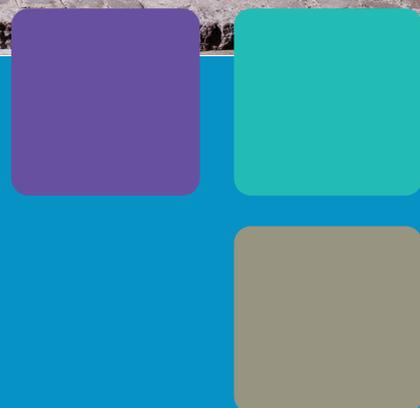


Microcredit regulation in Europe: An overview



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Introduction



Along with the evolution of microcredit over the last 20 years, the legislation on microcredit activities has formalised the presence of non-bank microfinance institutions (non-bank MFIs) in the market. In contrast to banks, non-bank MFIs are the primary microcredit providers in Europe, and they are not obligated to comply with full banking requirements to offer loans. Their main target clients are primarily excluded from the banking system and therefore non-bank MFIs play a key role in promoting financial inclusion. However, what is the current legislation for non-bank MFIs in Europe?

This paper examines the various legislative frameworks adopted in Europe. For EMN, this is part of a larger learning process that will help to identify regulatory approaches that are more conducive to the development of the sector. This is key to help policymakers improve their own framework, capturing the specificities of microcredit that EMN advocates for, based on EU good practices. For microfinance practitioners, this paper can be a practical tool to compare their context with that of their peers across Europe and engage in discussion with policymakers on regulatory issues.

The main data sources used for this paper are the existing literature on the topic and the EMN Legislative Mapping Reports [↗](#), a series of national fact sheets that provides a snapshot of the various legislative frameworks concerning

the provision of microcredit in Europe by non-bank MFIs. This series currently covers 22 countries across Europe¹ and is compiled from information provided by EMN members operating in the different countries.

This paper will be periodically revised to integrate new information from existing countries as well as updated to cover additional countries in an effort to provide the most comprehensive and up-to-date picture on microcredit regulation in Europe.

The paper is structured as follows: in section 1, microcredit is defined and its scope is presented from a European perspective; section 2 presents the differences between bank and non-bank MFIs models; section 3 provides an overview of the microcredit regulatory environment for non-bank MFIs and classifies European countries under three scenarios. The first scenario includes countries where the legislation recognises microcredit activities. The second scenario covers countries where the legislation does not recognise microcredit activities but non-bank MFIs can operate in the market. Finally, the third scenario encompasses countries where the legislation does not recognise microcredit activities and lending is restricted to banks.

¹ - 22 countries across EU Member States, candidate countries, and potential countries: Austria, Belgium, Bulgaria, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxembourg, Portugal, Romania, Spain, Sweden, the Netherlands, United Kingdom, Montenegro, North Macedonia, Serbia, Bosnia and Herzegovina, and Kosovo.

1. Microcredit definition and scope in Europe

The microfinance networks advocate for a revision of the EU definition of microfinance and microcredit that fully recognise the specificities of the sector in terms of target clients, MFIs' objective, non-financial support and range of products offered. See [EMN/MFC proposal for a revised EU definition of microfinance and microcredit](#).

Microcredit has emerged at the European level as a crucial policy tool to fight against social and financial exclusion, promote self-employment and support microenterprises. The EU is supporting microcredit providers mainly through the Employment and Social Innovation (EaSI) programme as well as the European Social Fund (ESF). For the next multiannual framework (2021-2027), the commitment of the EU towards the microfinance sector is expected to continue through the InvestEU and ESF+ programmes.²

The EU traditionally defined microcredit as loans up to EUR 25.000 granted to existing and potential micro-entrepreneurs at risk of social and financial exclusion.³ This broad interpretation of microcredit has been adopted in the two waves of EU support to the sector (2007-2013: Jasmine and Progress Microfinance; 2014-2020: EaSI programme) with the aim of embracing the diversity of microcredit practices across Europe.⁴

A new definition, which will influence the implementation of the new EU tools to support the sector (e.g. InvestEU), can be found in the ESF+ regulation:⁵ "microfinance includes guarantees, microcredit, equity and quasi-equity, coupled with accompanying business development services such as in the form of individual counselling, training and mentoring, extended to persons and micro-enterprises that experience difficulties accessing credit for the purpose of professional and/or revenue-generating activities."

This interpretation establishes the scope of EU support for microcredit. By contrast, there is no harmonised regulation on microcredit at the Member State level as this is left to the national legislator initiative or current market practice.

According to the definition above, microcredit—part of the microfinance toolbox—is intended to be a combination of credit and accompanying non-financial services that are provided to individuals and enterprises that are financially excluded. Interestingly, no thresholds for microcredit are currently set in the ESF+ regulation. A key element of the

ESF+ definition is the central role played by non-financial support, which is now considered as an inherent part of the microcredit disbursement. This designation echoes the current practice in the sector whereby the vast majority of the MFIs have adopted an integrated approach.

An element of continuity with the previous definition is that microcredit is explicitly intended to support income generating activities. This indicates that the provision of personal (social inclusion) microloans is not yet part of the EU agenda and differs from the approach adopted in some Member States (e.g. France, Italy) where personal microcredit was considered as important as business microcredit. Advocates of personal microcredit envision a product designed for disadvantaged individuals and low-income households who want to finance personal and family development projects or necessities arising from daily needs, potential risks and temporary or unforeseen circumstances (e.g. home expenses, health, education, disability requirements, and family reunification).⁶

Today, half of the MFIs in Europe offer personal microloans⁷, which differs from business microcredit since it is not immediately directed to the creation of income generating activities but is designed to cover personal or family needs that can have indirect positive effects on integration into the labour market (e.g. investment in education and training) and, more generally, on social inclusion.⁸ Personal microcredit differs from traditional consumer credit since it doesn't merely target consumption needs. Rather, the objective is to enhance the financial and social inclusion of beneficiaries. However, as practices are different across countries (and MFIs) and there is no common agreement on what can be considered a "legitimate" need to be financed with personal microcredit, it is difficult to track the provision of this product in a homogeneous way. Further research is needed to highlight the specific breadth of coverage of personal microloans in the European market and establish a common understanding of its scope.

2 - EMN, ADIE & Paris Europlace (2019), *European Microcredit Whitepaper*.

3 - Commission Staff Working Paper "Microcredit for European small businesses," SEC (2004)1156; "Competitiveness and Innovation Framework Programme," 1639/2006/EC; Commission recommendation 2003/361/EC.

4 - European Commission (2007), *The regulation of Microcredit in Europe. Expert Group Report*

5 - European Commission (2018), *Proposal for a Regulation of the European Parliament and of the Council on the European Social Fund Plus (ESF+)*.

6 - Corbucci, V. (2016), *Personal loans: The forgotten half of microcredit?*

7 - Diriker D., Landoni P. and Benaglio N. (2018), *Microfinance in Europe: Survey Report 2016-2017*.

8 - Corbucci, Valentina (2016), *Personal loans: the forgotten half of microcredit?*

2. Microcredit providers in Europe



The microcredit market in Europe is relatively fragmented, with most microcredit providers (88%) operating under the legal status of NGO, NBFi or credit unions/financial cooperative. In addition, MFIs also operate under other legal forms such as banks, and governmental bodies.⁹

A categorisation of these models can also be done according to their "legal" classification: MFIs with or without banking license.¹⁰

Non-bank MFIs operate in the market under different legal types, which can generally be aggregated by the following categories: NGOs, non-bank financial institutions (NBFi), credit unions/financial cooperatives, and to a lesser extent, public funds.

The NGO umbrella captures not-for-profit organisations such as foundations, charities, social purpose cooperatives, associations and religious institutions. These NGO MFIs typically grant loans to vulnerable populations in line with their social mission. NBFIs are primarily for-profit institutions that provide credit services similar to those of banks but generally target the lower end of the market. NBFIs are licensed under a separate category from banks, which in certain countries can correspond to a special regulation created for microcredit providers.

Finally, credit unions (also known as credit and saving unions or financial cooperatives) are membership-based organisations that aim to encourage savings and use pooled funds to make loans to members. Usually credit unions are allowed to lend money exclusively to natural persons (members) but it is accepted that some loans to individuals will be used for business purposes.¹¹ Credit unions are historically rooted in the Eastern part of Europe, and in some countries, they play an important role for microcredit, especially in rural areas. Due to the specificities of credit

union model, most credit unions have a dedicated regulation at the country level. For this reason, regulation on credit unions does not represent the main focus of this analysis (with minor exceptions when data was available).

For **Bank MFIs**, microcredit is a small part of their overall operations. Microcredit may be offered either as part of their CSR (corporate social responsibility) activities or as a type of specialised commercial activity. In Europe, the main categories of bank models providing microcredit include:

- ➔ Commercial banks with downscaling programmes or operating finance companies that provide microcredits;
- ➔ Savings and cooperative banks;
- ➔ Ethical banks that have a focus on social enterprises and micro-enterprises, providing first-tier or second-tier (wholesale) finance;
- ➔ Development and state-owned banks or funds; and,
- ➔ MFIs transforming into banks.¹²

As banks are fully regulated, including the disbursement of microloans, we focus our attention on the specific legislation that allows (or not) non-bank MFIs to disburse microcredits in this report.

Although banks and non-banks MFIs own a similar share of the portfolio in the European market, non-bank MFIs cater to the majority of the microcredit clients (66% of the active borrowers) with loans that are, on average (in particular NGOs and credit unions/financial cooperatives), smaller than loans offered by banks, which suggests that these MFIs serve poorer client segments.¹³

The legal framework under which non-bank MFIs operate is of primary importance since non-bank MFIs play a crucial role in supporting the social and financial inclusion of the most vulnerable clients.

9 - Diriker D., Landoni P. and Benaglio N. (2018), *Microfinance in Europe: Survey Report 2016-2017*.

10 - Bruhn-Leon B., Eriksson P. and Kraemer-Eis H. (2012), *Progress for Microfinance in Europe*.

11 - European Commission (2007), *The regulation of Microcredit in Europe. Expert Group Report*.

12 - Cozarenco, A. (2015), *Microfinance Institutions and Banks in Europe: The story to date*.

13 - Armendariz, B., and Szafarz, A. (2011), *On Mission Drift in Microfinance Institutions, The Handbook of Microfinance*, Singapore: World Scientific Publishing, pp. 341-366.

3. Overview of the microcredit regulatory environment for non-bank MFIs

The regulatory approach to microcredit differs from country to country due to diverse factors related to history, economy, and financial system development. Recognising that some key elements related to the banking law are set both at the European and national level is critical to understand the regulation that applies to non-bank MFIs in the provision of microcredits.

In Europe, the main regulations concerning banks are the European banking legislation and national banking laws.

EU regulation¹⁴ on the financial system establishes a set of micro-prudential rules for financial institutions. On the other hand, Member States are encouraged to implement rules with a macro-prudential oversight to preserve their own financial stability. These macro-prudential measures include assessments in relation to risk management which may ultimately affect the macroeconomic, fiscal and budgetary situation of the relevant Member State.¹⁵ In addition, each Member State is responsible to protect its depositors by adopting its own structural measures to authorise credit institutions to operate in the financial market.

According to the EU Banking law, a 'credit institution' is defined as "an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account."¹⁶ For the bank model, the factor determining whether an institution falls under the scope of EU banking legislation is the right to take deposits. Hence, according to the EU legislation, non-bank MFIs do not have any specific restriction to provide credits if they do not take deposits from the public.

It is also worth noting that the EU banking regulation does not include a definition for microcredit, as they do for other financial products like mortgage credit, payment services, deposit guarantee schemes, cross-border payments, and e-money. Therefore, the specific features of a microcredit product are currently defined only at the national level.

Based on this premise, Table 1 outlines the legal grounds under which non-bank MFIs are allowed to operate in their respective markets. Three main scenarios arise in this respect:

- ➔ **Existence of a microcredit legislation in the national law:** This scenario encompasses a variety of approaches ranging from countries that introduced a distinct category for microcredit providers (Bosnia and Herzegovina, France, Italy, Montenegro, Portugal and Kosovo) to others where microcredit is one of the products listed in the NBFi regulation (Romania, Montenegro);
- ➔ **No microcredit legislation, but non-bank lenders¹⁷ can disburse loans:** This provides the legal ground for non-bank MFIs to directly offer microcredit (Belgium, Bulgaria, Finland, Hungary, Ireland, Luxembourg, North Macedonia, Spain, Sweden, the Netherlands and UK); and,
- ➔ **No microcredit legislation and the banking law limits the lending business to banks (banking monopoly):** The provision of microcredit is prevented or highly restricted for non-bank MFIs unless they partner with banks (Austria, Germany, Greece and Serbia).

¹⁴ - The EU regulations are legal acts that apply automatically and uniformly to all EU countries without needing to be transposed into national law. They are binding in their entirety on all EU countries.

¹⁵ - Regulation (EU) No 575/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (page 3). [↗](#)

¹⁶ - Regulation (EU) No 575/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (Page 18). [↗](#)

¹⁷ - We define non-bank lenders as a wide category of financial providers that offer loans of various sizes. Non-bank MFIs are non-bank lenders offering small loans. Other examples of non-bank lenders can be an NBFi whose mission is to provide larger loans to SMEs or a crowdfunding/fintech platform.

Table 1

➔ Overview of microcredit regulation by EU Member States, candidate and potential countries.

	With microcredit regulation	Without microcredit regulation and without bank monopoly for lending	Without microcredit regulation and with bank monopoly for lending
EU 28			
Austria	-	-	✓
Belgium	-	✓	-
Bulgaria	-	✓	-
Croatia*			
Cyprus*			
Czech Republic*			
Denmark*			
Estonia*			
Finland	-	✓	-
France	✓	-	-
Germany	-	-	✓
Greece	-	-	✓
Hungary	-	✓	-
Ireland		✓	
Italy	✓	-	-
Latvia*			
Lithuania*			
Luxembourg	-	✓	-
Malta*			
Poland*			
Portugal	✓	-	-
Romania	✓	-	-
Slovakia*			
Slovenia*			
Spain	-	✓	-
Sweden	-	✓	-
The Netherlands	-	✓	-
United Kingdom	-	✓	-
CANDIDATE COUNTRIES			
Albania*			
Montenegro	✓	-	-
North Macedonia	-	✓	-
Serbia	-	-	✓
Turkey*			
POTENTIAL CANDIDATE COUNTRIES			
Bosnia and Herzegovina	✓	-	-
Kosovo	✓	-	-

Table elaborated by the authors based on the information presented in the EMN country regulatory reports.

*: Countries not covered by the EMN Country Reports.

This categorization and subsequent analysis are based on data gathered by the EMN in its country regulatory reports, the revision of the existing primary regulation on

microcredit at the national level and the (limited) literature on regulation at the EU level.

3.1 Countries with microcredit regulation

During the last 20 years, seven countries decided—with different modalities—to adopt legislation on microcredit: four EU Member States, one candidate country, and two

potential candidate countries. Information regarding the implementation of the legislation is presented in Table 2.

Table 2

➔ Specific regulation for microcredit provision

Country	Main Laws	Chapter / Article	Law passed	Supervisory authority
France	Monetary and Financial Code ↗	L. 511-6-5	2001	Central Bank (ACPR, 'Autorité de contrôle prudentiel et de résolution')
Italy	Consolidated Law on Banking ↗	Title V, Subjects operating in the financial sector; articles 111, 113	2010*	Bank of Italy
Portugal	Legislative Decree no. 12/2010 ↗ and Ordinance no. 1315/2010 ↗	/	2010	Bank of Portugal
Romania	Law on non-bank financial institutions (no. 93/2009) ↗ and Regulation no. 5/2012	/	2009	National Bank of Romania
Montenegro	Law on financial leasing, factoring, purchase of receivables, micro-lending and credit-guarantee operations ↗	Chapter V, Micro-lending; articles 88 - 95	2017	The Central Bank of Montenegro
Bosnia and Herzegovina	Law on Microcredit Organizations Federation Bosnia and Herzegovina (no. 59/06), and Law on Microcredit Organizations Republic of Srpska (no. 59/06) ↗	/	2006	The Banking Agency of the Federation of Bosnia and Herzegovina; and The Banking Agency of Republic of Srpska
Kosovo	Law on banks, microfinance institutions and non-bank financial institutions (no. 04/L-093) ↗	Chapter II, Microfinance Institutions and non-bank financial institutions	2008	Central Bank of Kosovo

* Implementing rules were issued in 2014.

The earliest legislation on microcredit was introduced in France in 2001, followed by Bosnia and Herzegovina (2006) and Kosovo (2008). Italy and Portugal both passed a law in 2010, although Italy implemented the rules four years later. The most recent legislation was passed in Montenegro in 2017.

Microcredit regulation was passed with different approaches in these countries. In **France, Italy, Kosovo, Bosnia and Herzegovina and Portugal**, the **legislation establishes the scope and rules for microcredit provision and introduces a distinct category for non-bank MFIs**. These are specialised microcredit providers that can operate only under certain conditions established by the law (see 3.1.1).

In the case of France, Italy and Kosovo, microcredit regulation is incorporated into the banking law. In Bosnia and Herzegovina and Portugal, the regulation consists either of a single law or decree that covers the provision of microcredit in the country.

By contrast, **Romania and Montenegro** reference microcredit in the NBFi regulation and there is no distinct category for microcredit providers. In both countries **NBFIs can offer a wide array of financial products, among which microcredit is explicitly mentioned**.

A common element in these regulatory frameworks is that the supervisor of the non-bank MFIs is the National Bank.

Interestingly, Romania had a dedicated law on MFIs before it adopted the current law on NBFIs (2009). The MFI law passed in 2005 (Law no. 240/2005) and introduced a legislative framework that recognised microcredit activity and specified that only MFIs and banks could offer microloans under the supervision of the National Bank of Romania. The law also obliged NGOs operating the sector to transform into joint stock companies and established a minimum capital requirement (EUR 200,000).¹⁸ In 2009, the law on MFIs was revoked and substituted by the current law on NBFIs who are allowed to offer a wider array of financial

¹⁸ - A joint-stock company is a business owned by its investors, with each investor owning a share based on the amount of stock purchased. Joint-stock companies are created to finance endeavours that are too expensive for an individual or even a government to fund. The owners of a joint-stock company expect to share in its profits. [↗](#)

products, including microcredit. In the current law, MFIs lost their distinct status¹⁹ and there is no trace of a microcredit definition.

It is also worth noting that in Portugal, although a law for non-bank MFIs was established in 2010 (along with a

national microcredit program that can be delivered both by banks and MFIs), microcredit provision is only done by banks. In Portugal, there are no non-bank MFIs operating in the market.

3.1.1. Type of non-bank MFIs

In the existing regulations on microcredit, the legislator established rules that facilitate or prevent the creation of new MFIs and influence the business model for MFIs wanting to operate in the market. In this report, we consider

three specific types of requirements (Table 3): legal type, minimum capital requirements and authorized funding options.

Table 3

➔ Specific regulation for microcredit provision

Country	Non-bank lenders qualified to offer microcredit	Minimum Capital	Authorised resources for lending
France	Non-profit associations/organisations, recognized public-interest foundations	Not defined	<ul style="list-style-type: none"> ➔ Own funds ➔ Credit contracted with credit institutions
Italy	Specialised microcredit operators: limited companies, cooperative limited companies	EUR 250.000	Not defined
	Non-profit organisations: associations, foundations, mutual aid societies; local and governmental agencies; social cooperatives; non-profit cooperatives	Not defined	Not defined
	Other non-bank lenders that adhere to the criteria of Art. 111 ²⁰		
Portugal	Microcredit financial companies (for-profit)	EUR 1.000.000	Not defined
Romania	NBFIs (joint-stock companies)	<ul style="list-style-type: none"> ➔ EUR 200.000 ➔ EUR 3.000.000 (if NBFIs disburse mortgages) 	Own funds and additional capital (reserves or subordinated loans received)
	Credit Unions (under law no. 93/2009 and 122/1996)	Not defined	Not defined
Montenegro	NBFIs (joint-stock companies, limited liability companies)	EUR 125.000	<ul style="list-style-type: none"> ➔ Own funds ➔ Credit contracted with credit institutions
	Credit unions	N/A	N/A
Bosnia and Herzegovina	Microcredit foundations (non-profit)	EUR 25.565 (50.000 KM)	Not defined
	Microcredit companies (for profit)	EUR 255.646 (500.000 KM)	Not defined
Kosovo	MFI commercial entities (joint-stock companies)	EUR 200.000	Not defined
	Licensed NGO MFIs (not-for profit)	EUR 200.000	Not defined
	NBFIs (for-profit)	Dependent upon the particular activities (e.g. EUR 300.000 for loans)	Not defined

19 - Barković, I. and Lulić, M. (2015), Contemporary Legal and Economic Issues V.

20 - Non-bank financial Intermediaries (for profit organisations regulated under the article 106 of the banking law) and mutual financial operators (cooperatives with specific by-law conditions) can also offer microloans and use this denomination for their products provided that they adhere to the criteria of Art. 111.

With respect to the legal type that can be adopted by microcredit providers, in some countries, microcredit provision can only be performed by commercial entities, e.g. Portugal, Romania (excluding credit unions that disburse microloans under a different law) and Montenegro. By contrast, the French law is the only one that restricts the disbursement of microloans to organisations that are not-for-profit. In the remaining cases (Italy, Bosnia and Herzegovina, and Kosovo), the legislator opted for a mixed approach where both not-for-profit and for-profit organisation can operate in the market.

Minimum capital requirements vary considerably by country, in part due to the different purchasing power across these countries. In most cases, the legislator defined a minimum capital requirement, although in France and Italy that limit is not set for not-for-profit organisations in the main regulation. The minimum capital requirement of Portugal is an outlier (EUR 1 million) and could explain the absence of non-bank MFIs in the country.

With the exception of Portugal and the threshold set for NBFIs, the lowest and highest capital requirements to set up an MFI can be found in Bosnia and Herzegovina. In this context, a microcredit foundation can be created with a relatively modest equity base (EUR 25.565) while

3.1.2. Microcredit product(s) and specific features

This section highlights the different approaches being taken by legislators to define the products that non-bank MFIs can offer to clients. To this end, we selected and compared several elements related to microcredit conditions and objectives detailed in the primary legislation on microcredit, which are highlighted in Table 4.

In **France, Italy, and Montenegro**, the legislator has defined two products with unique conditions and objectives: **business and personal microcredits**. The Italian and French legislation are very specific in the conditions of both microcredit products (in terms of loan amount and term, interest cap) and their policy objectives (purpose of the loan and its beneficiaries). By contrast, the law in Montenegro is less prescriptive and limits its scope to defining the maximum loan amounts for business and personal microcredit.

Interestingly, the maximum size for both business and personal microcredit is lower in France compared to Italy (half of the size) and Montenegro (one-fourth of the size). Considering the profile of microcredit clients in France, the purpose of the loans and the nature of the organisations that can offer microcredit (exclusively not-for-profit), the French approach seems particularly focused on the needs of the most vulnerable clients. On the other hand, it is also worth

microcredit companies, which are of a commercial nature, need ten times more capital to start operations. This threshold is similar to the one for specialised microcredit operators in Italy (EUR 250.000), which is defined as five times the minimum capital for joint stock companies as set by the Italian civil law. Interestingly, in 2014, the minimum capital requirement for joint stock companies in Italy was reduced from EUR 120.000 to EUR 50.000, which led to a robust reduction of the capital foreseen to set up a for-profit MFI (from EUR 600.000 to EUR 250.000).

In Kosovo, both for-profit and non-profit MFIs have the same minimum capital level, a different approach compared to the regulation in Bosnia and Herzegovina.

In all countries, with the exclusion of credit unions, non-bank MFIs are prevented from deposit-taking. Their funding must come from their own funds and credit contracted with credit institutions, although the authorised resources for lending are not always specified in the primary legislation. There is a debate in the sector concerning the role of deposits as an alternative source of finance. Micro-savings are more volatile, and their balances are lower compared to savings accounts more generally. Often, micro-savings are perceived as an additional product for the poor rather than a source of funding.

stressing that honour (zero interest) loans, often disbursed together with a microcredit, are widely available in France.²¹ The average size of an honour loan in France fluctuates between EUR 9.700 and EUR 30.000 according to the issuing institution.²² This compensates for the relatively low microcredit size in France, which is limited to EUR 12.000.

In Montenegro, considering the maximum microloan size and the lower purchasing power compared to Italy and France, the legislation allows MFIs to cater to a wider spectrum of clients, which includes MSMEs with business loans up to EUR 50.000 and individuals with personal loans up to EUR 20.000.

The Italian approach lies closer to the French case than the Montenegrin environment. In fact, although microcredit thresholds are higher in Italy than in France, the primary target segment in the Italian law is the vulnerable population (small entrepreneurs and social and financially excluded people), and the MFIs are trying to balance social and sustainable objectives.

In **Portugal, Romania, Bosnia and Herzegovina, and Kosovo**, the legislation refers generically to microcredit without introducing any additional distinction among products,

21 - <http://www.initiative-france.fr/>

22 - <https://bpifrance-creation.fr/encyclopedie/financements/financement-fonds-propres/pre-donneur>

Table 4

➔ Microcredit definition and features according to the country legislation

Country	Product	Max. amount	Max. term	Interest cap	Purpose of the microcredit	Target clients	Mandatory non-financial support
France	Professional microcredit	EUR 12.000	5 years	Not defined in the law	To create and develop small enterprises (up to 3 employees)	Anyone willing to start and/or develop a business	Not defined in the law
	Personal microcredit	EUR 5.000	5 years	Yes, in accordance with the anti-usury legislation	Access to, maintenance of, or return to a job or social integration project not directly linked to a professional objective	Physical persons facing difficult financing, whose loan repayment capacity is judged to be sufficient and who are receiving social support	Not defined in the law
Italy	Entrepreneurial microcredit	EUR 25.000 (+ EUR 10.000 in special cases*)	7 years (or 10 years**)	Yes, in accordance with the anti-usury legislation	To support entrepreneurial activities	Self-employed individuals within their first five years of activity or microenterprises	Technical assistance, tutoring and monitoring
	Social microcredit	EUR 10.000	5 years	Yes, linked with the average market annual percentage rate	To support social and financial inclusion	Individuals who are experiencing economic or social vulnerability (e.g. unemployment, poor standard living conditions)	Technical assistance, tutoring and monitoring
Portugal	Business microcredit	EUR 25.000	Not defined in the law	Not defined in the law	To develop an economic activity.	Unemployed people with motivation and capacities to work in any economic activity and with desire to be a microentrepreneur	Monitoring
Romania	Microcredit	Not defined in the law	Not defined in the law	No	Not defined in the law	Not defined in the law	Annual information and education activities
Montenegro	Business microcredit	<ul style="list-style-type: none"> ➔ EUR 30.000 for microcredit to entrepreneurs ➔ EUR 50.000 for microcredit to MSMEs 	Not defined in the law	Not defined in the law	Not defined in the law	<ul style="list-style-type: none"> ➔ Entrepreneurs ➔ MSMEs 	Not defined in the law
	Personal microloan	EUR 20.000	Not defined in the law	Not defined in the law	Not defined in the law	Natural persons	Not defined in the law
Bosnia and Herzegovina	Microcredit	<ul style="list-style-type: none"> ➔ Microcredit foundation: EUR 5.106 (KM 10.000) ➔ Microcredit company: EUR 25.532(KM 50.000) 	Not defined in the law	Not defined in the law	To improve the financial position of microcredit beneficiaries, increasing employment, providing the support to the development of entrepreneurship and acquisition of profits	Not defined in the law	Not defined in the law
Kosovo	Microcredit	EUR 25.000***	Not defined in the law	Not defined in the law	Not defined in the law	<ul style="list-style-type: none"> ➔ Low-income households and individuals ➔ Micro and small legal entities 	Not defined in the law

* During the first loan, clients can receive an additional loan up to EUR 10.000.

** Loan term could be 10 years if the credit is for training and is provided by a mutual organisation.

*** The total amount of annual debt service, including principal and interest, for all loans may not exceed 25% of the individual's total annual income.

which allows MFIs the possibility to define their offer. Currently, where microcredit is not further defined, MFIs offer both business and personal microcredit and the features are defined by the internal policy of the MFIs in accordance with existing legislation. In these countries, given the broad scope of the microcredit interpretation and the absence of specific conditions (interest rate, terms, etc.), the main characteristic defining microcredit is the maximum loan amount. In this respect, these legislations share the same maximum threshold (EUR 25.000) in line with the definition at the EU level. The only exception is Romania, where the legislation does not establish a maximum amount for microcredits. In this case, the only limitation in loan disbursement is an evaluation of the repayment capacity and risk profile of the client.

Interestingly, in Bosnia and Herzegovina the maximum amount for a microloan is set according to the legal type of

the MFI. As a result, microcredit companies can offer loans which are five times larger than microcredit foundations. This also differs from the approach in France, Italy and Montenegro where the maximum amount is linked to the specific product offered.

In Italy and Portugal, the law establishes compulsory monitoring for microcredit usage. Moreover, the Italian legislation envisages mandatory technical assistance and tutoring for clients. Romania is the only country that established financial education as a mandatory non-financial service.

Most countries do not have interest rate caps, and only Italian and French (personal microloans only) law established an interest rate cap. In Romania, the interest rate cap set for the overall financial market, which was also applicable to NBFIs and credit unions, was removed in March 2019.

3.2. Countries with no microcredit legislation but where non-bank lenders are allowed to disburse loans

In this section, we provide an overview of the countries where the existing legislation is suitable for microcredit operations. Although there is no explicit microcredit legislation in these countries, non-bank lenders can disburse loans if they do not take deposits.²³ This framework provides the legal ground for non-bank MFIs to directly offer microcredit. However, since the scope of microcredit is not defined in the law, the specific features of the products offered and labelled as "microcredit" are defined by the internal policy of

each non-bank MFI in compliance with the overall legislative conditions for credit institutions and consumer/corporate loans applicable in the country.

For each country, there are several types of non-bank lenders that are allowed to offer business and personal loans; the maximum size depends on the legislation in place. An overview of these legislative schemes is provided in Table 5.

²³ - Except for Credit Unions that have their own regulation.

Table 5

→ Overview of legislation allowing non-bank lenders to grant (micro)loans

Country	Legislation allowing non-bank lenders to operate	Supervisory authority	Examples of non-bank lenders	Type of loans that non-bank lenders can offer	Max. Amount	Interest rate cap
Belgium	Banking and Consumer laws	<ul style="list-style-type: none"> ➔ No supervision is foreseen for non-bank MFIs by FSMA (Financial Service and Management Authority) for business loans ➔ Non-bank MFI providing personal loans must have an agreement from FSMA 	<ul style="list-style-type: none"> ➔ Social cooperatives ➔ Credit cooperatives ➔ ASBL (associations) 	<ul style="list-style-type: none"> ➔ Business loans ➔ Personal loans 	No restrictions	18% per annum on personal loans
Bulgaria	Law on Credit Institutions: Article 3a on non-bank financial institutions; Transitional and Final Provisions no 12 on Credit Cooperatives	Bulgarian National Bank	NBFIs: Joint-stock company, limited liability company, sole-owner joint-stock company	<ul style="list-style-type: none"> ➔ Business loans ➔ Personal loans ➔ Agricultural loans 	No restrictions	50% per annum on personal loans*
			Agricultural credit cooperatives (Mutual aid credit cooperatives)	<ul style="list-style-type: none"> ➔ Personal loans ➔ Agricultural loans 		
	Bulgarian commercial law	No supervision	Joint stock company and limited company disbursing loans to their members only	<ul style="list-style-type: none"> ➔ Business loans ➔ Personal loans ➔ Agricultural loans 		
Finland	Crowd Funding Law	Mandatory registration at the Financial Supervisory Authority but no supervision	Shareholder companies	Business loans	EUR 2,500,000	No restrictions
				Personal loans	No restrictions	50% for loans under EUR 2,000
Hungary	Act CCXXXVII on Credit Institutions and Financial Enterprises	Prosecutor's office	<ul style="list-style-type: none"> ➔ Financial enterprises (joint-stock companies) ➔ Saving cooperatives ➔ Foundations 	Business loans to SME and micro-enterprise segment	No restrictions	No restrictions
	Act CXII (1996) allows foundations to disburse loans from the National Microcredit Scheme	No supervision	<ul style="list-style-type: none"> ➔ County foundations for enterprise promotion (Local Enterprises Agencies - LEAs) 			

* 5 times the statutory interest, it is defined by the government and used for all kind of delayed payments (e.g. unpaid taxes, legal cases, etc.).

Table 5

→ Overview of legislation allowing non-bank lenders to grant (micro)loans

Country	Legislation allowing non-bank lenders to operate	Supervisory authority	Examples of non-bank lenders	Type of loans that non-bank lenders can offer	Max. Amount	Interest rate cap
Ireland	<ul style="list-style-type: none"> → Consumer banking law → Code of Conduct for Business Lending to SMES 	Central Bank of Ireland	<ul style="list-style-type: none"> → NBFIs (commercial lending institutions) → Credit unions 	<ul style="list-style-type: none"> → Business loans → Personal loans 	No restrictions	No restrictions
	<ul style="list-style-type: none"> → The Microenterprise Loan Fund Act → Specific governmental mandate to a non-bank MFI 	No supervision	Not-for-profit private company subject to an Act of Government and a Statutory Instrument (Microfinance Ireland)	Business loans to enterprises (sole-traders, partnerships or limited companies) to support start-up costs, working capital or small assets purchases	EUR 25.000	5% margin over cost of funds on a loan portfolio basis
Luxembourg	Consumer Credit Law	Supervisory Commission of the Financial Sector (CSSF)	Institutions labelled as Professionnel du Secteur Financier (PSF)	<ul style="list-style-type: none"> → Business loans → Personal loans 	No restrictions	No restrictions
			A limited company was exempted of the status of PSF (Microlux)	Personal loans (currently not provided by Microlux)	EUR 10.000 (ad hoc agreement with the CSSF)	No restrictions
			Business loans	EUR 25.000 (ad hoc agreement with the CSSF)		
Spain	Law 16/2011, consumer credit agreements	No supervision	<ul style="list-style-type: none"> → Private companies (limited liability companies or limited by partnership companies) → Foundations and associations 	<ul style="list-style-type: none"> → Business loans → Personal loans 	No restrictions	No restrictions
	N/A	No supervision	Financial Cooperatives	N/A	N/A	N/A
Sweden	<ul style="list-style-type: none"> → Legal framework for consumer and corporate credit institutions → Consumer Credit Law (if personal loans) 	Supervised by Financial Authority (FI)	Corporations	<ul style="list-style-type: none"> → Business loans → Personal loans 	No restrictions	No restrictions

Table 5

➔ Overview of legislation allowing non-bank lenders to grant (micro)loans

Country	Legislation allowing non-bank lenders to operate	Supervisory authority	Examples of non-bank lenders	Type of loans that non-bank lenders can offer	Max. Amount	Interest rate cap
The Netherlands	Financial Supervision Act	<ul style="list-style-type: none"> ➔ No supervision for business microloans ➔ Authority for Financial Markets (AFM) for consumer loans & investment funds & crowd funding 	<ul style="list-style-type: none"> ➔ NBFIs: private company, limited company, cooperative (for-profit) ➔ Association and foundations (non-profit) ➔ Credit unions ➔ Crowdfunding platforms ➔ Fintech lending applications 	<ul style="list-style-type: none"> ➔ Business loans ➔ Operational lease ➔ Working Capital 	No restrictions	No restrictions
				<ul style="list-style-type: none"> ➔ Personal loans provided by non-bank lenders with an AFM license 	Depends on the permission received from AFM	14% per annum
United Kingdom	Consumer Credit Act	Financial Conduct Authority (FCA) for credit offered to individuals and business**	Community development finance institutions (CDFIs): Company limited by guarantee or by shares, Co-operative and community benefit society, community interest company, etc.	<ul style="list-style-type: none"> ➔ Business loans ➔ Personal loans ➔ Social enterprise loans 	No restrictions	CDFIs: a total cost cap of 100% for short-term loans (less than 12 months)
				<ul style="list-style-type: none"> ➔ The Co-operative and Community Benefit Societies Act 2014 ↗ ➔ Credit Unions Act 1979 ↗ ➔ The Legislative Reform (Industrial and Provident Societies and Credit Unions) Order 2011 ↗ ➔ Credit Unions (Northern Ireland) -Order 1985 ↗ 	Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA)	- Credit unions
North Macedonia	Law on associations and foundations jointly with the law on obligations	No supervision is foreseen for associations and foundations	Associations and foundations			
	Law on financial companies	<ul style="list-style-type: none"> ➔ Ministry of Finance 	Financial companies	<ul style="list-style-type: none"> ➔ Business loans ➔ Personal loans 	No restrictions	Reference rate set by the Central Bank: +8% (personal loans) and +10% (business loans)***
	Banking law	Central Bank	Saving houses (deposit-taking, non-bank MFI)			

** Customers who are a sole trader, a partnership with fewer than four partners, or an unincorporated association. All other business lending in the UK is unregulated.

*** Reference is adjusted every 6 months.

In Belgium, Ireland, Luxembourg, Spain, Sweden and the UK, non-bank lenders operate under the national consumer law, although the loans disbursed are meant to finance enterprises.

In the Netherlands, Spain, Sweden and Ireland, the flexibility of the regulation opens the gates for crowdfunding platforms and fintechs to operate in the market. Finland is the only country with a law on crowd funding, under which non-bank MFIs can operate.

In some countries, an individual agreement allowed for the creation of ad-hoc non-bank MFIs (Ireland, Luxembourg) or established a specific category of non-bank lenders that pursue social and financial inclusion goals (UK). Additionally, in one country, an exemption was made in the banking law to allow non-profit, semi-public entities to disburse microloans under a national programme on microcredit (Hungary).

Although Ireland and Luxembourg do not have specific microcredit legislation, some non-bank MFIs individually agreed on the conditions under which they can offer microloans to help start-up microentrepreneurs with the relevant supervisory body and the government. These organisations were granted authorisation to offer microcredit because they are deemed crucial to reach a specific policy purpose: filling a market gap supporting the smallest businesses in their country that would otherwise be financially excluded.

In Ireland, the National Central Bank allows one non-bank MFI (Microfinance Ireland) to grant microcredits through an Act of Government and a statutory instrument. This non-bank MFI is a non-profit institution and is permitted to offer business microcredits up to EUR 25.000 to microenterprises with a maximum duration of five years for start-up expenses, working capital or small asset purchases. This business microcredit is subject to a maximum 5% interest rate margin over cost of funds on a loan portfolio basis.

A similar case also occurs in Luxembourg where Microlux, a limited company exempted of the status of Professionnel du Secteur Financier (PSF), provides business microcredits under a specific permission from the Supervisory Commission of the Financial Sector (CSSF). Microlux defines business microcredit as a credit up to EUR 25.000 for business creation or business development. Recently, Microlux has also agreed with the CSSF to offer personal microloans that increase the employability of clients entering the labour market (e.g. buying a car). In this case, there is no interest rate cap in place. Microlux also offers non-financial services like coaching and training.

In the UK, the Consumer Credit Act introduced a special status for community development finance institutions (CDFIs).²⁴ CDFIs aim to grant access to finance for businesses that find it hard to raise money like start-ups, sole traders, informal and unincorporated ventures and microenterprises employing fewer than ten people. They provide loans and support to individuals and enterprises unable to access finance from the mainstream financial services sector, thereby enabling them to contribute to their local economy.²⁵ CDFIs can disburse personal, business and social enterprise loans, however, these credits do not have any loan amount restrictions. There is an interest rate cap in place for short term loans (up to 12 months). CDFIs are part of the Responsible Finance network.

In Hungary, Act No. CXII of 1996 on Credit Institutions and Financial Enterprises was previously interpreted in a restrictive way that required bank involvement in not-for-profit microcredit programmes. In 1998, the Hungarian Parliament amended Act No. CXII of 1996 on Credit Institutions and Financial Enterprises to remove the crediting activity performed under the National Microcredit Scheme. As a result, the provision of credit by county foundations for enterprise promotion, and performed in the framework of the National Microcredit Scheme, no longer falls under Act.²⁶ However, it is important to stress that county foundations for enterprise promotion are no longer involved by the government in the delivery of microcredit, which is currently done by banks.

24 - CDFIs are not allowed to take deposit from the public. The funding is received from commercial and social lenders, grants from the government.

25 - Hadjimichael, T. (2014), Inside Community Finance-The CDFI industry in the UK 2014.

26 - European Microfinance Network (2012), Legal & Regulatory Working Group: A collection of Case studies on the Legal and Regulatory Framework for Microfinance.

3.3. Countries with no microcredit legislation and where the banking law restricts lending business to banks

In Austria, Germany, Greece and Serbia, the regulatory framework does not consider microcredit activities and **non-bank lenders are prevented or highly restricted from operating in the market**. The banking monopoly results from the **banking law formally forbidding non-bank lenders the ability to offer credit** (Austria and Serbia) **or because the rules set by the banking law make it impossible for a non-bank lender to enter/operate in the market** (Germany and Greece).

In Austria, the banking law forbids non-bank lenders to lend money, and the provision of microloans in Austria is primarily carried out via the social banking programme of Erste Bank in partnership with the Ministry of Labour. In Serbia, non-bank lenders are not authorised to disburse loans, and most non-bank MFIs operate as limited liability companies in partnership with banks. The only non-bank MFI that can lend money directly to legal entities, entrepreneurs and farmers is the Serbian Development Fund, operating under the Law on Development Fund. The role of MFIs is typically to approach potential clients, screen them and prepare their files for the bank to review. The bank gives the final approval and disburses the loan. In this kind of partnership, the MFIs work as a management consulting firm while the loan portfolio is on the books of the bank.

In Germany, the provision of loans by non-bank lenders is possible only under strict conditions related to the size to

the portfolio, the number of loans and the interest rate. According to the German banking law, the portfolio of a non-bank lender is limited to EUR 500.000. A banking license is required if (1) the portfolio exceeds EUR 500.000 with a minimum of 21 loans or (2) a non-bank lender has issued more than 100 loans. In addition, the offer of loans with an interest rate above 0% also requires a banking license. In this context, some associations and cooperatives can provide loans to their members without a banking license provided they comply with the above-mentioned limitations. However, since loan provisioning at an interest rate of 0% is not sustainable, exemption from banking regulation is hardly used in practice.

In Greece, the banking law states that non-financial institutions that are licensed by the Bank of Greece require a minimum capital of EUR 18 million to carry out financial or credit activities. A partnership with a licensed bank is therefore required by all legal entities (such as associations, foundations, entrepreneurship programs, European programs, etc.) that are interested in serving the microcredit market. Within this forced partnership model, NGOs screen potential clients and provide non-financial services both pre- and post- loan disbursement. Banks assess the applications received, disburse the loan (using their own capital) and are responsible for monitoring client performance and any recovery actions.

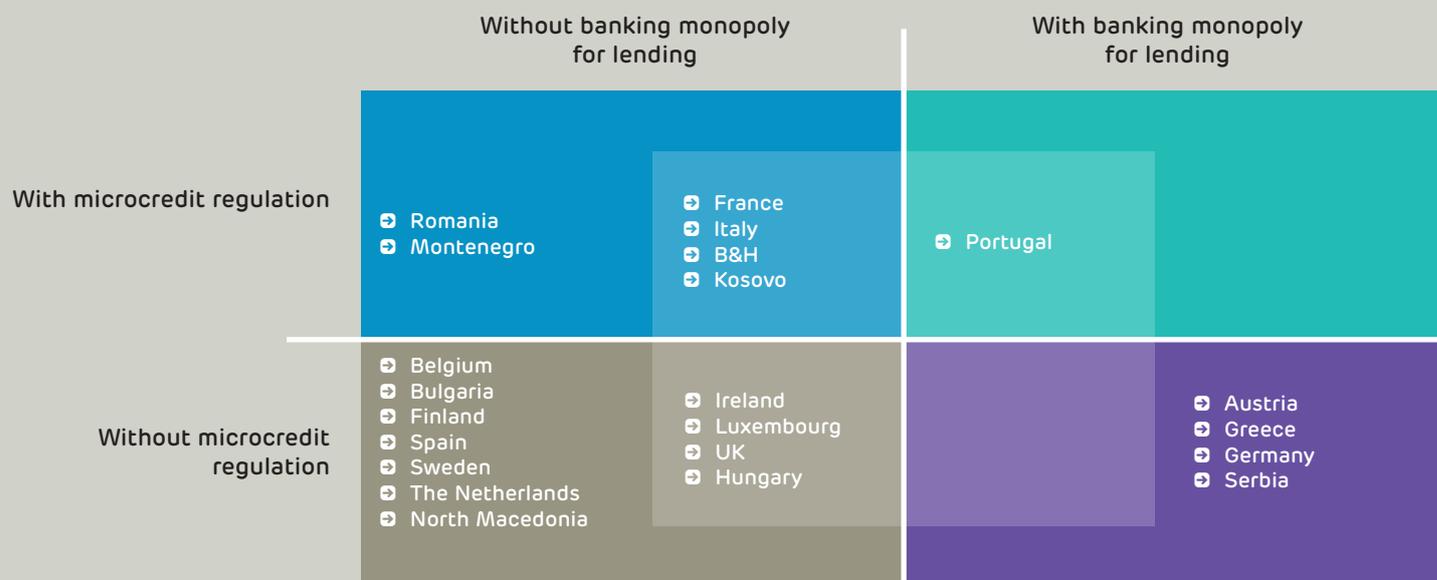
Conclusions

Although banks and non-bank MFIs have a similar share of the European microcredit portfolio, non-bank MFIs cater to the needs of a different client segment by offering loans that are, on average, smaller than those offered by banks. Therefore, the legal framework under which non-bank MFIs operate has an important social role since non-bank MFIs play a crucial role in supporting the social and financial inclusion of the most vulnerable clients. Depending on the legislation implemented, the regulatory environment can either support or prevent the development of the sector in Europe and the achievement of its social goals.

The microcredit market and regulatory environment that non-bank MFIs operate in is highly heterogeneous across European countries. This paper describes three main scenarios for the operations of non-bank MFIs based on the existence (or not) of microcredit regulation and the presence (or not) of a banking monopoly for lending, as illustrated in Graphic 1.

Graphic 1

➔ Overview of the microcredit regulation in Europe



Lighter color for each sector: Special Category/Status for non-bank MFIs

1) Existence of microcredit legislation in the national law: during the last 20 years, seven European countries adopted legislation on microcredit. In France, Italy, Kosovo, Bosnia and Herzegovina and Portugal, the legislation establishes the scope and rules for microcredit provision and introduces a distinct category for non-bank MFIs. These are specialised microcredit providers that can only operate under certain conditions established by the law.

On the other hand, in Romania and Montenegro, reference to microcredit is found in the NBFIs regulation and there is no distinct category for microcredit providers. In both countries, NBFIs can offer a wide array of financial products, among which microcredit is explicitly mentioned.

A common element of these regulatory frameworks is that the National Bank serves as the supervisor of non-bank MFIs.

In France, Italy, and Montenegro, the legislator has defined two unique products: business and personal microcredits. By contrast, in Portugal, Romania, Bosnia and Herzegovina, and Kosovo the legislation refers generically to microcredit without introducing any distinction among products, which allows MFIs to define their microcredit offer.

Although a law on microcredit was passed in 2010 in Portugal, there are currently no non-bank MFIs in the country. This might be due to the high minimum capital requirement set for microcredit financial companies. As a result, no institutions are exclusively providing microcredit in Portugal, and only banks offer microcredits as part of their social responsibility policies or in the framework of public programs.

2) No microcredit legislation, but non-bank lenders are allowed to disburse loans: in Belgium, Bulgaria, Finland, Hungary, Ireland, Luxembourg, North Macedonia, Spain, Sweden, the Netherlands and the UK, existing legislation is suitable for microcredit operations. In these countries, although there is no explicit microcredit legislation, non-

bank lenders can disburse loans if they do not take deposits. This framework provides the legal basis for non-bank MFIs to offer microcredit. However, as the scope of microcredit is not defined in the law, the specific features of the products offered and labelled as "microcredit" are defined by the internal policy of each non-bank MFI in compliance with the overall legislative conditions for credit institutions and consumer/corporate loans applicable in the country.

In this context, organisations in Ireland and Luxembourg have engineered individual agreements with the government and supervisory body to create non-bank MFIs in the country. In the UK, a specific category of non-bank lenders that pursue social and financial inclusion goals was established (CDFIs). Additionally, in Hungary, an exemption was made in the banking law to allow semi-public, non-profit entities to directly disburse microloans under a national programme on microcredit.

3) No microcredit legislation and the banking law limits the lending business to banks: in Austria, Germany, Greece and Serbia a regulatory framework for microcredit activities does not exist and non-bank lenders are prevented or highly restricted from operating in the market. The resulting banking monopoly can be attributed to the banking law formally forbidding non-bank lenders from offering credit (Austria and Serbia) or because the rules set by the banking law makes it impossible for a non-bank lender to enter/operate in the market (Germany and Greece).

Final thoughts: With the information currently available, it is not yet possible to assess the benefits and limitations of each approach or how the different legislative approaches affect MFIs and their clients. More in depth analysis is needed for each individual country to assess the approaches which are more favourable for the development of the sector, and most importantly, for the overall financial inclusion of vulnerable people in Europe.



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