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Development of Private Credit Bureaus Lessons from Romania

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Executive Summary:

The explosion of retail credit in Romania during 2000–2004 caused an urgent need for greater capacity and specificity in credit reporting. In response to this demand, in a period of less than six months, government bodies, donor institutions, membership associations, and banks worked together to assemble a private sector model to supply credit reporting data. The establishment and growth of the Biroul de Credit in Romania is a prime example of how apparent market need plus stakeholder recognition of that need can result in effective action.

Introduction

The increase in the availability of retail credit that occurred in Romania during the period from 2000–2004 caused an urgent need to establish greater capacity and specificity in credit reporting through the establishment of a credit bureau. A credit bureau serves to mitigate the risk of lending by providing lenders with credit histories of loan applicants.

In Romania, the development of a private credit bureau, known as the Biroul de Credit, was a joint venture of market participants, the relevant government regulatory body, and donors with vested interests.

The Biroul's creation demonstrates that emerging economies such as Romania, with some degree of assistance from international donor organizations, are now developing entities of public interest through what is primarily a private sector response to market needs.

Context

In the period from 2000 to 2004, Romania experienced explosive growth in the retail credit industry. Progress towards European (EU) accession, the continued expansion of foreign banks in the Romanian market, rising

purchasing power among individuals in urban areas, and strong consumer demand—particularly in the area of white goods—caused an explosion in the availability of retail consumer credit. The increased access to credit caused an urgent need to establish greater capacity and specificity in credit reporting.

Further, the International Financial Corporation (IFC) held major positions in several Romanian banks, including the Banca Comerciala Romana (BCR). BCR is Romania's largest bank in terms of market share and was state owned at the time. Lending growth without appropriate risk management in the area of credit reporting increased the IFC's financial exposure in Romania. The IFC urged the Romanian banking sector and the National Bank of Romania (BNR), Romania's central bank and chief regulator of the banking industry, to establish a credit bureau.

As a separate but related matter, the BNR, as the chief economic regulatory body in Romania, had concerns about inflation due to the overheated domestic demand resulting from increased consumer debt. Establishing a credit bureau provided an additional constraint on consumer debt.



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By late 2003, there was a convergence of precipitating factors: the commercial banking industry recognized the need for improved credit reporting, a donor with a stake in the success of Romania's banking industry, and a willing government regulator. At the time the need for better credit reporting facilities became an issue, only two credit bureaus were operating, with limited effect.

The BNR maintained credit information and payment-incident databases that provided baseline credit reporting. All banks in Romania are required to submit the relevant data to the BNR's databases. These databases provide only negative data, only on loans exceeding 20,000 RON (about 5,600 Euros) that were made before 2004. (In 2004, before the Biroul was operational, the BNR began collecting credit information on all loans.) Thus, while the credit-reporting data in the BNR databases represented the majority of the financial value of credit supplied, the majority of transactions were not monitored. Romania's major commercial banks realized that the rapid growth in lending required more detailed credit reporting and greater coverage of transactions.

A private credit bureau also operated in Romania at this time, but focused mainly on reporting negative data from telecommunications companies – information that was insufficient for the risk management needs of banks.

Approach

Organization

The banks approached the Romanian Banking Association (ARB), and asked for assistance in developing a credit bureau model. The ARB developed the shareholder model, introduced the initiative to the BNR, and served as a liaison among the commercial banks, the Biroul and the BNR. The Biroul was registered as a Romanian company, Biroul de Credit SA, in February 2004. Once the company was established and the participants identified, specific steps were needed to develop the Biroul.

Corporate Governance and Ownership

To begin operations, the Biroul needed a budget and capital. A shareholder agreement was developed, and initial capital was provided by 24 participating banks. Under the terms of the agreement, only banks may own shares in the Biroul, and ownership is based on a bank's market share of retail lending in Romania. Thus, BCR is the larg-

est shareholder followed by Societe General's BRD. Nonbank institutions may report to the Biroul but may not own shares. While the share allocation obviously varies among banks, the technical and administrative obligations for reporting and participation are the same for all banks. Further, all shareholders pay the same fee per credit report.

The banks agreed to hire Serban Epure as the director of the Biroul in February 2004. As of May 2006, Mr. Epure continued to serve as the head of the Biroul.

Developing a Product Strategy

The banks realized that they wanted a sophisticated system that met international standards, but they needed credit reporting implemented quickly. They developed a product strategy based on adding functionality in the following three phases: Phase I—reporting of negative credit; Phase II—reporting of positive credit; and Phase III—credit scoring.

Results

Phase I was commenced in August 2004, only six months after the company was registered. Originally scheduled to be completed in May 2005, Phase II is still incomplete. Only five banks and one leasing company are currently reporting positive data. There is no official implementation timeline for Phase III. Several credit-scoring vendors are operating in the Romanian market, and a number of banks use the services of those entities in their lending programs.

One of the critical requirements for the Biroul to begin reporting was the development of a suitable information technology (IT) solution. An international tender was issued, and a local Romanian firm, SIVECO, was selected rather than one of the larger international IT companies. SIVECO had prior experience with PREVENTEL, a negative credit database used by Romanian mobile telephone companies. Accordingly, SIVECO offered both local and functional expertise. The tender was awarded in April 2004 and the system became operational in August 2004. The system's data standards are in compliance with European and American credit industry standards.

Public Information

There was no formal public information campaign, but the debut of the Biroul engendered greater than expected media coverage, mostly positive. An initial press conference was held at the launch of the Biroul's operations, followed by a second con-

ference on the one-year anniversary. The media's depiction of the Biroul's operation and the ability to request one's credit report were perceived as contributing to transparency. Until the media focus on the Biroul, many borrowers were unaware their credit histories were being recorded.

Overcoming Legal Obstacles

While a major reform effort was not necessary, development of the Biroul's credit-reporting database required ensuring that data privacy and protection laws were not violated. The Law on Protection of Persons Concerning the Processing of Personal Data and Free Circulation of Such Data [Romanian Law 677/2001] stipulated that the express or unequivocal consent of the borrower is needed before processing his or her data. This provision was seen as a major hurdle in obtaining historical data on borrowers who had not previously signed consent forms. With help from the ARB, the Biroul turned to the office of the Avocatul Poporului (People's Attorney), which assesses if there has been or could be an infringement of the people's rights. This office recognized that the Biroul maintained a legitimate interest in collecting both negative and positive credit data, and based on other provisions of the law, the Biroul was allowed to collect historical data without obtaining customer consent.

Borrowers are entitled by law to see their credit reports. The report indicated which financial institution entered the borrower in the credit registry. An individual can request to see his or her credit report in person, online, or by telephone, fax, or e-mail. The Biroul reports that it receives approximately 30 to 40 such requests per day. Borrowers can also ask to be entered into the database.

Coordinating with the BNR

A current effort is under way to improve coordination with the BNR. Currently, financial institutions are "double reporting" certain negative credit information to both the Biroul and the BNR. Norms were passed in May 2006 to address this situation. Now, banks report credit data regarding individuals with loans less than 20,000 RON (5,600 Euros) to the Biroul.

IFC role in Developing the Biroul

In December 2003, the IFC launched its assistance to Romania. The IFC focuses on assessing the regulatory framework to ensure establishment of a credit bureau that would be both legal and appro-

priately supervised by the BNR. The IFC also provided feasibility studies and database structures for the credit databases. Representatives of the banks and the Biroul mentioned that the IFC representative was instrumental in the early stages.

While the Biroul has grown rapidly and provides a valuable service, as set forth below, there are still a number of challenges remaining. Some smaller banks and non-banking financial institutions have expressed their concerns about the access to, quality of, and price of the credit reports.

Conditions of Participation

Participation is based on the reciprocity principle. All banks are entitled to receive credit bureau data, but they must contribute as well. Microfinance institutions have claimed difficulty gaining access to the Biroul, as there is no fee-for-service arrangement that would enable an interested party to purchase credit reports without participating in data reporting. The Biroul has stated that its future objectives include enrolling more nonbank financial institutions to make the credit information more useful. Outreach to these institutions is necessary.

The shareholder structure is based on market share and gives the largest banks the largest portion of shares. Because shareholders approve participants in the Biroul, they have a relatively powerful voice in deciding who will participate.

Collection of Positive Data

To facilitate credit scoring and give a more complete credit report, positive data must be captured in the credit database. There is a problem with compatibility between the bank software system and the Biroul system. With the acquisition of the previously state-owned BCR by Erste Bank, 90 percent of the Romanian banking sector is foreign owned and reflects different countries' systems and rules of disclosure. The Biroul system is compatible with specific international standards in the credit industry.

More complete borrower information and exposures were expected in 2006–2007. Many more Romanians pay mobile phone or utility bills than repay bank loans. As a result, many in the industry would like to see additional data reported from organizations such as leasing, utility, and telecom companies. The Biroul and the ARB indicate that they have sought to include these institutions in the future.

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About BizCLIR:

BizCLIR, or the Business Climate Legal & Institutional Reform Project, is a multi-year initiative of the United States Agency for International Development with the goal of improving the efficiency and impact of assistance programs intended to help developing countries improve their business enabling environments. This series, Best Practices for the Business Environment, represents one of many knowledge management components of the BizCLIR project. The goal of the series is to highlight the known best practices, case studies, lessons learned, and in some cases worst practices, so that the lessons can benefit other practitioners in the field. All issues are available at www.bizclir.com.

Development of the Credit Bureau Sector

While the subject of this document is the Biroul, it is not the only credit bureau in Romania. Currently, in addition to the Biroul and the BNR, credit bureaus include Alfa Credit, Delos, Intercredit Bucuresti, and Experian, one of the largest credit bureau companies in the world. As a result, the credit bureau market in Romania is competitive.

In September 2005, Experian acquired Expert Credit Bureau, which had been started to provide credit-reporting data from telecommunications companies. Experian plans to expand its credit data offerings in Romania. Experian currently provides credit scoring.

Delos Credit Inform began collecting information related to shareholders of public companies traded on the Bucharest Stock Exchange in 1993. Delos currently gathers data from consumer credit companies, telecom companies, and other sources including three banks.

In order to adapt to the rapidly changing Romanian market, the following developments will be necessary:

1. *Credit scoring.* As soon as the positive credit data is in place, the Biroul believes that plans can be made to implement credit scoring at the Biroul. Until then no, specific plans for credit scoring exist.
2. *Inclusion of legal entities.* The scope of the data is limited to individuals. If there is market demand, the Biroul would consider including companies and other legal entities in the databases, most likely starting with small and medium-sized enterprises. Several banks mentioned that they would be interested in this type of data.
3. *Adherence to Basel II requirements.* As of January 1, 2007, all banking systems must be in line with Basel II requirements.

Despite the challenges and shortcomings, the Biroul did begin operations within six months of inception and does provide a valuable service to the commercial banking sector and a growing number of financial institutions. In fact, the price per report has fallen as technical improvements have been made. Previously, at the price of 1 Euro per report, the Biroul was receiving 4,000 report requests per day. Now, at approximately half the price, the Biroul

is receiving 24,000 report requests per day. Countries seeking to establish a credit bureau may find the following recommendations valuable:

1. Maximize national and international pressure.
2. Emphasize cooperation of banks and consider use of an intermediary.
3. Devote the resources to prepare a high-quality tender document.
4. Use available government resources.
5. Exploit IFC technical assistance.

Conclusions

The development of the Biroul and the credit bureau industry in Romania is not a study of government reform in the financial sector. In this regard, there was no significant regulatory reform or donor project funding. Rather, it is a prime example of how apparent market need plus stakeholder recognition of that need can result in effective action. Government bodies, donor institutions, membership associations, and banks worked together to assemble a private sector model to supply credit-reporting data in less than six months. The Biroul's creation demonstrates that emerging economies such as Romania, with some degree of assistance from international donor organizations, are now developing entities of public interest through what is primarily a private sector response to market needs.

The challenge ahead for the Biroul is to ensure that its founders and shareholder are pleased with its performance and receive a satisfactory financial return but also to provide a public service to those with credit-reporting need in a rapidly changing market.