNERS

Imagine a rule-writer unaware of, or unpersuaded by, the thesis of this Article that microfinance must be disaggregated before it can be regulated.

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<sup>175</sup> SEC v. Citigroup Global Markets, Inc., 673 F.3d 158, 161 (2d Cir. 2012) (reviewing a proposed \$285 million settlement of a civil complaint).

<sup>176</sup> Adam Levitin, *Is Redefault Risk Preventing Mortgage Loan Mods?*, CREDIT SLIPS (July 16, 2009, 2:03 PM), <http://www.creditslips.org/creditslips/2009/07/is-redefault-risk-preventing-mortgage-loan-mods-.html>.

<sup>177</sup> Schwarcz, *supra* note 165, at 1175.

<sup>178</sup> See *infra* Part IV.

This regulator might set out to codify the rules of microfinance in one unitary compilation—and promptly face a palimpsest of existing laws. The slate on which they write is not blank. Banking law might or might not govern a microfinance entity, depending on whether the entity fulfills a legal definition of a bank. Corporate governance law, which focuses on ownership, will apply divergently to businesses that can be held in different modes and may or may not pursue economic rents for owners.<sup>179</sup> This Part turns to owners of microfinance-providing entities.<sup>180</sup>

#### A. Pertinent Distinctions Among Providers

A sorting device that offers particular use to regulators is a relatively simple question: Who owns the entities that furnish credit and savings to low-income clients, and what do these owners want? Institutions that provide financial services to the poor may be classified along many lines. The smallest number of cohorts that pertain to regulation is three.<sup>181</sup> I

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<sup>179</sup> One early study of microfinance institutions identified three categories and seven types. See van Greuning et al., *supra* note 20 and accompanying text (describing the World Bank's *Framework for Regulating Microfinance Institutions*).

<sup>180</sup> Like every other discussion of regulation that pays attention to who owns and governs firms, this Part owes a debt to Henry Hansmann, whose writings on the law of business associations and donor-funded entities span decades. HENRY HANSMANN, *THE OWNERSHIP OF ENTERPRISE* (1996) [hereinafter HANSMANN, *OWNERSHIP*]; Henry B. Hansmann, *The Role of Nonprofit Enterprise*, 89 YALE L.J. 835 (1980); Henry Hansmann, *Ownership of the Firm*, 4 J.L. ECON. & ORG. 267 (1988); Henry Hansmann & Reinier Kraakman, *Toward a Single Model of Corporate Law?*, in *CORPORATE GOVERNANCE REGIMES: CONVERGENCE AND DIVERSITY* 56 (Joseph A. McCahery et al. eds., 2002).

<sup>181</sup> Cf. Bernstein, *supra* note 82, at 22-23 (noting another division, by Hans Dieter Seibel, of microfinance institutions into three categories: informal, semiformal, and formal). Some writers favor a number smaller than three. In *The Ownership of Enterprise*, Hansmann works with the number two, dividing firms into for-profit versus non-profit and distinguishing those owned by producers from those owned by consumers. HANSMANN, *OWNERSHIP*, *supra* note 180, *passim*. For present purposes, however, I find a third group necessary: so much of the financial lives of poor people consists of mutual aid, and the entities formed are often neither for-profit nor nonprofit. Another owner-focused division into two categories restricts “microfinance” to formally incorporated providers and says that other providers offer “informal finance.” Mark Schreiner, *Informal Finance and the Design of Microfinance*, 11 DEV. IN PRAC. 637 (2000). This dichotomy ignores myriad legal distinctions between for-profit and nonprofit entities that pervade regulation. A third route to the number two is to divide providers into those that offer savings and those that offer loans. Prudential rules keep the former category relatively small and regulate it more stringently. This division makes some sense, but I contend it makes even more sense for regulators to focus on the point of view of an owner: its risks, its returns, what it wants. For numbers bigger than two, see, for example, Joselito Gallardo, *A Framework for Regulating Microfinance Institutions: The Experience in Ghana and the Philippines*, THE WORLD BANK

divide them here into (1) mutual aid, (2) nonprofit, and (3) for-profit institutions.<sup>182</sup>

The mutual aid category covers microfinance providers that pool and distribute money to and for a group of individuals. These entities fall under the rubric of what Henry Hansmann called “customer-owned enterprise”;<sup>183</sup> they also illustrate what Hans Dieter Seibel has deemed “member-owned institutions based on social solidarity.”<sup>184</sup> Mutual-aid microfinance providers can hold loans and collect money without regulatory oversight, but regulated entities like credit unions also fit in this group.

Charitable nonprofit microfinance providers offer financial services to low-income clients consistent with a philanthropic mission, typically pertaining to economic development or the alleviation of poverty. Whereas entities in the mutual-aid category can be regulated or unregulated, nonprofit entities are always regulated by some domestic law. Typically they are not overseen by a bank superintendency, however. Only a minority of nonprofit microfinance institutions are licensed to take deposits or held to prudential regulations aimed at promoting safety for clients.<sup>185</sup> Nonprofit microfinance institutions offer credit more than any other financial product.

For-profit microfinance institutions seek returns for investors, rather than the gains for customer-owners that mutual-aid entities pursue or the philanthropic missions that define nonprofits. For these providers, microfinance is a source of income derived most readily by charging interest on loans. Other microfinance products—savings and insurance in particular—can be profitable too; but lending is the most remunerative

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24 (2001), <http://www1.worldbank.org/finance/assets/images/2755.pdf> (noting that Ghanaian and Philippine laws divide microfinance providers into numerous cohorts, some regulated and some unregulated).

<sup>182</sup> The categories contain some overlap. This Article uses “nonprofit” as a rough synonym for charity, referencing an eleemosynary mission. Should a mutual-benefit entity be incorporated as a nonprofit, I would put it in the mutual-aid rather than the nonprofit category because it lacks this mission, focusing instead on gains for its member-owners. I also believe that a classification focused on ownership can include nonprofits, the notion that a nonprofit corporation cannot have owners notwithstanding. See Henry B. Hansmann, *Reforming Nonprofit Corporation Law*, 129 U. PA. L. REV. 497, 574 (1981) (reminding readers that most generalizations about nonprofits contain exceptions). For purposes of this Article, the “owners” of a nonprofit are those persons who govern the corporation.

<sup>183</sup> HANSMANN, OWNERSHIP, *supra* note 180, at 149.

<sup>184</sup> Hans Dieter Seibel with Andrea Armstrong, *Reparations and Microfinance Schemes*, in *THE HANDBOOK OF REPARATIONS*, 676, 691 (Pablo De Greif ed., 2006).

<sup>185</sup> Christen, Lyman, & Rosenberg, *supra* note 25, at 25.

microfinance activity and so some entities that are licensed to take deposits choose to forgo savings and focus on loans.<sup>186</sup>

Ghana offers an illustration of the three categories at work in one country. Mutual aid microfinance in this country takes the form of *susu*, a term for pooled savings and credit.<sup>187</sup> Participants in a *susu*, following the rotating-credit model, turn over small sums to a collector, who pays out the pool to individuals in rotation.<sup>188</sup> Although efforts are underway to regulate this form of microfinance,<sup>189</sup> the category remains in the informal tier. An example of a nonprofit microfinance institution is Microfin Plus Ghana, a registered NGO that lists as its partners both the Ghana Cooperative Susu Collectors Association, at the informal end, and Barclays, a bank.<sup>190</sup> First Allied Savings and Loan is an example of a Ghanaian for-profit microfinance institution.<sup>191</sup>

In another country, Mexico, the mutual aid sector includes the *tanda*, a credit association formed by individuals in small groups united by acquaintance and a degree of mutual trust.<sup>192</sup> An example of a Mexican nonprofit microfinance institution is the Mexican Association for Rural and Urban Transformation, whose website announces work in “education, hygiene, healthy diets, appropriate technology, microfinance, emergency support, infant care centers and more.”<sup>193</sup> Compartamos Banco, having

<sup>186</sup> ROBINSON, *supra* note 58, at 234.

<sup>187</sup> Kent McKeever, *A Short History of Tontines*, 15 FORDHAM J. CORP. & FIN. L. 491, 516 (2010) (noting that *susu* is the West African word for an entity known as a *tontine* in French-speaking countries like Togo and Cote d’Ivoire, and an *esusu* in Nigeria).

<sup>188</sup> *Id.*

<sup>189</sup> “Since 1990 the Ghana Cooperative Susu Collectors Association (GCSCA) is trying to minimize fraud and regulate the operations of Susu collectors across the country.” Thilo Kunzemann, *Do You Susu?*, ALLIANZ (Feb. 20, 2010), <http://www.knowledge.allianz.com/search.cfm?114/do-you-susu>.

<sup>190</sup> See *Partnership*, MICROFIN PLUS GHANA, [http://microfinplusghana.org/index.php?option=com\\_content&view=article&id=12&Itemid=12](http://microfinplusghana.org/index.php?option=com_content&view=article&id=12&Itemid=12) (last visited Nov. 1, 2012).

<sup>191</sup> See *About FASL*, FIRST ALLIED SAVINGS AND LOANS, <http://www.firstalliedghana.com/about.php> (last visited Nov. 1, 2012).

<sup>192</sup> For an anthropological account of the Mexican *tanda*, see Donald V. Kurtz & Margaret Showman, *The Tanda: A Rotating Credit Association in Mexico*, 17 ETHNOLOGY 65, 67-68 (1978); for a contemporary U.S.-based account, see Nezua, *In Tough Economic Times, Will a Tanda Work for You?*, EL MACHETE (Aug. 4, 2009, 1:03 PM), <http://theunapologeticmexican.org/elmachete/2009/08/04/in-tough-economic-times-will-a-tanda-work-for-you/> (encouraging Mexican-Americans who need cash to explore this tradition).

<sup>193</sup> See AMEXTRA, [http://www.amextra.org/1\\_amextraingles.html](http://www.amextra.org/1_amextraingles.html) (last visited Nov. 3, 2012).



started microfinance operations as an NGO, shifted to the for-profit category in 2006.<sup>194</sup>

The large cohort of nonprofits offering microfinance in a third country, India, includes Bhoomika, a registered charity with operations in the state of Orissa; among providers in the for-profit group is SKS, continuing its microlending in troubled Andhra Pradesh.<sup>195</sup> Self-help groups dominate informal microfinance in India following an initiative by the National Bank for Agricultural and Rural Development. This central bank enlists nonprofits to help assemble groups of ten to twenty poor people, typically women. The self-help group meets regularly to discuss social issues and poor funds in a small savings account. When deposits are large enough, the group can make loans to members, and after it has built a history of disbursing and collecting these internal loans, it becomes eligible for commercial lending.<sup>196</sup>

## B. Owner-Specific Attentions

### 1. Microfinance as Mutual Aid

The mutual-aid category ranges in sophistication from humble rotating savings-and-credit associations to well-capitalized and technologically advanced credit unions. Mutual-aid entities of the first type are in the typology of Hans Dieter Seibel “informal” microfinance institutions, meaning unregulated entities; credit unions are “formal,” regulated as banks and typically licensed to take deposits.<sup>197</sup> This divergence in regulatory attention—from none to much—limits what can be said about attentions

<sup>194</sup> See COMPARTAMOS BANCO, <http://www.compartamos.com/wps/portal/AboutCompartamosBanco/History> (last visited Nov. 3, 2012). For a critical account of the reincorporation and initial public offering of Compartamos, see Malcolm Harper, *The Commercialization of Microfinance: Resolution or Extension of Poverty?*, in CONFRONTING MICROFINANCE: UNDERMINING SUSTAINABLE DEVELOPMENT 49, 50-51 (Milford Bateman ed., 2011).

<sup>195</sup> See SKS MICROFINANCE, [http://www.sksindia.com/known\\_sks.php](http://www.sksindia.com/known_sks.php) (last visited Nov. 3, 2012). See also Felix Salmon, *The Lessons of Andhra Pradesh*, REUTERS (Nov. 18, 2010), <http://blogs.reuters.com/felix-salmon/2010/11/18/the-lessons-of-andhra-pradesh/> (faulting SKS for an initial public offering that enriched the bank's principals without enhancing wealth for its poor clientele); AKULA, *supra* note 99 (describing SKS from the vantage point of its Indian-American founder).

<sup>196</sup> See generally Klaus Deininger & Yanyan Liu, Policy Research Working Paper, *Longer-Term Economic Impacts of Self-Help Groups in India*, THE WORLD BANK (2009), <http://elibrary.worldbank.org/docserver/download/4886.pdf?expires=1351993334&id=id&acname=guest&checksum=23F566C12E348B42F7B4BAC64CE47769> (summarizing formation and operations).

<sup>197</sup> See *supra* note 181 (referring to the tiers-framework associated with Seibel).

specific to this type of ownership. Existing regulation treats mutual-aid providers differently from one another, as it should, depending on whether these providers do business as chartered banks. Despite this variation in the category, each mutual-aid banking entity is like all the others in that it seeks, at least in principle, to increase the prosperity and financial security of the client-members who own, spend, save, and borrow its money.

This goal not only unites modest rotating savings and credit associations with prosperous credit unions and the all mutual-aid entities in between (large rotating savings and credit associations and fledgling credit unions, for example), but distinguishes this category from the other two. For a for-profit entity, microfinance exists to return earnings to investors; a nonprofit provides microfinance to advance its mission. Mutual-aid microfinance—again, in principle—recognizes no such external goals or beneficiaries. It pays no dividends, sells no shares on any exchange, and advances no philanthropic ends. The mutual-aid entity exists for its own sake.

The simplicity of this agenda makes the mutual-aid category of microfinance uniquely attractive for what it lacks and eschews. Existing only for itself gives the entity independence. The absence of external investors and donors means more power, once again in principle, for owner-clients. Geographic constraints and restrictions on who may join, if available, keep the entity responsive to the communities to which it is tied. Because its members have to live with the results it occasions, the mutual-aid entity is likely to be the most risk averse of the three kinds of microfinance provider.

And so, in the name of safety, regulatory policy might plausibly favor this sector over the other two. Regulators in Britain reached a pertinent conclusion in 2012 following a report by the Department for Work and Pensions (“Department”).<sup>198</sup> The expansion of credit unions, according to this report, offered great promise to the national economy as well as millions of low-income Britons trapped in predatory lending.<sup>199</sup> The UK government established a £38 million fund, directed mainly toward information technology “to modernise” credit union operations, building on an appropriation of £15 million in the previous year.<sup>200</sup> In addition to allocating funds to credit unions for infrastructure, the Department expressed support for regulatory relief, announcing its openness to

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<sup>198</sup> Sarah Neville, *Report Calls for Expansion of Credit Unions*, FINANCIAL TIMES (May 24, 2012, 10:24 PM), <http://www.ft.com/intl/cms/s/0/7cc3edb2-9abf-11e1-9c98-00144feabdc0.html#axzz2BDKahOXn>.

<sup>199</sup> *Id.*

<sup>200</sup> *Freud Announces Further Investment To Secure Future of Credit Unions*, DEPARTMENT FOR WORK AND PENSIONS (June 27, 2012), <http://www.dwp.gov.uk/newsroom/press-releases/2012/jun-2012/dwp070-12.shtml>.

increasing the interest rate cap on credit union loans from 2 to 3 percent per month.<sup>201</sup>

This instance of favoritism for the mutual-aid sector of microfinance, though responsive to conditions in one country only, illustrates a direction that other regulators can take. A strong mutual-aid sector can compete robustly with nonprofits and commercial banks in the provisioning of savings accounts and loans to low-income clients. How much encouragement it should receive might be debated, but the defining characteristic of owners-cum-customers presents a constructive alternative to other sources of banking for poor people, which are entities that have their own agendas.

## 2. *Microfinance for Profit*

Banking marketed to poor clients imposes significant regulatory challenges yet is in another sense the simplest category for regulators to consider. Extraction of income through commerce is a pursuit that follows predictable paths. The agenda for a mutual-aid or nonprofit microfinance provider necessarily contains variety and can evolve, but an entity oriented toward profit will rarely be distracted from this central goal. It may jettison services and products in response to what markets deliver and what regulators require, but it maintains its emphasis on earnings. Uniformity in its agenda streamlines the regulatory response.

Putting aside as unregulable those providers popularly known as moneylenders or loan sharks,<sup>202</sup> the for-profit group consists of commercial banks, already a well-regulated cohort.<sup>203</sup> And so most of the owner-specific attention recommended here reduces to Carry On. Laws pertaining to banking, tax, crimes, consumer protection, real property, insolvency, secured transactions, and other fields are already in place—or can be installed without fanfare—to regulate this sector.

Owner-specific attention adds a task to this familiar list, however. Much more than the mutual-aid and nonprofit categories, for-profit microfinance has tempted opportunistic politicians to encourage defaulting on loan payments. The notorious “no pago” movement in Nicaragua had counterparts elsewhere.<sup>204</sup> Even if regulators think that predatory

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<sup>201</sup> See Neville, *supra* note 198.

<sup>202</sup> See discussion in *supra* note 10.

<sup>203</sup> Well-regulated in a relative rather than an absolute sense: a jurisdiction that can enforce any regulations at all will regulate its banks.

<sup>204</sup> For more information on “no pago,” see *supra* notes 52-56 and accompanying text. See also In India, Microcredit Faces Uncertainty, MICROFINANCE AFRICA (Jan. 4, 2011 1:54 AM), <http://microfinanceafrica.net/tag/microfinance-borrowers-commit-suicide/> (noting

microlenders deserve to suffer, widespread failures to make loan payments impose adverse effects on the larger community and should be forestalled. Regulators familiar with historical instances of default-incitement like No Pago can make a contingency plan. They might, for instance, establish quantitative triggers for safeguards to fall in place without the need for hasty emergency legislation.

### 3. *Microfinance as Instrumental to a Nonprofit Mission*

Of the three cohorts that offer banking for poor people, only the nonprofit sector fits well with the Microfinance Needs Regulation impulse to write a comprehensive and unitary rule-scheme.<sup>205</sup> Nonprofit entities work to generate income and stability for poor people, understood as their beneficiaries. Banking advances a mission—to alleviate poverty, improve the position of women, enhance national or regional economic development, or otherwise carry out a donor—endorsed goal. The presence of these donors gives regulators a distinct target not present in the mutual-aid or for-profit categories.

Charity or nonprofit legislation—codified around the world—typically addresses the desire of outsiders to know about an entity’s financial condition.<sup>206</sup> Microfinance regulation for this category has a natural home in statutory nonprofit law, which can compel these providers to describe their operations by accounting for their money. Toward this end, drafters of comprehensive proposals to regulate microfinance ought to consider narrowing their compendia to focus on nonprofits only.

Model legislation or best practices that eliminate the mutual-aid or customer-owned category on one hand, and for-profit entities on the other, can address the concerns and operations of nonprofits. Topics eligible for Principles for Nonprofit Microfinance Institutions could generate transparency. Entities would be encouraged to make public declarations about, *inter alia*, what “the double bottom line” means for their operations

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incitements to default on loans in Pakistan circa 2008 and 2009); Interview by India Knowledge at Wharton with Vijay Mahajan, President of the Microfinance Institutions Network of India (July 26, 2012), *available at* <http://knowledge.wharton.upenn.edu/india/articlepdf/4696.pdf?CFID=229662359&CFTOKEN=17171314&jsessionid=a8309519c7ecf8f8ffaf252517d5f85c1405> (reporting the same phenomenon in India).

<sup>205</sup> See *supra* Part I.

<sup>206</sup> In the United States, donors and prospective donors are understood as the constituency that wants this information about finances; in the nonprofit law of other countries, accounting to the government plays a stronger role. Alyssa A. DiRusso, *American Nonprofit Law in Comparative Perspective*, 10 WASH. U. GLOB. STUD. L. REV. 39, 75-76 (2011).

(for example, when sustainability and a charitable mission conflict, which of the two will they pursue?), how their operations or priorities differ from those of other nonprofits that offer microfinance, which services they offer and plan to offer in the future, what other entities they work with, and how they do business with their clients.<sup>207</sup>

This last transparency-topic, on client dealings, gives information to borrowers as well as donors. We have noted that as a fix for the ills of consumer banking, transparency has proved elusive, disappointing, and to some observers even an impediment to meaningful reform.<sup>208</sup> Those who regulate the nonprofit cohort of microfinance providers would be wise not to expect great consumer-protection strides forward from transparency as policy. The exercise of communicating more accurately with one's donors may, however, enhance entity-client communication. For example, informing donors in standardized terms how much the entities charge clients in interest on loans, a reform idea pressed for years by Microfinance Transparency,<sup>209</sup> would put nonprofit providers in the habit of describing their interest rates in more user-financially diction.

A variation on Principles for Nonprofit Microfinance Institutions ought to foster the writing and enforcement of voluntary standards and certification. Nonprofit managers have extensive experience with this mode of reaching donors and fellow nonprofits. A microfinance provider could use a certification mark to indicate its compliance with key terms of a Principles compendium.<sup>210</sup> Charity or trademark law would in turn provide redress for the wrongful use of this certification. Membership in a voluntary-standards association would build a forum for peer discourse, facilitating dialogues to raise standards. Even though managers of nonprofit microfinance institutions working in a particular region compete with one another and likely hold philosophical differences, they could agree

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<sup>207</sup> See Beth Rhyne, *Social Performance: A Truth in Advertising Approach*, CENTER FOR FINANCIAL INCLUSION (Jan. 5, 2012), <http://cfi-blog.org/2012/01/05/social-performance-a-truth-in-advertising-approach/#more-4920> (advocating transparency among microfinance nonprofits "to achieve mission-related results"). As with transparency generally, see *supra* notes 143-54 and accompanying text, reformers should expect increases in the quantity and quality of information acquired by nonprofit donors and clients to be modest at best. Entities and individuals who want information and can benefit from it already have the power to demand it; individuals who do not demand information about nonprofits are likely ill-situated to gain from it when it arrives. I thank Dana Brakman Reiser for elucidating this point.

<sup>208</sup> See *supra* Part III.B.1.

<sup>209</sup> *About MicroFinance Transparency*, MFTRANSPARENCY.ORG, <http://www.mftransparency.org/about-our-organization/> (last visited Nov. 3, 2012).

<sup>210</sup> This suggestion received a helpful airing from participants at a University of Maine School of Law workshop.

on norms of conduct and be able to list injurious behaviors that any reputable institution would avoid and abjure.

#### 4. *Fitting the Three Provider Categories Together*

After regulators disaggregate microfinance providers by focusing on ownership, they can move to relations among the three groups. An analogy to this “macro” approach to regeneration appears in competition law, which addresses behaviors that enhance or thwart competition within an industry or sector. Following the pattern of competition regulation (or antitrust, as this field is more frequently known in the United States), which seeks to promote multiplicity and choice in markets and to oppose monopolies, regulators of microfinance disaggregated start out preferring multiple types of ownership rather than a unitary model. Regulators who conclude that it is desirable for all the categories to flourish might consider how to encourage the continuing operations of each. They start by identifying the conditions that cause providers in each category to abandon their provision of financial services to poor people.

For-profit might look like the most durable type of provider. Entities commonly transform themselves from nonprofit to for-profit; the reverse move is rare.<sup>211</sup> Yet for-profit providers of loans and savings are never, *pace* the banking cliché, too big to fail. A for-profit entity whose loan portfolio declines has little incentive to stick around in the way that a mutual-aid or nonprofit provider, more tied to a community or a mission, would wish to linger. Nonprofit sources of banking services can disappear by various routes. They might leave one region to take up their work in another, shift their mission and operations away from microfinance, run out of money, or reincorporate as for-profits. A formally incorporated mutual-aid provider like a credit union can live indefinitely,<sup>212</sup> but a rotating savings and credit association is likely to change along with the fortunes of its members. Defaults or losses in a bad economic climate at one end, or the opening of a commercial bank branch in response to prosperity at the other, can end its reason for being. In sum, providers in all groups face

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<sup>211</sup> See generally John Tozzi, *Turning Nonprofits into For-Profits*, BLOOMBERG BUSINESSWEEK (June 15, 2009), [http://www.businessweek.com/smallbiz/content/jun2009/sb20090615\\_940089.htm](http://www.businessweek.com/smallbiz/content/jun2009/sb20090615_940089.htm) (discussing the fact that For-Profit companies would not turn into Nonprofit companies, because For-Profit companies’ goals are to put shareholder profits first).

<sup>212</sup> But see Tim Worstall, *It’s the Mutual, Not for Profit, Banks Which Are the Problem in Spain*, FORBES (May 10, 2012, 12:13 PM), <http://www.forbes.com/sites/timworstall/2012/05/10/its-the-mutual-not-for-profit-banks-which-are-the-problem-in-spain/> (commenting on the decline of incorporated mutual-aid providers in Spain).

conditions that can put them out of business. Enabling regulation can nurture some or all of the groups.<sup>213</sup>

As was noted, favoring the mutual-aid category is a plausible starting point.<sup>214</sup> This stance rests mainly on the premise that remote investment begets new and dangerous financial instruments that push underwriting standards down.<sup>215</sup> Banks rooted enough in their communities to suffer in the event of defaults lend money on more sober terms. If their practices had been universal, the disastrous residential real estate bubble that emerged in the United States might have been fended off.<sup>216</sup> The drawbacks of securitization, amply showcased, support a regulatory stance favoring those providers who have to live with the consequences of what they lend and hold. In this perspective the third group, nonprofits, might mean well (or might not) but nevertheless are inferior to mutual aid because nonprofits furnish charity, which is in principle inferior to self-reliance.<sup>217</sup>

More scrutiny of this proposition ought to precede its implementation, as there is no safe sector to provide banking for poor people. Nor is it obvious how to allot this type of banking in ratio terms for the groups. What, after all, is being distributed among the three: number of providers, number of clients served, number of loans made, cash value of monies held, cash value of loans outstanding? Even if regulators could in principle agree on how to plan these balances *ex ante*, market conditions alter the distribution. What regulators ought to pursue, instead, is the more modest goal of awareness. Distinct patterns of ownership pervade microfinance, and shifts in the relative balance of these holdings affect the experiences of clients and the performance of microfinance more generally.<sup>218</sup>

Although regulators may not know which sector to favor above the other two, fitting the categories together leaves them plenty of other work. Consider for example the desirability of competition.<sup>219</sup> Because the

<sup>213</sup> See *supra* note 67 and accompanying text.

<sup>214</sup> See *supra* notes 198-200 and accompanying text.

<sup>215</sup> See Black, *supra* note 50.

<sup>216</sup> Raymond H. Breschia, *Trust in the Shadows: Law, Behavior, and Financial Regulation*, 57 BUFF. L. REV. 1361, 1419-22 (2009). By way of response, a British commentator noted the failure of the Spanish conglomerate Bankia, an entity formed by the merger of “mutually owned, regional, usually not for profit banking entities.” Worstall, *supra* note 212.

<sup>217</sup> “Give a man a fish, and you feed him for a day. Teach a man to fish, and you feed him for a lifetime.” 44 *Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 511 n.19 (1996) (quoting the ancient Chinese proverb).

<sup>218</sup> DiRusso, *supra* note 206, at 85.

<sup>219</sup> That this goal is worth pursuing is axiomatic whenever poor people in a nation or region face inadequate access to banking—with the important proviso that poor borrowers should not have access to more loan money than they can reasonably repay. See *supra* note

income that a nonprofit micro-lender receives is directed to a charitable mission rather than paid out to investors, it has less incentive than a for-profit to charge all it can get for its loans, and thus its presence in a loan market may help to temper interest rates.<sup>220</sup> And because microloans are relatively costly to administer, a for-profit lender that starts out making small loans predictably will move to larger ones, which are cheaper to administer on a dollars-borrowed basis. It is small loans that do the most to alleviate unbankability.<sup>221</sup> Nonprofits are not immune to pressures to charge higher interest rates and make bigger loans, but their mission tempers the tendency.<sup>222</sup> Accordingly, rules to encourage nonprofit participation in regions where for-profit entities are making microloans should be considered.

In fitting the three provider categories together, regulators are tasked with managing relations that are both reciprocal and rivalrous. Nonprofits give mutual-aid providers loan capital, options for safer savings, and advice about how to pursue goals in which nonprofits have expertise. Both nonprofit and mutual-aid entities can become institutional customers of for-profit banks. Nonprofits frequently choose to work with mutual-aid entities when seeking clients and for-profit banks when expanding their operations. The nonprofit form has also been a way for entities to start their microlending operations before going public as for-profit entities.<sup>223</sup> For-profit providers find customers in the mutual-aid sector, and rely on nonprofit networks to find them.<sup>224</sup> The groups also compete with one another in the banking market.<sup>225</sup>

## CONCLUSION

Rejecting microfinance as a category for legal regulation emphatically does not reject microfinance as policy. Quite the contrary. Instead, I have argued, moving away from this dense neologism will permit regulators to

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178 and accompanying text.

<sup>220</sup> See Rosenberg, *supra* note 157.

<sup>221</sup> See DICHTER, *supra* note 90.

<sup>222</sup> Kenneth Downey & Stephen J. Conroy, *Microfinance: The Impact of Nonprofit and For-Profit Status on Financial Performance and Outreach*, ACAD. OF ECON. AND FIN. (2012), <http://www.econ-jobs.com/research/35795-Microfinance--The-Impact-of-Nonprofit-and-For-Profit-Status-on-Financial-Performance-and-Outreach.pdf>.

<sup>223</sup> See *supra* notes 194-95 and accompanying text (noting that two large for-profit microfinance institutions, SKS in India and Compartamos in Mexico, started out as nonprofits).

<sup>224</sup> See *supra* note 187-96 and accompanying text.

<sup>225</sup> See *supra* note 187-96 and accompanying text (giving Ghana, Mexico, and India as examples of countries where all three categories offer banking for poor people).



support the financial needs of poor people and the imperatives of a maturing market by honing their attention on relevant specifics. Like its Latinate cousins “development” and “industrialization,” microfinance remains central to economic and financial progress. The change that this Article urges—attention to the products and providers that need regulating—strengthens the sector.

Disaggregation is central to the undertaking. This Article has identified the products of microfinance as loans and savings accounts offered to poor persons, and the providers as falling into three groups: mutual-aid, nonprofit, and for-profit entities. Governments and rule-drafters might well disagree about these particulars. They can add to the list of microfinance products,<sup>226</sup> or choose a different number of providers.<sup>227</sup> The crucial point for them to bear in mind is that microfinance is many things rather than one.<sup>228</sup>

Disaggregation helps regulators to focus not only on the improvements they want but the rules they already have.<sup>229</sup> Sources of regulation already in place—such as bank superintendencies, corporate registry authorities, and self-regulatory organizations like trade associations and cooperatives authorities—can advance the social-developmental goals of microfinance without implicitly asserting, via the prefix “micro-,” that transactions and customers are and shall remain puny. Consumer protection law, banking law, and prohibitions of abusive debt recovery practices furnish some shelter for poor clients.

These existing safeguards are modest, of course. Meaningful protection for consumers of financial services has proved difficult to codify and enforce all over the world, and efforts to augment the bargaining power of poor people in financial markets have yielded disappointing results.<sup>230</sup> Should consumer protection make gains, however, the concept of

<sup>226</sup> See Christen, Lyman, & Rosenberg, *supra* note 25, at 2 (suggesting that microfinance might be understood to include not just savings and loans but also insurance and cash transfers).

<sup>227</sup> See Bernstein, *supra* note 181 (citing alternative ways to count and group providers).

<sup>228</sup> For an example of how to do so without fuss, see Stijn Claessens, Patrick Honohan & Liliana Rojas-Suarez, *Policy Principles for Expanding Financial Access: Report of the CGD Task Force on Access to Financial Services*, CENTER FOR GLOBAL DEVELOPMENT (2009), [http://www.cgdev.org/files/1422882\\_file\\_Financial\\_Access\\_Task\\_Force\\_Report\\_FINAL.pdf](http://www.cgdev.org/files/1422882_file_Financial_Access_Task_Force_Report_FINAL.pdf). The Center for Global Development, which describes itself as a “nimble, independent, non-partisan” think tank, scarcely uses the term “microfinance” in this report. See *About CGD*, CENTER FOR GLOBAL DEVELOPMENT, <http://www.cgdev.org/section/about/> (last visited Nov. 3, 2012).

<sup>229</sup> See generally BALDWIN & CAVE, *supra* note 8, at 9-16 (asking “Why regulate?”).

<sup>230</sup> See *supra* notes 145-52 and accompanying text (summarizing findings about the near-futility of transparency and financial literacy initiatives).

microfinance will have played little role. Abstract polysyllabic words speak to elites. This term has sited poor borrowers and savers at a distance.<sup>231</sup>

“The trouble with regulating microfinance,” in sum, has distinct facets, of which this Article has explored three. The first is definitional. A word whose meanings are obscure, contested, or multi-layered can function well elsewhere in a language, but regulation demands a more precise definition of the sector or activity in question than this term offers. Second, microfinance as a neologism has brought what looks like mood swings—optimism, pessimism, centrism—to a workaday challenge. A less distracted agenda, jargon- and buzzword-free, would return regulators to their task of making loans and savings more available and safer.<sup>232</sup> Third, microfinance as big tent is too big to be regulated, because it includes providers with too much divergence in their form and governance.<sup>233</sup> Policymakers must at the same time keep microfinance in focus as policy and recognize that it is not a single sector amenable to unitary regulatory attention.

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<sup>231</sup> See *supra* note 9 and accompanying text; see also *supra* Part II.B.3.

<sup>232</sup> See McNew, *supra* note 67.

<sup>233</sup> See Marc Labie & Roy Mersland, *Corporate Governance Challenges in Microfinance*, in *THE HANDBOOK OF MICROFINANCE* 283, 287 (Beatriz Armendáriz & Marc Labie eds., 2011) (arguing that attention to corporate governance is integral to regulating microfinance institutions).

