Principles and Practices of Microfinance Governance

by

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Any errors or omissions are solely the responsibility of the authors.
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EXECUTIVE SUMMARY

As microfinance institutions (MFIs) expand their outreach and increase their assets, and as more MFIs become regulated entities that can capture savings deposits, clear articulation of the functions of their boards of directors is essential for effective governance.

Governance is a process by which a board of directors, through management, guides an institution in fulfilling its corporate mission and protects the institution’s assets. Fundamental to good governance is the ability of individual directors to work in partnership to balance strategic and operational responsibilities. Effective governance occurs when a board provides proper guidance to management regarding the strategic direction for the institution, and oversees management’s efforts to move in this direction. The interplay between board and management centers on this relationship between strategy and operation, both of which are essential for the successful evolution of the institution.

In exercising their governance responsibilities, board members must consider the perspectives of numerous external actors. Depending on the legal status of the MFI, these actors can include providers of capital such as donors, governments, depositors or other financial institutions; regulatory bodies such as the superintendency of banks; and other stakeholders, including clients, employees, and shareholders. In its governance role, the board also is accountable to all these stakeholders and must assess continually which of these are the most important for the institution.

All board members must follow basic codes of conduct in carrying out their governance roles and responsibilities in good faith. “Duty of loyalty” requires board members place the interest of the institution above all others. “Duty of care” calls for board members to be informed and to participate in decisions prudently. Finally, “duty of obedience” requires that board members be faithful to the institution’s mission.

Not all boards maintain the same level of involvement in the institution. At one end of the continuum of board involvement is a rubber-stamp board, which is generally reactive to management. At the other end is a hands-on board, which provides excessive oversight and engages directly in operations. In the middle are representational boards, made up of highly influential individuals who are not necessarily experts in microfinance. These boards resemble rubber-stamp boards except that board members’ access to sources of power and funds is exercised to the benefit of the institution. Multi-type boards balance representational members with those that have microfinance expertise, and generally are better equipped to make informed decisions on a timely and efficient basis.

The relationship between the board and the executive requires clarity about the roles and responsibilities of each, and about the complementarity of these roles. The board should exercise this responsibility by (1) maintaining distance from daily operations; (2) drawing on the institutional memory of the directors; and (3) making binding decisions as a group. Application of these factors results in a process of decisionmaking that empowers the board.
and adds significant value to the management of the institution. Major board responsibilities can be grouped into the following four categories:

- The board has legal obligations that revolve around ensuring compliance with the institution’s bylaws, procedures, and other legal requirements. The board may be held liable for the institution’s activities.

- The board must ensure management accountability by hiring competent professionals, establishing clear goals for these executives and closely monitoring their performance, and confronting weaknesses when they surface.

- The board is responsible for setting policy and providing strategic direction to the MFI. The board must work closely with management in carrying out this role to ensure congruence between the institution’s strategic thinking and its operations.

- The board must assess its own performance on a regular basis. It is the board’s responsibility to maintain continuity or “institutional memory” in its ranks, to renew its membership with new directors, and to evaluate its own processes for decisionmaking.

Diligence in fulfilling these roles and responsibilities does not in itself ensure effective governance. Other essential factors are the commitment of the directors to the institutional mission; directors’ skills and expertise; attributes of the chairperson; the presence, structure, and function of committees; clearly defined board policies and procedures; and a climate that allows for critical self-evaluation.

Governance Issues in Microfinance

The Dual Mission: Balancing Social Impact with Financial Objectives. In this paper, MFIs are defined as institutions that combine a social mission—provision of financial services to the lowest-income population possible—with a financial objective that drives the institution to achieve self-sufficiency. Some sophisticated MFIs have attracted private sources of capital, including deposits, and have become regulated institutions. The extent to which microfinance institutions seek to maintain the dual focus of profitability and outreach to poor clients is directly shaped by the composition of the boards of directors and by the priorities established by the board. This paper argues that these two objectives are not mutually exclusive, and that boards, through their strategic decisions and policies, can move institutions in the direction of achieving superior profitability and reaching an expanding clientele of low-income entrepreneurs.

Ownership of Microfinance Institutions. Traditionally, the board of directors either consists of owners or represents the interest of owners. Aligning the interests of individual directors with the interests of the institution is key to realizing effective governance. Creating this alignment within the microfinance industry depends on understanding the issues associated with each of the four corporate structures of MFIs: public (government), nonprofit (NGO), for-profit, and cooperative (credit unions). The specific corporate structure does not
in itself define effective governance. For each, however, factors exist that may strengthen or undermine a board’s ability to fulfill its roles and responsibilities:

- **Public ownership/government corporate structure.** With the exception of Bank Rakyat Indonesia, public ownership models for microfinance from the past three decades have failed because of misguided policies that distorted markets through targeted subsidized credits, political interference, and corruption. In the past three years, however, some governments have taken new approaches to public ownership of MFIs. These approaches range from various mixes of public and private ownership, mechanisms to depoliticize the institutions, and an increased adherence to market principles. Because these efforts are still nascent, it is not possible to draw conclusions about their success.

- **Nonprofit NGO corporate structure.** Because nonprofits have no owners, commitment to the institutional mission is what drives NGO board members to fulfill their duties responsibly. Failed governance in NGOs has occurred where power has been concentrated in the hands of an executive who does not receive proper oversight from the board, as evidenced by the collapse of Corposol in Colombia. The NGO model has yielded important successes when individual board members have strongly identified with the institutional mission and possessed the ability to guide the MFI strategically and hold management accountable to performance objectives.

- **For-profit corporate structure.** There are two types of for-profit MFIs. The first includes commercial banks and finance companies that moved down market to serve the microenterprise sector; the second type includes NGO-established regulated financial institutions. While profitability primarily motivates the owners of the former, the motivation of owners in transformed NGO-MFIs varies with the mix of capital. Rather than pure, private capital, four principal sources of social capital typically are provided: NGOs, public entities, specialized equity funds, and limited private investors. Each of these potential investors has its own set of concerns and brings different experiences to the institution. In planning for the participation of various parties on an institution’s board, balance should not be put ahead of individual ability and commitment. The key is to have clarity in the requirements for effective governance, and to determine the willingness and capability of potential investors to perform the duties required.

- **Credit union corporate structure.** In credit unions, where owners are also the institution’s clients, three critical lapses in governance arise: (1) a misalignment of priorities among elected directors, contracted management, and member-owners; (2) unequal representation of the interests of the two categories of clients—net savers and net borrowers—generally in favor of borrowers; and (3) a lack of regulation and supervision of credit unions. Successful governance of the credit union corporate structure requires a balance between savers and borrowers; this balance can be achieved by reorienting the services of the institution to attract more savers. In addition, specific rules should be in place to guard against excessive risk-taking by the board. These include rules to enforce the fulfillment of board roles and responsibilities, compliance with external auditor requirements, controls on insider operations and loan risk, and the exercise of prudent discipline.
Fiduciary Responsibility of Microfinance Institutions. In general, the fiduciary responsibility of the board of any financial intermediary is considered greater than that of other corporate entities. Besides maintaining the solvency of a financial institution, boards of MFIs have three additional issues to consider. Low-income microentrepreneurs, as borrowers and savers, lack multiple sources of financing and are at greater risk than middle-income savers if their savings are lost. An insolvent microfinance institution, in most countries, means the end of a client’s access to capital at commercial rates. Additionally, microfinance boards incur a responsibility with donors, in the case of NGOs, but this fiduciary responsibility increases when the MFI intermediates funds by borrowing from a bank, mobilizing deposits, or floating an instrument in the local securities exchange. Finally, the insolvency of any large-scale microfinance institution that is considered a “success” around the world would have an effect on the domestic and international microfinance sector. It is likely that lenders and other investors would become concerned about the viability of this field and withdraw or curtail the financial resources to microfinance. Hence, boards of advanced MFIs must understand that their fiduciary responsibilities extend beyond their governed institution and can affect the wider microfinance industry.

Risk Assessment Capacity in Microfinance Institutions. In its role as corporate fiduciary, the board must be able to assess risks associated with the provision of financial services. The growth of microfinance institutions, combined with significant increases in competition, and the creation of regulated microfinance institutions require greater ability on the part of boards to assess risk. The paper covers these factors that make risk assessment an essential board responsibility and discusses effective integration of personnel in NGOs that hire private sector (usually banking) staff to strengthen their financial and banking expertise.

Achieving Best Practices in Microfinance Governance

Board Membership. The composition of the board has to be considered from several perspectives: skills and characteristics of microfinance board members; directors’ commitment to the dual mission of microfinance; directors’ ability and willingness to fulfill the duties of care, loyalty, and obedience; the board’s commitment to develop the knowledge and skills of new and existing members; the size of the board; and finally, board member terms, removal of inactive members, and board performance evaluations.

Government Structure. There are three mechanisms a board establishes to operate effectively: (1) the separation of the role of the board chair and that of the managing director or chief executive officer (CEO); (2) the role of the board chair in relation to other board members; and (3) the use of board committees. The paper calls for the splitting of responsibilities between the CEO and the chair and discusses the important role a chair plays in ensuring ample discussion, debate, and the achievement of consensus among board members. Creating and utilizing board committees to address key issues in preparation for consideration by the full board can be useful. The effectiveness of the committee structure, like that of the full board, depends on the clarity of the committees’ responsibilities.
Procedures. Well-defined and clear procedures are essential for effective governance. Even the most committed and highly qualified individuals cannot discharge their roles effectively without following well-documented procedures. Proper documentation—in accurate board minutes, up-to-date articles of incorporation or by-laws, and a board policy manual—is essential.

Issues for Future Research

The paper concludes by identifying three areas related to effective governance that require further analysis:

1. Conflicts of interest, such as the ability to fulfill the duty of loyalty and the practice of reciprocal board service;

2. Ownership considerations on microfinance boards, which comprise diverse types of people and are becoming ever more diverse; and

3. The effect of rapid change in the microfinance field—caused by competition, a movement toward the commercial model of microfinance, and increased participation by governments—on MFIs’ board composition, incentives, function, and leadership.
Governance is the process by which a board of directors, through management, guides an institution in fulfilling its corporate mission and protects the institution’s assets over time. A board of directors is established to provide oversight and give direction to the managers of an institution. The board carries out this function on behalf of a third party, referred to as shareholders in the case of for-profit corporations. Because there are no owners in nonprofit corporations, that third party is not as easily identified and has been defined to include the corporation’s clients, staff, board, and donors.

Fundamental to good governance is the ability of individual directors to work in partnership to accomplish an effective balance between strategic and operational responsibilities. Effective governance occurs when a board is able to provide guidance to management in strategic issues and is effective in overseeing management carry out the agreed upon strategic plan. Management, in turn, assumes operational authority and ensures that the institution’s program of activities responds to the direction jointly agreed upon with the board. The interplay between board and management centers on this relationship between strategy and operation, with the board basing its discourse on the strategy it has jointly defined with management and with management ensuring that operations are deployed effectively. Both sets of priorities are required to successfully navigate an institution through its short- and long-term evolution. The challenge of governance, therefore, is to employ the perspectives and experiences of the board and management to maximize their overall contribution to the institution’s performance.

In the microfinance field, governance has assumed increasing importance for several reasons. First, as microfinance institutions (MFIs) grow in their outreach, the size of their assets, as reflected in their portfolio, also grows to considerable size. Ensuring effective management of this growth requires added input and involvement by a board. Additionally, increasing numbers of MFIs are becoming regulated and assuming the responsibilities and challenges of a regulated entity. Capturing deposits from savers and investors is perhaps their most important challenge and requires the greatest oversight. Finally, MFIs are operating in increasingly competitive markets, and maintaining or increasing market share has become an important component of their strategic objective.

Therefore, a clear articulation of the function of microfinance boards is essential for their effective governance. After briefly discussing the basic standards of board conduct and types of boards, this chapter details the specific role and responsibilities of microfinance boards and the conditions that must exist to achieve effective governance.
DUTIES OF A BOARD DIRECTOR

The standards of conduct applicable to individual board directors fall into three categories: Duty of Care, Duty of Loyalty, and Duty of Obedience. These concepts provide a “code of behavior” that serves to frame the way board members carry out their respective roles and responsibilities.

Duty of Care. The Duty of Care calls on a director to participate in the decisions of the board and to be informed on the data relevant to such decisions. A common statement of the Duty of Care asks a director (1) to be reasonably informed, (2) to participate in decisions, and (3) to do so in good faith and with the care of an ordinarily prudent person in similar circumstances. To discharge the Duty of Care efficiently and effectively, directors must attend meetings, exercise independent judgment, and ensure that they have an appropriate level of understanding of the issues critical to the institution.

Duty of Loyalty. The Duty of Loyalty requires directors to exercise their powers in the interest of the corporation and not in their own interest or in the interest of another entity or person. By assuming a board position, directors acknowledge that for any corporate activity, the best interests of the corporation must prevail over their individual interests or the particular interests of the constituency that selected them. The Duty of Loyalty primarily relates to conflicts of interest, corporate opportunity, and confidentiality.

Directors may have interests in conflict with those of the corporation. The Duty of Loyalty requires that a director be conscious of the potential for such conflicts and act with candor and care in dealing with such situations. Conflicts of interest are neither inherently illegal nor are they to be regarded as a reflection on the integrity of the board or of the director. Once a director discloses a potential conflict of interest issue, it is the board’s interpretation of the issue that will determine if it is a proper or improper transaction.

Corporate opportunity is another area related to Duty of Loyalty. It requires that a director, before engaging in a transaction that he or she knows may be of interest to the corporation, inform the board of directors in sufficient detail and adequate time to allow it to act or decline to act to a director’s possible involvement in that transaction.

Duty of Obedience. The Duty of Obedience requires board members to be faithful to the institution’s mission. Although board members have the authority to determine how the institution is to best meet its mission, they are prohibited from behaving in a manner inconsistent with the basic institutional objectives. The Duty of Obedience grows, in part, out of nonprofit organizations’ heavy reliance on the public’s trust when soliciting donations and grants. In turn, the public has the right to be assured that such funds will be used for the purpose for which they are given. In for-profit organizations, the responsibility is toward the investors (both equity and debt), especially if the funds are from public sources. In this

1 This section is drawn from “Guidebook for Directors of Nonprofit Corporations,” edited by Overton, 1993.
2 Leifer and Glom, 1992, p. 33.
context, being faithful to the institutional mission translates into maximizing returns to investors (and in some cases, like microfinance, balancing profitability with social impact), in a manner consistent with ethical practices.

CONTINUUM OF BOARD INVOLVEMENT

Before discussing the roles or responsibilities of a board, it is instructive to discuss the continuum of a board’s involvement in the governance of the institution. At one end is the rubber stamp board, which exercises too little oversight of management. At the other end is the hands-on board, which can play an effective governance function, yet, in the extreme, may exercise too much oversight of management. In the middle of this continuum falls the representational board, which, although less involved than the hands-on board, contributes to the institution in establishing key linkages with the business, banking, and government sectors. The challenge facing a microfinance institution is to achieve the type of board, which here is termed multi-type, in which members actively provide guidance in strategic issues and assist the institution in establishing the key linkages outlined above.

Rubber Stamp Board

A board of directors that is generally reactive in its relationship with management is called a rubber stamp board. Management tends to present strategic thinking as well as plans and decisions to the board merely for its official approval. Directors may be poorly prepared for meetings and may know very little about the MFI’s operations and activities. Although such an arrangement may expedite the decision-making process for management, it negates the fundamental reason for a board’s existence and in the long term severely diminishes the institution’s overall effectiveness. This board type also may have one member—often the founder—who works closely with the executive director, makes most of the decisions, and assumes acquiescence from other board members. A rubber stamp board is likely to create one or more of the following situations:

- The board brings no additionality to the institution and is thus amenable to whatever strategy or program is submitted for its approval.
- The institution is denied the benefit of varied thoughtful voices and experiences that are essential for its proper functioning and growth.
- Enormous responsibility and power are placed in the hands of the top executive or on one board member. Such a situation is likely either to drive away a good executive who demands effective governance or to concentrate authority unduly in one person.
- In the worst case, rubber stamp boards, which do not act as a check and balance, leave the institution vulnerable to mismanagement and fraud.
Representational Board

A representational board includes influential and well-respected persons who provide important visibility for the institution and give it a level of credibility it would not otherwise have. This board type depends heavily on management to play a key role in strategic and operational decisions, but board members remain informed of the institution’s operations. Members of such a board are often short of time and are more likely to provide a more distant level of oversight. When deploying their responsibilities effectively, members of this board type are likely to accomplish the following:

- Open doors for the institution that would otherwise remain closed or hard to open. A representational board member might improve the institution’s ability to establish key linkages with the government, business, or banking sectors, allowing it to more effectively achieve its institutional mission;
- Increase the institution’s access to information outside its direct area of operations and enhance its national and international exposure; and
- Maintain necessary oversight in part to ensure that their names and reputations are not damaged by their association with a poorly performing institution.

Hands-on Board

A hands-on board of directors consists of members who offer strong expertise and are actively involved in defining and monitoring the activities of the institution. Directors are kept informed of the ongoing operations and issues of the institution, are well prepared for meetings, and play a proactive role in overseeing the management of the institution. An effective board of directors that is well versed in the needs of the institution and able to utilize its collective experiences, skills, and contacts will consistently exhibit the following characteristics:

- Will raise issues that are at the core of the proper functioning of the institution and will not be distracted by peripheral or semi-peripheral concerns;
- Will engage in more constructive and challenging discourse with management and provide the type of useful analysis that enables management to pursue increasingly higher levels of performance;
- Accompanies good management and, if necessary, takes the lead in defining the overall strategy of the institution and works closely with management in overseeing its implementation;
- Understands the difference between its strategic-based role and the operational responsibilities of management; and
- Is more likely to identify quickly and effectively shortcomings in the board’s functioning and seek to address them.

Clearly, the above characteristics apply to an effectively functioning hands-on board. Ironically, a hands-on board that loses sight of its primary strategic function is likely to cross
the line into micromanaging the operation and thereby may become more harmful to the institution than the other board types.

Multi-Type Board

A multi-type board includes members who play a representational role and those who are well informed about the operations of the institution and have solid expertise, here termed hands-on. The former provides the role of visibility and stature, whereas the latter provides useful input to strategic decisions facing the institution and, to some extent, specific operational issues. The multi-type board combines the representational and hands-on boards described above and extracts from each its comparative advantage on behalf of the institution. This board would be able to make well-informed, timely, and efficient decisions because it has the elements at hand to do so. Moreover, this board type can evolve, balancing the types of members it incorporates into the board based on changing institutional needs and priorities.

Clearly, a board that fits into the rubber stamp category is not executing its role effectively. Similarly, boards in which all directors fit into one of the other two types—hands-on or representational—will also demonstrate limitations in their capacity to govern effectively. A mix of directors who together can effectively address the governing needs of the institution is the preferred option for quality governance.

The above description serves only as a continuum to guide boards in their own formation. A board needs to understand the advantages that arise from each of the board types and to tap these advantages as appropriate. However, regardless of the board that emerges in an institution, its functions as a governing body do not vary. The next section defines this function in terms of the specific role and responsibilities of a board.

Role and Responsibilities of Boards of Directors

Most of the literature on governance focuses its analysis within the framework of a given corporate structure: a for-profit corporation, a nonprofit entity, or a public agency. Such approaches implicitly assume that the board of directors’ behavior is defined by the corporate structure it governs. While acknowledging that corporate structure affects the achievement of effective governance, it does not define it. The following is a broad definition of effective governance that can be applied regardless of the corporate structure of a microfinance institution.

A board of directors is entrusted with the fiduciary affairs of the corporation. The term “fiduciary” refers to a person or persons to whom property or power is entrusted for the benefit of another. Treating directors and managers as fiduciaries provides a mechanism for imposing sanctions if they fail to exercise their responsibilities to the corporation, without necessarily requiring that all of those responsibilities be detailed in advance. As explained by legal scholars Frank H. Esterbrook and Daniel R. Fischel, “the fiduciary principle is an
alternative to elaborate promises and extra monitoring. It replaces prior supervision with
deterrence, much as criminal law uses penalties for bank robbery rather than pat-down
searches of everyone entering banks.”

Legal Obligations of the Board

As a fiduciary, the board of directors has several legal obligations. First, the board must
ensure that the institution complies with its articles of incorporation, bylaws, and internal
policies and procedures. Further, the board must ensure that the institution maintains its legal
status. The board must also ensure that the institution complies with government rules and
regulations, which will vary with the institution’s corporate structure. For example, as a
microfinance institution becomes regulated, it will be subject to a new set of regulatory
requirements that the board must understand. A final element of the board’s legal obligations
is the level of personal liability of individual directors for the institution’s activities. Such
liability varies by country, yet board members must be keenly aware of the degree of
responsibility and immunity provided for them by local law.

In representing the interests of a third party and fulfilling their legal obligations, boards
delegate responsibility to management and hold management internally accountable to a set
of objectives and performance standards that the board has defined. However, achieving
these standards and objectives can be impaired and effective governance diminished when
board members are unclear about their role. For example, a director may assume that
activities related to operations are part of his or her responsibilities and may hinder
management’s ability to perform effectively or management’s accountability. Similarly, a
CEO may depend too much on a board and request its input on decisions outside of the
board’s domain.

Relationship Between Board and Executive

Although the relationship between a board and the executive director or CEO is dynamic, it
must be grounded in a clear understanding of the roles each serves. Effective governance
strikes the appropriate balance in the relationship between a board of directors and
management in their combined efforts to move the institution forward. Each brings unique
skills to this joint effort and views the institution from a different lens. Together they add
value precisely because they are complementary. Diane Duca suggests that this
complementary nature exists because board and executives use different frames of reference
to understand the institution and to deploy their responsibilities. Table 1 highlights some of

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3 Blair, 1995, p. 57.
4 If necessary and where possible, board directors may consider purchasing Directors & Officers (D&O)
   Insurance, which will protect them against personal liability and may cover legal costs that might arise from
   a legal action taken against the institution.
5 Though Duca’s (1996) presentation is in the nonprofit context, these frames of reference also apply to the
   corporate and public sectors.
these differences and contrasts the governing body of the board, not its individual members, with the executive position of the institution, which is only one person.

Table 1: Contrasting Frames of Reference

<table>
<thead>
<tr>
<th>Executive</th>
<th>Board of Directors</th>
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<tr>
<td>Executives are individuals</td>
<td>Boards are legal entities and a group</td>
</tr>
<tr>
<td>Executives deploy professional skills only one organization</td>
<td>Each board member has many additional commitments</td>
</tr>
<tr>
<td>Executives are compensated</td>
<td>Board members serve voluntarily or receive insubstantial compensation7</td>
</tr>
<tr>
<td>Executives can make decisions alone</td>
<td>A board makes binding decisions as a group</td>
</tr>
<tr>
<td>Executives rely on staff</td>
<td>Boards operate without staff</td>
</tr>
<tr>
<td>Executives serve at the pleasure of the board</td>
<td>Boards as entities are permanent, despite director rotation</td>
</tr>
<tr>
<td>Executives are professionals in the organization’s area of activity</td>
<td>Directors most likely are not experts in the institution’s area of activity</td>
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</table>

Effective boards carry out their responsibilities by (1) maintaining operational distance from the institution, (2) drawing on the institutional memory of the directors, and (3) making binding decisions as a group. Board decisions are based on the voice of the majority. Arriving at a consensus may be time-consuming and decrease the board’s operating expediency, but the process is essential to a well-functioning board. These three factors empower the board and add significant value to the management of the institution.

Management, in contrast, is intimately involved in daily operations, has an up-to-date and in-depth understanding of the immediate challenges and opportunities facing the institution, and the flexibility to react quickly. An institution’s executive will consult with senior management on key issues but is individually accountable. What then is the optimal balance between these two sets of circumstances and perspectives and how do they meld to create effective governance?

Effective governance requires boards to focus on three major areas of responsibility: (1) management accountability, (2) strategic planning and policy-making, and (3) self-regulation. These three areas allow the board to fulfill its fiduciary obligations, and each requires board members to perform specific tasks, as outlined in Table 2 and discussed below.

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6 Based on Duca, 1996.
7 Although board directors are often compensated in the corporate setting, microfinance board directors of for-profit MFIs currently are not compensated or are compensated minimally.
### Table 2: Functions of a Board

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<td>Set clear and measurable goals</td>
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<td>Self-regulation</td>
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#### Management Accountability

To ensure that management is held accountable for the activities of the organization, a board must first focus on the process and mechanisms it uses to identify a competent executive. Second, it must set clear and measurable goals. Third, a board must monitor the performance of the executive. Finally, it must be able to identify managerial weaknesses and confront them when these adversely affect the institution. If necessary, the board must be prepared to remove the CEO.

**Install Management Capacity.** Hiring a strong, competent CEO is one of the primary functions of a board of directors. This individual, as the operational leader for the institution and the representative of the entire staff to the board, plays a key role in the long-term success of the institution and in the realization of effective governance. A board can only be as effective as the CEO it appoints, and therefore it must consider this a core responsibility.

**Set Goals.** Once an executive is in place, the board’s role is to monitor the performance and progress of the institution through its oversight of the CEO. Well-functioning boards spend the required time working with management to define goals and set targets for the institution. They then monitor the institution’s attainment of these goals and targets by assessing the executive’s performance. Boards identify the key areas in which an executive should perform effectively, which often include the following:

- **Vision.** Vision refers to management’s capacity to define a long-term view of the institution’s future, which is critical for its sustainability over time. Management’s vision should be clearly defined and the steps to its achievement well conceived. The vision is articulated in a strategic plan, which also outlines the main program areas of the institution and the results that are expected. For example, key benchmarks for a nonprofit microfinance institution against which management performance is measured will likely include targets for scale of operation, market penetration, level of self-sufficiency of the institution, legal structure required to reach targets, level of efficiency of the operations, and quality of the assets.
Management. A board assesses a CEO’s ability to manage the institution’s human resources. This area addresses issues of productivity, performance, and development of staff. Additionally, a board reviews the organizational structure of the institution to ensure its adequacy for the effective deployment of its operations.

Financial performance. The CEO is responsible for maintaining an institution’s financial solvency. In the for-profit context, this includes generating a return to investors. In the nonprofit context, a balanced budget or surplus is expected. Although losses or deficits may be acceptable in the short term for well-defined circumstances, a board should not allow repeated poor financial performance. Asset quality and the ability to mobilize financial resources are also key in obtaining good financial results.

Relationship to the board. The CEO is responsible for ensuring an effective board-staff relationship. This relationship is a product of the official, formal board meetings and the numerous informal interchanges that occur between individual board directors, the CEO, and individual staff members. Among the factors that contribute to this relationship are the extent to which the board is well informed and prepared for meetings, the strength of the working relationships between board directors and staff, and the degree to which individual directors are knowledgeable of the institutional mission.

It is generally understood that board members have access to an institution’s staff but will use judgment in their interactions so as not to distract the business operation of the institution or undermine the CEO. Additionally, boards often invite senior staff members other than the CEO to attend board meetings. This provides the board with additional insight into areas under discussion and allows board members to have exposure to staff with future potential for senior management positions.

Monitor Performance. How can the board of a microfinance institution most effectively ensure that management attains the established goals and objectives? The effective monitoring of executive performance requires the following elements:

- **Availability of information.** The board must have timely access to the appropriate information.
- **Clarity of objectives.** Strategic goals and objectives against which the performance of a particular period is measured must be clearly articulated. This is a prerequisite to receiving the right information.
- **Candor.** The executive must report to the board with candor and the level of detail and analysis necessary for effective board deliberations. For example, an executive can not withhold information from the board about a situation or crisis that may seriously affect the institution, even if that member thinks it will be resolved soon.
- **Analytical rigor.** Board members must have the analytical skills to pose the right questions and to be incisive in their discussion of institutional performance.

One approach to motivate management’s performance in attaining the mutually agreed upon goals is to create incentive mechanisms. The latter should align the well-being and interest of the individual manager with what is good for the institution and by extension, in the case of
for-profit corporations, the shareholders. The need for such incentive plans arises because in most organizational structures in the private sector, ultimate ownership of the assets may reside in the shareholders but day-to-day control of those assets rests in the hands of management. In the nonprofit setting, the tension could also exist between individual and institutional priorities. Examples include individual job security and comfortable stability versus rapid institutional change, and personal friendships versus job performance.

In designing an incentive scheme for the executive of a microfinance institution, it is important to consider the following principles and measures of operational performance:

- **Focus.** Key indicators in the incentive scheme must be limited to those few factors that truly matter. In microfinance, although portfolio size and quality are obvious indicators related to effective management, financial performance and the number and characteristics of clients are examples of additional indicators that could be utilized.

- **Control.** Incentives should reward people for issues that are within their control and for a behavior that they can directly affect.

- **Simplicity.** Incentive schemes should be simple. No more than five, and preferably fewer, variables should be selected. Staff should readily understand the mechanics of the plan.

- **Logic.** The rationale for the selected indicators should be clear for them to have legitimacy.

- **Targets.** The targets set must be measurable and achievable. It is no use to select a variable that everyone agrees is very important, like customer service, but no one knows how to measure reliably, or to set targets that are unattainable.

**Confront Weaknesses.** In assessing the performance of the executive, the board must also be willing to confront institutional and management weaknesses and act to address them. Countless examples have shown that effective management competency and conduct can not be taken for granted. It is incumbent upon the board to identify those areas in which the institution displays poor performance because of weak management practices. Examples might include poor financial controls, low staff morale, or weak information systems. A board’s responsibility is to demand and support management in strengthening these areas and to monitor the process of improvement. The strength of trust between the board and management and the level of the board’s exposure to other members of senior management facilitates this process.

Institutional and management weaknesses fall on a spectrum of severity. On one end are procedural matters that may result from management inexperience and require a practical solution. On the other end are actions that may include fraud. In either case—inept performance or fraudulent actions—boards must be willing to confront and, in the worst case, fire the CEO.

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8 This discussion on incentive schemes is drawn from Chu, 1998.
9 This concept is referred to in the literature on corporate governance as the principal-agent theory and was developed by Michael Jensen.
Confronting management, however, can be a difficult and uncomfortable task for a board. The pitfalls of “group think” often are played out, with no single individual willing to step out in front of the others and challenge a CEO. This may be due to a sense of personal loyalty to the CEO or to the chair of the board. Individual directors may also hesitate to act because they are unsure that they have seen the full picture; in so doing, they may give the benefit of doubt to an incompetent or ill-intentioned CEO. A board’s ability and willingness to make the hard decisions and confront weakness in the executive, and therefore the institution, is a function of the following:

- Degree of board member independence from management;
- Leadership skills of individual directors;
- Climate that allows for dissension;
- Mechanisms or opportunities for the board as a group or individually to voice their concerns; and
- Effective ownership stake in the institution or strong identification with the objectives of the organization.

Many times, with the best of intentions, boards are tempted to assist an under-performing CEO by assuming the management of certain tasks or projects. This approach is extremely damaging because it both obscures the accountability of the CEO and delays addressing that individual’s underlying incompetence. Additionally, it displaces decision making from those that are close to operations (management) to others who are remote (board). Accordingly, board assumption of management duties should be assumed only after the board has decided on a permanent solution to the deficiency and only as a temporary solution in the absence of any other alternative.

**Strategic Planning and Policy Setting**

The second major area of board responsibility is strategic planning and policy making. However, although effective governance assumes that the strategic planning process involves the board in a significant way, the board should include and expect strategic thinking to be part of the leadership qualities that the top executive brings to the institution. The distance and diversity of experiences of board directors enables them to bring a perspective to the institution unique from that of management. If the board does not add significant value to the institution’s strategic plan, it is not performing its duty. The board should provide guidance and input in three distinct areas: charting the institution’s strategic course, setting broad operational policies for the institution, and resolving strategic issues as they arise.

**Providing Direction.** It is not uncommon for daily operational priorities to overtake the more thoughtful process of strategic planning. Effective governance requires that the board raise strategic issues that may not otherwise be addressed and, thus, significantly contribute to identifying and setting long-terms goals for the institution.
Setting Institutional Policy. A central feature of board leadership is to define and clarify, with management, general institutional policies. On a practical level and with few exceptions, the board role in setting policy should differ from that of management not by topic but by levels within topics. For example, it is typical for management to bring to the board general policies on compensation. In this matter, the board might decide that the institution should compensate its staff with packages that are competitive with other institutions of the same size and scope. The actual wage and salary administration plan is then left up to management. Or a board might be involved in setting a policy on the characteristics of the neighborhoods in which it wants to establish additional branch offices, and management is left to determine the specific locations.

A policy-centered approach allows a board to effect the most change and to place all operational and administrative activities of the institution within the framework of defined policies. This approach also encourages the recruitment of individual directors with general strategic management skills who are more likely to keep the board focused on its governing mandate.

In actuality, everyone in the organization unknowingly sets policy or impacts strategic direction in their daily activities. A board can be most valuable in establishing a clear, accessible set of overarching policies that synchronizes these various levels.

Developing and Mobilizing Solutions. Boards that go beyond the above-mentioned elements—providing key input in charting a strategic direction and in defining general policies—assist the institution in identifying tactics and solutions for reaching its goals. In this sense, the board provides governance plus guidance. Additionally, a board that includes individuals with specific technical skills might assist the institution in addressing legal issues, public relations, and fundraising concerns or topics related to technology or pricing.

Board Self-Assessment

A final area of effective governance involves the board’s assessment of itself as a body of individuals and as a permanent entity. Three areas constitute the core of any assessment that the board conducts on itself: continuity, renewal, and evaluation.

Continuity. Of great value to management is that the board and its individual directors possess an institutional perspective. In cases of management turnover, this perspective of the board is unique. Even when there has been continuity at the executive level, the board perspective adds greatly given its collective experience. The board must therefore be responsible for maintaining this continuity by ensuring that even with natural attrition, the board’s “institutional memory” is preserved. The design of board terms and succession policies, as well as a corporate binder, are the mechanisms used to ensure continuity.

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11 Interview with Mary Houghton on October 30, 1997.
Renewal. Having stated the need for continuity, so too is there a need for an infusion of new directors who bring fresh perspectives, talents, and expertise. Working with management, board members can fundamentally shape effective governance by identifying new directors who could enhance the board operation. Ideally, board composition is a balance of the old and new.

Evaluation. As discussed earlier, given the contradictory frames of reference of boards and management, by definition board performance is vulnerable to being undermined by a set of complex dynamics. An effective board recognizes its own weaknesses and has in place mechanisms for self-evaluation. Board performance can be assessed under three categories: the role, the working style, and the directors themselves. Though still an infrequent part of board processes, self-evaluation is being embraced by increasing numbers of entities. (The subject of board performance evaluations is discussed further in Chapter Three.)

Having defined the fundamental role and responsibility of a board of directors, it is also necessary to understand the broader context in which a microfinance board conducts its work. Discussion now turns to that topic.

THE CONTEXT THAT FRAMES GOVERNANCE

actors who expect a certain level of performance from the institution and whose position the board must consider. External actors can be divided into three groups: (1) providers of types and degrees of accountability from the institution. Table 3 presents the characteristics of each based on MFI organizational structure.

donor agency might require that an institution’s customer base include a certain percentage of women. Regulators set legal limits on leverage for a microfinance institution or procedural requirements, depending on how important they are to ensuring the long-term survival of the institution, might become part of the regular reporting made to the board by management. In outsider with appropriate expertise, such as legal counsel when abiding by regulations, or by incorporating such expertise directly into the board through an individual director.

performance criteria, so too will these actors react by investing or withdrawing their funds. Regulatory authorities establish prescribed legal norms, which, if violated, will result in

Demb, Ada and F-Friedrich Neubauer. 1992. The Corporate Board
| Table 3: Actors in the Governance Environment by MFI Organizational Type |
|---|---|---|---|
| **Providers of capital** | **Public** | **Mutual** |
| Donor institutions and individuals, commercial banks (lines of credit), providers of guarantees, NGO itself through retained earnings | Government, second-tier financial institutions | Savings deposits of owners/ Members and external sources of funding, such as donors, liquidity funds organized by national and international federations | Profit-maximizing investors, socially responsible investors, NGO-retained earnings, Management, employees, Savings deposits, equity provided by multilateral public sector development banks (IIC, IFC) |
| **Regulatory Body** | No regulatory body for NGOs. Few regulations for NGOs in developing countries | Superintendency of Banks, Central Bank, Finance Ministry | Where it exists, specialized credit union regulatory agency | Superintendency of Banks |
| **Other Stakeholders** | Clients, employees, suppliers of expertise (e.g., legal counsel) | Government officials, clients, employees, suppliers | Members as clients, employees, suppliers | Shareholders, employees, clients, suppliers |

Customers sensitive to the quality of service, stakeholders will buy when the MFI meets their needs or leave when they are dissatisfied. And as employees who demand certain compensation and quality of work environment, stakeholders will choose to work in the institution or seek other employment.

Every microfinance board should assess its governance environment. To whom is the microfinance institution externally accountable and in what way? Does the institution’s governance adequately and appropriately respond to the expectations of relevant external actors? How does accountability differ among the four MFI corporate structures of nonprofit, public, mutual, and private/for-profit? For each structure, a set of external actors exists whose expectations will serve as a framework for the board’s work. External actors, and their demands on an institution, are continually changing and require the board’s close and frequent assessment.

The external actors, the board, and the internal operations as led by management share a dynamic relationship. The board demands internal accountability from management, yet is accountable to outside actors and must ensure that the institution’s strategy and operations respond to these actors. The board also must constantly assess which of the external actors are most important for the institution. Figure 1 illustrates the context within which a board operates and its relationship to outside forces of accountability. Effective governance

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13 Regulations governing nonprofit corporations in the United States are more extensive.
requires that board members understand the context in which they operate and respond to it appropriately.

![Figure 1: The Context that Frames Governance](image)

**SUMMARY: CONDITIONS FOR EFFECTIVE GOVERNANCE**

With board roles and responsibilities defined, the following are the necessary conditions to ensure effective governance within an institution.

1. Individual directors must have something at stake. Foremost is their commitment to the institutional mission. Board directors of nonprofits, and many board directors of public companies as well, do not have any monetary investment in the company on whose board they serve. What they do have at stake, however, is their personal investment of time and energy from having fully “bought into” the mission of the organization. A secondary motivation might be their personal reputations. If this were board directors’ principal motivation, however, one might doubt their staying power if the institution were to face difficult times. Directors who have invested a significant percentage of their own net worth in an institution will usually be very alert to the institution’s performance. This does not mean, though, that those who have not invested their own resources, but who are strongly committed to the institutional mission, will not be equally attentive to the institution’s health. The key point is that in the nonprofit setting (and, to a limited extent, with directors of public companies who do not have a significant financial investment in the institution), it is especially important to identify board directors who are genuinely committed to the institutional mission.

2. Individual directors should have the following characteristics:

   - Skills as leaders, visionary thinkers, and managers;
   - Technical expertise and experience relevant to the organization (i.e., financial, legal, and marketing);
Independent minds that are not beholden to the chairperson or CEO;
Basic genuine commitment to the activities of the organization; and,
Willingness to set time apart to participate actively.

3. Responsibility between the board and management should be clearly defined. This translates into the fundamental understanding by both board and management that the role of the board is at the strategic rather than the operating level.

4. Well-defined and regularly implemented measures of management (and board) performance are needed and should be based on merit and hence shielded from personal or political influence.

5. Strong information systems and communication channels must be in place within the institution to provide relevant and timely information to measure the performance of the institution in areas such as portfolio quality, profitability, human resource management, and programmatic goals. In too many cases, information provided to boards is biased toward accounting data, which alone is insufficient.

6. A skillful chairperson is needed to run effective meetings by focusing the agenda on big picture issues and policies. The chair also must be able to direct actions and build a consensus by bridging the gap in opinions, which often arises among independent-minded directors.

7. Mechanisms should be established to allow for individual director participation, such as committees. This approach seeks to overcome the individual director’s tendency toward passive involvement and to discourage the tendency of “group think” mentality.

8. A climate and structure is needed that allows for critical evaluation. This should include a trusting relationship between the CEO and individual directors. An executive session (without the CEO) should be held periodically, with a summary performance evaluation to give directors the opportunity to raise concerns before crises arise. The chair should also periodically seek input on the board’s effectiveness from fellow board members and senior staff.

9. Board policies and procedures should be in place to ensure continuity of board leadership and individual director participation. Significant institutional memory should be maintained for the entity within the board of directors.

With the presentation of the roles and responsibilities of the board and the conditions for success delineated, the next chapter focuses on governance issues that pertain particularly to microfinance. Boards of MFI's must understand these issues to exercise their governance function more effectively.
Chapter One defined the major components of effective governance for any institution and made general observations of MFIs. There are, however, issues pertinent to microfinance operations that require a more detailed analysis and must be incorporated into a discussion about governance for the microfinance field. Critical issues are as follows:

- The dual mission of MFIs;
- Ownership of MFIs;
- The fiduciary responsibility of the board; and
- Risk assessment in MFIs.

A Dual Mission: Balancing Social Impact with Financial Objectives

MFIs originated, in most cases, with a dual mission that combines social and financial objectives. The social mission seeks to provide financial services to as many of the lowest income population as possible; the financial objective drives the organization to achieve financial self-sufficiency, which permits sustained service delivery without dependence on subsidies.

As MFIs have evolved, they have achieved increasing levels of financial sophistication. The more advanced MFIs are successful in breaking even in their operations—covering all their costs from income earned through the deployment of financial services. Those institutions that have sought to increase significantly the number of microentrepreneurs reached and, in some cases, to expand the types of products offered to this sector (e.g., savings) have turned to private sources of capital for funds and established regulated institutions. Because profits are a key ingredient to attracting private capital, these MFIs face the difficult task of balancing social and financial objectives: reaching large numbers of low-income microentrepreneurs while generating profits. In this context, the boards play a key role in ensuring that the MFI responds adequately to both objectives.

MFIs can be placed in one of three categories, based on how they define their mission. In Figure 2, one category is represented by the sphere client coverage (as defined by the number and economic level of clients reached). The second sphere in that figure represents profitability, as measured by a competitive positive return on assets or return on investment. The overlap of these two spheres represents the intersection between profitability and client coverage.

Most microfinance nongovernmental organizations (NGOs) fall within the client coverage sphere. For these institutions, success in fulfilling their mission is measured by the number and economic level of the microentrepreneurs they service. Although many NGOs are not financially self-sufficient, some that fall into this sphere have made financial self-sufficiency a goal that is on par with client coverage. NGOs that have converted into for-profit
institutions, however, must move beyond financial self-sufficiency to incorporate profit generation into their mission. The new for-profit MFI, as well as a small group of NGOs, has a dual mission, illustrated by the intersection of the client coverage and profitability spheres.

![Figure 2: The Dual Mission of MFIs](image)

As several institutions have shown, the goals of client coverage and profitability are not mutually exclusive, and there is no trade-off between social goals of providing services to very poor and unbankable clients and generating a profit. In different corners of the world, institutions operating both as NGOs and regulated institutions clearly illustrate this point: BancoSol (Bolivia), Los Andes (Bolivia), ACCION Comunitaria del Peru (Peru), K-Rep (Kenya), ABA (Egypt), and ASA (Bangladesh), among others. For example, BancoSol’s first-time loans start at US$125 and its average loan size is US$800; further, as of December 1997, it was one of the most profitable banks in Bolivia, as measured by returns on assets and on equity. ASA in Bangladesh had over 630,000 clients as of December 1997 and financial self-sufficiency of close to 140 percent, with loans averaging US$106. These institutions occupy the space in Figure 2 where the two spheres overlap.

In the **profitability** sphere, one finds new entrants to the microfinance field—commercial banks and finance companies—that are interested in the microfinance market because of the profit potential. These entrants seek client coverage only as it relates to expanding the market they reach.

Balancing a dual mission becomes more complex when the microfinance activity is not the sole or main activity of the institution. This profile fits an NGO involved in microfinance as well as health care, literacy, and other social programs, or a regulated financial institution for which microfinance is not a key business segment. In these situations, there might be little or no representation of microfinance issues at the board level, leaving, in the extreme case, the microfinance manager to deal with strategies or policies. In short, the governance function as it relates to microfinance is delegated to the staff. Also in these cases, the profits of the microfinance unit might be diverted by the boards of NGOs and regulated financial institutions to cover deficits generated by social programs or by other business ventures. This limits the ability of the institution to achieve high client coverage and superior profitability.

Through its composition and the priorities it sets, the board of directors directly shapes the extent to which MFIs seek to maintain the dual focus of profitability and client coverage. Ideally, for those institutions trying to strike a balance, microfinance boards would be composed of directors who personally represent the necessary balance. In the absence of such individuals, institutions may fill the seats on the board with relatively equal numbers of
persons from both orientations. On the commercial side, bankers and business people can assume the lead in ensuring efficient operations and focusing on the bottom line. To represent the development side, other professionals (such as academics or community leaders) can focus on the institution’s goal of client coverage.

Figure 3 suggests that an effective board should seek, through its own strategic decisions and policies, to move the institution in the direction of the shaded quadrant, where superior profitability and high client coverage—as defined here—are achieved. Such an approach affirms the importance of both the social and the profitability mission of an MFI and builds on the experience of those that have achieved it.

![Figure 3: Balancing Profitability and Client Coverage](image)

**Figure 3: Balancing Profitability and Client Coverage**

Closely linked to the issue of governance is the issue of ownership. The board of directors either consists of owners or represents the interests of owners. Aligning the interests of individual directors with the interests of the institution is key to realizing effective governance. Creating this alignment depends on understanding the issues associated with each of the four corporate structures of MFIs—public, nonprofit, for-profit, and credit unions. The specific corporate structure does not in itself define effective governance. For each, however, factors exist that may strengthen or undermine a board’s ability to fulfill its roles and responsibilities.

**Public Ownership/Government Corporate Structure**

With the one conspicuous exception of the government-owned Bank Rakyat Indonesia (BRI), public ownership of financial institutions chartered to service low-income

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14 Note that an essential ingredient in BRI’s success was the protection government officials gave the Unit Desa System to avoid political interference. For a full discussion of BRI and its unique success as a government-owned microfinance institution, see Robinson, 1994, and Churchill, forthcoming 1998.
populations historically has been a failure worldwide. In the best cases, well-intended, yet misguided, development policies have severely distorted the market by directing credit to microentrepreneurs at subsidized rates. The result has been unsustainable levels of borrower delinquency and a severe undermining of public confidence in government development initiatives. In addition, political interference and corruption have further undermined performance standards and confidence.

Although the model that prevailed in the last three decades has failed, public ownership of MFIs may be successful with economically sound credit policies and mechanisms to protect the institutional assets from political manipulation. Moreover, the extensive branch infrastructure of many government-owned banks, and the significant financial resources that the public sector brings to a given microfinance project, merit understanding the elements that make public sector involvement in microfinance successful. Several nascent efforts are worth noting as examples of new approaches; however, their early stage of development prevents drawing conclusions.

One example of government participation is found in South Africa in the public-private partnership, KHULA, which is providing funds for the microenterprise sector. Created in 1996 as a public company, KHULA is currently capitalized with public funds and provides the following products:

- Business loans to MFIs;
- Start-up loans for emerging MFIs;
- Technical assistance to MFIs;
- Equity investment in businesses; and
- A guarantee fund that allows MFIs to borrow from commercial banks.

KHULA adheres to market principles in its operations. The government has board representation. Once the fund demonstrates significant returns and attracts private investors, the government’s participation is supposed to decrease. Whether this occurs will be a true test of the ability to depoliticize government involvement in microfinance in a highly charged political atmosphere.

Banco del Nordeste in Brazil, a government-owned bank that is entering the microfinance field, presents another example of government participation. The bank has an extensive branch network and approximately 180 branches, and it understands the key methodological elements that have resulted in success in this field (i.e., market rates, ever-increasing loan size, and so on). Provided the bank is able to insulate itself from political pressure from the government—in terms of targets for numbers of clients reached, for example, which might be politically advantageous but result in unmanageable growth—Banco del Nordeste’s involvement in microfinance has much promise.

At the other end of the spectrum of government participation is the example of the newly created microenterprise bank, MIBANCO, in Peru. President Alberto Fujimori announced the creation of this bank at the Microcredit Summit in February 1997; in April 1998, MIBANCO was formally established. In this case, the Peruvian government played a key
role in facilitating the necessary processes for establishing the bank and in bringing together potential investees to ensure that it would be wholly privately held. For example, the government helped bring Banco Wiese and Banco de Credito to the table, both of whom took a 6.5 percent ownership interest in the bank. The remaining shares are held by the NGO ACCION Comunitaria del Peru (ACP), which sold its microenterprise portfolio to MIBANCO (60 percent); by PROFUND (20 percent); and by ACCION International (7 percent). ACP has five board members, with the other shareholders having one board member each, to total nine board members. The Peruvian government has no equity participation in MIBANCO; instead, there is an invited representative of the President for a two-year period, giving the government a voice but no vote.

In contrast to the MIBANCO example in Peru, the government of Argentina made US$40 million available for investment in microfinance. FONCAP, S.A., a private sector corporation under a fiduciary agreement with the Argentine government, was created in 1997 to wholly manage the resources made available by the Argentine government. FONCAP’s goal is to help create the infrastructure necessary to increase financial services to Argentina’s microentrepreneurs. FONCAP will help develop NGOs and other MFIs offering credit to microentrepreneurs by providing financial and nonfinancial services to MFIs. The structure of this entity, in which the government holds a minority position, and the fact that it is managed by a private entity, helps to ensure that the program does not become politicized.

The above examples demonstrate an evolution in the approach some governments are taking toward public ownership of MFIs. Recent initiatives reveal various mixes of public and private ownership, mechanisms to depoliticize the institutions, and an increased adherence to market principles. Although these efforts are relatively new—conceived and initiated in the last three years—if successful, they will open the door for more approaches by other governments.

Nonprofit NGO Corporate Structure

Although some NGOs have become or established regulated institutions to access larger amounts of capital and offer savings, the vast majority of MFIs worldwide operate as nonprofit NGOs. Thus, it is important to understand the strengths and weaknesses of this governance structure of microfinance NGOs.

In the case of nonprofit organizations, no owners exist. Donors provide capital for nonprofit MFIs as grants or concessionary loans. These may be private foundations, government foreign aid agencies, multilateral institutions, or individuals. For whom, then, do nonprofit boards act as a fiduciary? To whom is the board accountable? Although one can identify various key stakeholders in the NGO setting, as shown in Table 4 (see the following section, For-Profit Corporate Structure), the answer to the question of accountability is larger than

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15 In the early stages of an MFI’s existence, this capital is used for both operations and lending. As the institution matures and achieves greater levels of self-sufficiency, the loan capital is often obtained from local financial institutions.
any of the components identified in that table. Foremost in its accountability, the NGO board is accountable to the institutional mission as defined and approved by current and previous boards. It is imperative therefore that the institutional mission be clearly defined and accurately communicated to the institution’s various stakeholders, including donors, lenders, staff, and clients.

What drives nonprofit board members to responsibly fulfill their Duties of Loyalty and Care? Here, too, the answer lies with the institutional mission. To the extent that the board is composed of individuals who have a strong commitment to the mission, its members will be driven to responsibly fulfill their Duties of Loyalty and Care. As described in Chapter One, unless the board is strongly committed to the mission, one can not guarantee that directors will remain with the institution in times of trouble. The personal reputation and credibility of individual directors in being publicly associated with a success or failure also provide a compelling force in achieving effective governance.

As examples of failed governance in NGOs have shown, beyond their commitment to the mission, directors must have the ability to responsibly fulfill their duties. This is primarily a function of (1) their thoughtfulness and basic business sense—allowing board members to identify the warning signs of trouble—and (2) their willingness to pose difficult questions and face other board members and management with the problems they identify. Additionally, directors must avoid situations that often have led to serious problems or failures. A common mistake is concentrating power in the hands of the executive who may not receive proper oversight and who could lead the institution toward disaster. Further, because this person has not invested personal resources in the institution due to its NGO status, he or she can walk away more easily from a difficult situation. The failure of CorpoSol in Colombia exemplifies, among other problems, the concentration of power in the hands of an incompetent executive.

One can argue that the NGO ownership structure of no real owners presents a structural weakness in the NGO model. Nevertheless, one must not draw the conclusion that the lack of ownership necessarily results in unstable, risky institutions. The experience of MFIs under this model spans the spectrum from very weak to very successful. For example, the NGO model has yielded important successes within microfinance when individual board members have strongly identified with the institutional mission and possessed the ability to strategically guide the MFI and hold management accountable to performance objectives.

Good governance is common to successful NGOs. Examples, among many others, include PRODEM in Bolivia, ACCION Comunitaria del Peru (ACP), ADEMI in Dominican Republic, Kenyan Rural Enterprise Program (KREP) in Kenya, ABA in Egypt, BRAC and the Association for Social Advancement (ASA) in Bangladesh, and SHARE in India. The success of these institutions has created the option for them to transform to regulated for-profit financial institutions, an option several of these institutions have chosen. Effective governance and clarity about the concept of ownership in a context where there are no real owners is an essential factor in the success of these institutions.
For Profit Corporate Structure

Two types of for-profit MFIs exist. The first includes existing commercial banks and finance companies, referred to as “traditional financial institutions,” that have chosen to extend their services to the microenterprise sector. Sub-units or subsidiaries are created within these institutions to carry out microfinance operations, and a relatively small amount of the total institutional assets make up the microfinance portfolio. Most of the existing examples of these institutions have evolved in Latin America and include Banco de Desarrollo in Chile, Banco Solidario in Ecuador, Multi Credit Bank in Panama, and Financiera Familiar in Paraguay, among others. These institutions are downscaling because they believe that given the availability of microfinance methodology, they will be able to make a profit working with this sector. Investors provide the capital for these institutions with a primary interest in a return on equity that is competitive with alternative uses of their capital. As long as microfinance generates a competitive, risk-adjusted return for these institutions, their involvement is likely to remain and grow.

The second type of for-profit microfinance institution is the NGO that has established or is establishing a regulated financial institution, a topic that will be the focus of discussion for the remainder of this section. Unlike the board of a nonprofit MFI, the board of directors in this case comprises or represents the owners of the equity capital invested in the institution. Who is investing in these newly established MFIs? What motivates them to invest and is there an appropriate mix of these investors to ensure effective governance? To answer these questions, it is necessary to identify the nature of the capital at risk and the nature of the owners that sit on the boards of these emerging for-profit MFIs.

With few exceptions, there is little to no pure private capital in these newly created MFIs. Such pure private capital is provided by private individuals, corporations, investment funds, and financial institutions that are interested solely in making a return on their investment. These specialized MFIs are beginning to demonstrate that they can yield competitive returns, as exemplified by BancoSol. However, regulated MFIs are young, and the impressive results they have achieved as regulated institutions—which is what gives potential investors confidence in the transparency and therefore replicability of these results—spans only a handful of years. If these positive results continue, one can expect a greater participation in the capitalization of these institutions from pure private capital.

Today, however, in place of pure private capital are several forms of social capital provided by four principal sources: NGOs, private investors, public entities, and specialized equity funds. Each of these owners has its own set of concerns at stake. Understanding what an owner stands to lose or gain clarifies the factors that contribute to effective governance of a microfinance institution, as outlined in Table 4. The discussion that follows assumes that these different owners understand their roles and responsibilities and are deploying them effectively.

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Table 4: What is at Stake for Owners of MFIs?

<table>
<thead>
<tr>
<th>NGO</th>
<th>Private Investors</th>
<th>Public Entities</th>
<th>Specialized Equity Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Return on investment</td>
<td>Political concerns</td>
<td>Return on investment</td>
</tr>
<tr>
<td></td>
<td>Preservation of capital</td>
<td>Interest in entering a field new to them</td>
<td>Institutional mission</td>
</tr>
<tr>
<td></td>
<td>Sense of social responsibility</td>
<td>Return on investment</td>
<td>Long-term concern</td>
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<tr>
<td></td>
<td>Institutional mission</td>
<td>Sense of social responsibility</td>
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<td>Return on investment</td>
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<td>Preservation of capital</td>
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<td></td>
<td>Institutional mission</td>
<td>Return on investment</td>
<td>Long-term concern</td>
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</table>

Each of the owner types is concerned with a return on its investment; however, two important differences exist among owner types. First, the return on investment is typically the primary concern for private investors and equity funds, whereas NGOs and public entities may have other key priorities. Second, as defined by their institutional missions, social investors, in addition to the financial return on investment, are concerned with the depth (how poor are the clients) and breadth (how many clients) of client coverage.

**NGOs** that are investors in MFIs are featured in the first column in Table 4. Examples include PRODEM, which currently owns 35 percent of BancoSol, or K-Rep Holdings, which will own 25 percent of the K-Rep Bank. An NGO has its institutional mission at stake when it assumes an ownership role in a for-profit financial institution. However, its investment serves as a means for the NGO to further its mission. Therefore, its ownership role is to ensure that the MFI does not lose sight of the need to balance profitability with client coverage. In addition to expecting a social and financial return on its investment, an NGO owner has a long-term concern for the institution. Because the NGO continues to work in the microenterprise development field in some capacity, it is committed to this investment for the long term.

When evaluating the effectiveness of the governance role of an NGO in a for-profit institution, it is important to highlight the level of expertise and effort this role will require. That is, the NGO must be able to deploy individuals to perform this function, sacrificing at times other priorities like providing technical assistance to other institutions. The profile of the person deployed by the NGO—broad-based experience and facility with business issues, as well as an ability to express opinions independently in a board—is also key in ensuring effective board representation. Additionally, careful review of reports, financial data, and projections requires an additional time commitment and is necessary for effective participation on a for-profit board. Finally, beyond the human resources deployed by the NGO, the latter must allocate financial resources to cover expenses related to travel for board representation. If an NGO is to play a significant role (e.g., as chair of the board or member of the executive committee of a for-profit board), then it must make a considerable investment in time and travel of executive-level staff.

**Private investors** are concerned with capital preservation and obtaining a return on their investment. But as discussed above, considering the level of maturity of the microfinance field, pure private investors are rare in most markets. To date, the majority of private investment in microfinance brings with it a level of social responsibility. To the extent that
private investors make an investment in the MFI that is “significant” to them (independent of the absolute amount), they will bring to the board a sharpened interest in detecting early warning signs of potential problems. Deterioration in returns would affect a private investor adversely, and, in the case of a socially responsible investment institution, associate it with a weak or failed effort, outcomes an investor would seek to avoid. Private investors, however, bring not only a concern with profitability, but in the best of circumstances, can also access additional capital, which allows them to respond more quickly than other investors to a capital call.

**Public entities** include two very different types of entities—national governments and multilateral agencies (e.g., the World Bank, the Inter-American Development Bank, the Asian Development Bank, and the Corporación Andina de Fomento). They participate in the ownership of a microfinance institution largely in response to their own policies and to “political” issues, with the term *political* used in the broadest sense of the word. Investment in microfinance by public entities is often motivated by the expected social and economic benefits to microentrepreneurs, such as increased levels of employment and income. Consequently, these owners may be less concerned with the financial return they receive than with their participation in an activity that provides solutions to social and economic problems in a region or country that is of importance to them.

As public entities, multilateral agencies can contribute a significant percentage of the total equity of the MFI, although in absolute terms an investment in microfinance is small when compared with other projects in which these institutions invest. Moreover, while multilaterals have vast resources at their disposal, they cannot respond quickly to a capital call from an MFI because of their internal processes for decision making.

This is especially the case with multilateral agencies, whose internal structure and operating procedures often impede their effective participation as owners on a board. Staff that is responsible for a portfolio of loans or projects generally can not dedicate the necessary time to a board. In some cases, there may not be continuity in the person that represents the institution on a given board, thereby decreasing the institution’s ability to function effectively as an owner.

Nevertheless, some multilaterals are interested in contributing financial expertise and rigor as board members to the institutions in which they invest. Several of them—most notably the Inter-American Development Bank through the Multilateral Investment Fund—have selected to invest in specialized equity funds, which, as discussed below, can serve more effectively as owners of MFIs.

**Specialized equity funds** for this sector, such as ProFund in Latin America, are concerned primarily with their return. They also are concerned with achieving a balanced portfolio in terms of country risk, for example, and of meeting the criteria outlined by the fund’s charter, such as the breakdown in investments between microenterprise or small business. However, these owners also have an institutional mission at stake. For example, in the case of ProFund, where the founding shareholders are four NGOs that specialize in microfinance—ACCION,
Calmeadow, FUNDES and SIDI—the Fund mirrors the long-term interest in the success of the field that is key to the NGOs that established it.

An entity like ProFund brings additional important elements to the governance of an MFI. Because the Fund’s main purpose is to realize a gain on its investment, it allocates experienced staff and resources to monitor the performance of the MFI and to provide input at key junctures via board participation. Further, a specialized equity fund brings with it the accumulated expertise in this field through exposure and equity or debt participation in other MFIs. Finally, as compared to multilaterals, it is also important to highlight the agility a specialized fund has in making decisions. The example of Finansol, where ProFund played a key role in the re-capitalization of the institution, is a case in point.

Having defined what each potential investor in an MFI has at stake and what each brings to the board of the institution, one should ask what the appropriate mix of these various investors might be. The response is that in designing the participation of various parties on an institution’s board, one should not put balance ahead of the willingness and ability of these potential investors to execute their governance role. For example, including an NGO on the board that does not make the commitment necessary for effective participation will not provide the balance one seeks. Moreover, one should be very careful not to stereotype potential classes of investors—NGOs, multilaterals, governments, private sector, or equity funds. The key is to have clarity in the requirements for effective governance (as outlined in Chapter One) and to determine the willingness and capability of potential investors to perform the duties required for effective governance.

Credit Union Corporate Structure

Credit unions, in which owners are also the institution’s clients, constitute another form of ownership structure that provides services to the microenterprise sector. In some cases, an NGO has transformed itself into a credit union as a way of mobilizing deposits. Cooperativa Emprender in Colombia and ACEP in Senegal are two examples. In other cases, a credit union simply may be broadening its reach within a community to include micro-entrepreneurs. Though credit unions mobilize the savings of their client-members, in many countries, they either are not regulated or are regulated only minimally. Experts in the credit union movement, like Brian Branch and Christopher Baker, believe that the dearth of regulation of credit unions, combined with ineffective governance by the boards of these institutions, has resulted in insolvency for many of them. Branch and Baker outlined the following governance issues that face credit unions.

Misalignment of Priorities. One critical governance issue facing credit unions is the misalignment that can arise between the priorities of elected directors (who are clients of the MFI) and contracted management, as well as those of member-owners. Although such misalignment can occur in any financial institution, certain features of credit unions exacerbate this dynamic. Member-owners are clients who fall into two categories—net savers and net borrowers—each with its own interests and priorities in the functioning and financial

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standing of the credit union. Therefore, credit unions not only face the typical separation between ownership and decision making, they must also attend to the divergent objectives of owners, discussed in more detail below.

Board directors are democratically elected by membership (one person, one vote), but they may remain beholden to individual members who have mobilized votes on their behalf. Directors also may not necessarily possess the skills and experiences required to manage a financial institution.

**Board Representation of Owners.** The second governance issue for credit unions is the tendency toward unequal representation of the interests of the two categories of clients—net savers and net borrowers—on the board of a credit union. For example, in Latin American credit unions, net borrowers tend to dominate, as a result of the original intent of credit unions to provide cheap credit to borrowers. In this traditional service structure, savings received little attention and, therefore, credit unions were unsuccessful in attracting member savings beyond the amounts required to serve as collateral for loans from the institution. Borrower domination also resulted from international organizations channeling subsidized lines of credit through the credit unions and thus discouraging credit unions from savings mobilization. Similarly, the consequences of defaulting on these external funds were minimal and encouraged a culture of high loan delinquency. Not surprisingly, net savers were hardly attracted to such financial institutions.

According to Branch and Baker, experience has shown that better governance is achieved in credit unions that have a balance between net savers and net borrowers. Net savers are better able to hold management accountable because they have a vested interest in the institution’s profitability as a means of preserving the long-term viability of the credit union. They are also more successful in holding management accountable because of the threat of withdrawing their deposits. In contrast, net borrowers have a much shorter time frame and favor policies that undermine financial viability, such as low interest rates on loans.

Credit unions can regain the balance in ownership through reorienting services by adjusting interest rates, limiting reliance on external subsidized credit, and aggressively marketing savings services. According to Branch and Baker, as more and larger savings accounts are mobilized from moderate income groups, governance of the credit union is likely to improve. These net savers, with more at stake, will monitor management more closely.

**Prudent Regulation and Supervision.** The third issue is the lack of prudent regulation and supervision of credit unions. Because credit unions do not raise capital in the financial markets, they are not subjected to fiscal controls, yet they capture savings from their members. When implemented effectively, prudent regulation and supervision act as a check against excessive risk taking by the board and contracted management and thereby protect credit union members and their savings.

Branch and Baker suggest that specific guidelines for credit union regulations might include rules enforcing the roles and responsibilities of the board of directors, external auditor...
requirements, controls on insider operations, rules enforcing prudent disciplines, and loan risk control standards.

The discussion throughout this section suggests that each type of MFI demonstrates structural weaknesses related to ownership that can adversely affect an institution’s effectiveness in microfinance. Public entities, even in cases where microfinance is deployed successfully, may not have it represented at the board table. In the case of NGOs, there are no real owners. With commercial banks, the focus on profit maximization and lack of representation of microfinance at the board table is a structural weakness. Finally, in the case of credit unions, the differing priorities of net savers and net borrowers can create serious conflicts at the board level.

Understanding the structural characteristics of these different types of institutions should enable one to differentiate one type from another, but it is not enough simply to categorize by the type that exhibits the best ownership pattern. Ownership remains intrinsically linked to effective governance, and the latter is successful only if the terms and requirements outlined in the first chapter are followed.

**Fiduciary Responsibility of MFIs**

In general, the fiduciary responsibility of the board of any financial intermediary is considered greater than that required for other corporate entities. Protecting financial institutions and hence the financial system is a high priority for governments. Without solvent financial institutions, business, commerce, and the economy would become dysfunctional. Liquidity is essential for the deployment of a financial institution’s product: money. Moreover, because of their high leverage ratio and impact on the payments system, financial institutions require more stringent internal controls, and more prudent external supervision and regulation, than do non-financial entities.

In the absence of deposit insurance, as is the case in many developing countries, the fiduciary responsibility of the boards of financial institutions to savers increases even more. In addition to needing to maintain the solvency of a financial institution, the boards of MFIs, whether or not they oversee regulated institutions, have additional issues to consider in executing their fiduciary responsibility. These issues are discussed below.

**Access to Financial Services.** Microentrepreneurs as borrowers have few, if any, alternative providers of financial services. An insolvent MFI often means the end of a client’s access to capital at commercial rates. As a microenterprise grows, more individuals (and families) will come to rely on its success. Unlike middle-income individuals with access to multiple forms of financing, low-income microentrepreneurs’ growing circle of jobs and income will greatly suffer if the institution providing their financing falters. Similarly, microentrepreneurs as savers (i.e., in regulated institutions where they deposit their savings voluntarily or in nonprofit institutions that make savings compulsory for credit clients) are also at greater risk in the event of loss than are other sectors of the population. These low-income individuals
generally have no other pool of savings, nor do they have any significant financial support networks to assist them if loss occurs.

**Fiduciary Responsibility to Lenders**. Microfinance boards incur a fiduciary responsibility when a nonprofit MFI obtains funds from donors. However, the fiduciary responsibility increases when the MFI intermediates funds, by borrowing from a local bank, mobilizing deposits, or floating an instrument in the local securities exchange. The latter is the case in regulated institutions, like Finansol in Colombia, and in NGOs, like FUPACODE in Paraguay, which successfully issued securities in the local securities exchange.

**The Microfinance Field**. In the case of large-scale MFIs such as BRI in Indonesia, the Grameen Bank in Bangladesh, and BancoSol in Bolivia, insolvency would affect both the domestic and the international microfinance sector. The number of individuals suffering losses would be significant, which would harm the microenterprise sector in the country of the failing MFI. Additionally, insolvency of any of these large MFIs would set the microfinance field back many years. It is likely that lenders and investors to these institutions, and others considering investing in microfinance, would become concerned about the viability of this field in general and react by withdrawing or curtailing financial resources to microfinance.

**Risk Assessment in MFIs**

Providing financial services in general carries a set of risks that the board of directors must be able to assess in its role as corporate fiduciary. The fact that many MFIs operate in developing countries adds an additional layer of risk to these operations. The nature of microfinance, as discussed below, has always made risk assessment important. However, the growth experienced by MFIs, combined with heightened competition among MFIs in many settings and the evolution of some into regulated institutions, has required that microfinance boards have a greater ability to assess risk than was previously needed. In sum, although risk assessment has always been important for an MFI board, the factors discussed below have made risk assessment essential.

**Nature of Microfinance**. A basic characteristic of microfinance is its informal, decentralized process of gathering credit information. MFI loan officers gather the financial information used for making credit decisions at the business site; they have no annual reports from clients. Thus, MFI supervisors do not have the ability, as is the case in traditional banking, to check credit files for audited financial information to review a credit decision. Further, many MFIs lend to their clients without the traditional guarantees received by non-microfinance lenders. This lack of “fallback” requires that loan officers be clear about the institution’s credit policies and consistent in applying these policies. These conditions, when coupled with the high portfolio growth that many MFIs have experienced in recent years, require that microfinance boards be especially vigilant in their oversight function. Strong internal and external auditors are key to the board’s effective oversight in this area.
Another element of risk intrinsic to MFIs is the mobility of microentrepreneurs. Especially in those instances when an MFI is being intervened or liquidated, the recovery of a significant percentage of the institution’s loan portfolio can become a serious problem given the mobility of microentrepreneurs and the difficulty in locating them.

**Increase in Competition.** With the increased competition in the microfinance field, institutions are beginning to expand and diversify their financial products. For example, some MFIs are offering individual loans in addition to group loans and fixed asset as well as working capital loans. Boards must ensure that the appropriate mechanisms are in place (e.g., pilot-testing new products) to assess the risk of introducing these new products. As financial margins are squeezed, an institution may need to become more efficient to maintain its current level of profitability. Additionally, an MFI may attempt to grow and reduce its cost of funds quickly to secure a larger share of the market or enter new regions in the country to outdistance the competition. Boards must ensure that the institution’s growth can be managed effectively, and that its systems and staff are equipped to maintain high asset quality.

**Financial Analysis/Human Resource Integration.** NGOs that have established regulated MFIs and can access a broader range of funding, including issuing certificates of deposit and mobilizing savings, require boards with strong financial skills that can effectively assess risk. This expertise is greater than what is needed in an NGO whose funding sources may consist primarily of donations or concessional loans. The expanded funding possibilities require that the boards of the regulated or highly developed nonprofit MFIs assess issues such as mismatches of assets/liabilities in loan maturities, currency risks, and interest rate re-pricing periods.

NGOs that have established regulated MFIs must effectively integrate personnel that comes from the original NGO and private sector (usually banking) staff hired to strengthen the institution’s financial and banking expertise. The adjustment process required to integrate these two staff types has, in some cases, proven to be long and difficult and can emerge as an added risk that the board should consider.

The above factors are particularly relevant to any discussion of governance for MFIs. They demonstrate that although the microfinance field can avail the knowledge and experience accumulated in the topic of governance, this field has unique characteristics that require special attention. For those MFIs that are establishing regulated institutions and therefore designing capital and board structures, the governance issues outlined here provide the basis for addressing them in their own practice. The challenge for all MFIs—nonprofit NGOs; newly created, regulated MFIs; and credit unions—is to emerge with strong and long lasting governance structures that will help ensure their long-term sustainability. Toward this end, Chapter Three expands the discussion from issues specific to microfinance to identifying best practices in microfinance governance.
CHAPTER THREE
ACHIEVING BEST PRACTICES IN MICROFINANCE GOVERNANCE

This chapter highlights key issues in board membership, structure, and procedures to be considered in achieving best practices in microfinance boardrooms. Given the roles and responsibilities of a board and the governance issues specific to microfinance, certain practices and principles must be required by the board as it carries out its work. The information presented in this chapter is based on governance literature and the opinions of experienced individuals who advised this research. It is but a point of departure in identifying those practices that lead to effective governance and in providing some practical guidelines on this matter. The logical next step, which is outside the scope of this document, is to survey and analyze governance practices in specific MFIs to draw conclusions about the specific practices that lead to effective governance.

MEMBERSHIP

The relevant areas of board membership are composition, size, terms, director removal, and board evaluations. They are discussed in turn below.

Composition

Although board structures are relatively similar across institutional types and sectors, the individuals who compose the board display greater variation. The quality of board members is particularly important at two levels: to hold management accountable and to respond to external actors and issues of external accountability. Investors, and increasingly donors, consider the character and involvement of the board as assurance that their funds will be used properly. Moreover, bank superintendents evaluating the approval of a new regulated MFI will be keenly interested in the composition, skills, and financial position of the board. This level of interest is warranted because the directors will need to provide critical oversight of the operations and potential mobilization of replenishment capital if the institution becomes insolvent. In examining board membership, one should consider the following factors:

- The skills and characteristics of the directors;
- The directors’ understanding and commitment to the dual mission of microfinance;
- The directors’ ability and willingness to fulfill their Duties of Care and Loyalty; and
- The development of the board.

Skills and Characteristics of Microfinance Board Directors

Effective governance depends primarily on the skills and characteristics of the individual directors. Collectively, these attributes should represent a diverse set of experiences, backgrounds, areas of expertise, ethnicity, and gender. Although the main prerequisite for
effective governance of a financial institution is a solid business sense, an MFI board can provide additional guidance to the institution if its members have expertise in microfinance. Of equal value is expertise in law, marketing, or information technology, which are particularly relevant to microfinance. The level of board members’ experience and influence in their respective fields may vary significantly in a board that combines members able to dedicate greater time and energy to the board with those who can play more of a representational role. The following skills are important assets to any MFI board:

- **Business sense.** A microfinance board must have solid business sense, with some financial expertise in two areas. The first area is financial analysis, which allows the board to understand and measure the performance of the institution in the key areas of capital adequacy, asset quality, profitability, and liquidity management. The second area is financial auditing, which provides the board with the capacity to adequately assess the strength of the institution’s internal control mechanisms.

- **Microfinance experience.** Given the relative newness of MFIs, there are not many experts in this field. However, including individuals with some experience in this area on the board can be very valuable to the institution.

- **Financial markets expertise.** Individuals who understand the local financial markets and know the players, as well as understand or have experience in international financial markets, can be important contributors as MFI board members.

- **Legal and regulatory expertise.** All MFIs, but especially those that have entered the regulated financial sector or are considering such a change, will benefit from individual directors who bring legal expertise to their boards.

- **Marketing expertise.** With increasing competition, MFIs are being required to more aggressively “sell” their products to microenterprise customers. Because marketing is still a relatively new area for MFIs, directors with expertise in this field and in product development can provide guidance to MFIs.

- **Public relations.** MFIs must be concerned with the image they project to the client and to the public at large and must be able to conduct outreach campaigns.

- **Technology expertise.** Increasing competition, emphasis on cost reduction, and the increasingly complex nature of microfinance operations (e.g., savings mobilization and diversified products) require that institutions enhance the information technology they use. Integrated and automated information technology systems enable the institution to better evaluate its performance at any given moment, as well as reduce operating costs. Boards will benefit from individuals with technological expertise.

- **Fundraising.** For the nonprofit MFI, board members are expected to play an active role in fundraising. Individuals with prior experience and contacts represent a significant asset.

In addition to the above skills, the characteristics described below should be considered in composing a board.

**Demographics.** MFIs that operate nationally may select directors to represent different regions. Moreover, some MFIs, as discussed previously, have directors who reside outside the country where the MFI conducts its activities. These directors might contribute in broadening the perspective of the microfinance board. However, the challenge is to ensure
that they or their institutions are committed to expending the time and resources to participate actively in board meetings. To facilitate the participation of international directors, boards must avail innovative uses of technology and ease some of the restrictions on attending meetings, such as allowing international directors to cast votes by phone when distance makes their attendance difficult.

**Executive and Staff Directors.** The CEO is often a director on the board, and other executive and staff members sometimes are included as directors as well, especially when a senior manager is being groomed to succeed the CEO. Consensus exists among governance experts, however, that for adequate oversight, the number of executive directors serving on a board should be limited.

The situation at Citi Savings and Loans (Citi S&L), a microfinance non-bank financial institution in Ghana, illustrates this point. This institution was started with private capital by three individuals who serve as both managers and directors of the institution. However, Citi S&L has recently determined that the dominance of insider directors on the board does not provide the organization with sufficient oversight to assuage the concerns of banking regulators and potential donors. Consequently, the institution is now trying to identify new investors who also can serve as outside directors.

**Client/Employee Participation.** The risk that arises when clients or employees sit on the boards of MFIs is that their presence may become one of form rather than substance. The substantive aspect of client or employee participation on boards lies in ensuring that the board representatives for either group actually speak for their constituency and are not silent participants who acquiesce to other board members. Also to be considered when clients, for example, are on the board is whether they are then precluded from borrowing, and how one might prevent related-party loans.

In the case of the Kenyan NGO, K-Rep, the institution was concerned about ensuring that the three key organs—board, management, and staff—function semi-independently to avoid potential conflicts of interest. Thus, although the ownership of K-Rep Bank comprises both private investors and an employee association, the board has a slightly different composition. The employee association owns 10 percent of the shares of K-Rep Bank, but the association’s shares are a special class that does not carry voting rights and therefore does not allow the association a board seat.

Client/employee participation is an area of interest to many MFI institutions. Therefore, the lessons learned from the experiences of MFIs worldwide need to be documented and disseminated.

**Independent Advisors.** Although the directors of the board are selected for their particular skills and expertise, instances will arise when the board requires external advice or assistance. This occurs regularly with auditors, for example, and in extraordinary circumstances when the organization is considering a radical change, such as an NGO’s transformation to a regulated financial institution. Given the rapid evolution of microfinance, these special cases might occur more frequently in the future and could require guidance.
from those with expertise in compensation, law, and investment banking. In addition, the board may want to employ executive search firms to find new directors or to fill senior management positions.

The board must also attend to the process of electing board members. Both board members and executive level staff can play a role in identifying possible candidates. However, it is the role of the nominating committee to vet these candidates, to interview them on behalf of the board, and then to present recommendations to the board for a full board vote.

**Commitment to the Dual Mission of Microfinance**

Although effective governance requires diverse people who complement one another by contributing a variety of skills and experience, such diversity must be achieved without sacrificing agreement on the dual mission of MFIs. This dual mission is to provide client coverage (in terms of depth and breadth) and to achieve financial self-sufficiency. Individual directors may emphasize one mission more than the other, but in a well-functioning board, differences of emphasis will foster productive and lively discussions that result in well-reasoned strategies and solutions for the institution. The chairperson of the board is key in melding the two perspectives to establish consensus on the direction of the institution.

**Fulfilling the Duties of Care, Loyalty, and Obedience**

The third dimension of board composition involves the director’s ability and willingness to fulfill the Duties of Care, Loyalty, and Obedience, which are affected by the following key issues:

**Relationship between the Board and the CEO.** Board members and the CEO must maintain a degree of distance. Loyalty to the CEO, rather than to the organization, will not allow directors to make independent, responsible decisions, particularly on issues such as management performance and compensation. This issue is particularly relevant to many nonprofit MFIs in which the CEO/founder has hand-picked the board.

A well-functioning relationship between the board and the CEO also necessitates that both parties are clear about their respective roles. In brief, the board’s role is to provide guidance to management in the overall strategic direction of the organization, leaving the CEO to actually manage the institution. If the board loses confidence in the CEO, its role is not to step in, but to replace the CEO and manage the smoothest transition possible for the organization.

**Political Advantage and Conflicts of Interest.** Because microfinance involves many small loans, it has the potential to affect the lives of many people. Moreover, given that MFI clients are poor, it can be tempting for board members (or those in management positions of MFIs) with political aspirations to use their positions in the MFI to enhance their political futures.

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19 Bowen, p. 55.
Directors of MFIs must therefore be selected for their loyalty and commitment to the institutional mission above any political aspirations they might have.

Conflicts of interest occur when directors engage in related-party transactions, in nepotism, or in misappropriating property. Also, in many smaller, undeveloped economies where microfinance institutions operate, there may be only a handful of prominent business and community leaders. This situation may lead to reciprocal directorships, where friends render mutual favors by serving on each other’s boards. Here, too, board members must be mindful of their Duty to Loyalty and place the interests of the institution above other considerations. Similarly, family members should not sit on each other’s board, because it creates incestuous relationships and potential conflicts of interest that undermine effective governance.  

**Board Development**

Integral to composing a board is developing the knowledge and skills of its individual members. However, it is unlikely that board members come to an MFI with much exposure, if any, to microfinance. Moreover, the quickly evolving nature of microfinance requires boards to stay abreast of changes in the field to be able to fulfill their oversight responsibilities more effectively. Board development, therefore, consists of orienting new directors and continually educating existing members.

**New Director Orientation.** To build a new director’s commitment to the organization and to ensure that he or she understands issues specific to the industry and the institution, it is as necessary to orient new directors as it is to orient new staff. The following should be the minimal requirements for board member orientation:

- Receipt of previous board reports and minutes, annual reports, recent technical assessments, and biographies of the other directors;
- Meeting with managers and key staff; and
- Visits to the institution’s main office and branches and with clients.

**Continuing Education.** The education of board members needs to be ongoing. It is useful for directors to draw on the expertise of key staff members (besides the CEO), individual directors, and outside experts in the field to inform and update the board. Additionally, directors should visit successful world models in the field to help cement a vision of where their organization is headed.

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20 Avoiding reciprocal directorships and maintaining distance is rooted firmly in North American corporate governance, where it is believed that these arrangements promote conflicts of interest. However, in Asian and European governance models, a tight web of interconnectedness is expected if not encouraged. In these situations, a bank with a large loan to an MFI might expect a seat on the board. In the North American model, however, the bank representative would not be able to act in the best interests of the organization in a situation where it conflicted with the best interests of the bank.
Size

The capacity of the board to function effectively partly depends on its size. Although there is no optimum number of board members, extremes of size should be avoided. A microfinance board should be big enough to incorporate the various skills and perspectives as outlined above. However, it must be small enough to accommodate the need for frequent meetings, given the characteristics of microfinance. Because many MFIs have experienced rapid growth, the board has required frequent interaction with management to keep abreast of the institution’s performance. Moreover, the volatility in portfolio quality experienced by many MFIs also contributes to the need for frequent board meetings to monitor portfolio quality. Monthly board meetings are not unusual. Given frequent meetings, a board that is too small or too large may be unable to regularly achieve a quorum (an established number of members required to conduct business, as per the institution’s bylaws).

In addition, boards should consist of an odd number of members to avoid potential deadlocks when votes are taken. Boards with staggered terms may also want the number of directors to be a multiple of the term length so that the same number of seats are open each year.

Terms, Director Removal, and Performance Reviews

All microfinance boards should have mechanisms for regularly reviewing the performance of individual directors and for replacing those who are not providing the organization with the leadership it requires. This is particularly important in microfinance boards because of the changes facing this field and the need for directors who possess the vision and skills to respond effectively to these changes. Moreover, because boards of MFIs tend to combine individuals from diverse backgrounds in an effort to address the dual mission of this field, even a very able chairperson might be unsuccessful in ensuring that the board functions effectively.

Terms. Various ways exist to change the composition of a board. One is through mandatory retirement, which although an effective strategy for older members, is not adequate to remove a younger member. Board membership therefore often is limited to specified terms, and some governance experts believe that the number of consecutive terms should also be limited. In setting terms, however, the board must strike a balance between a tenure that is long enough to allow members to develop expertise that results in substantial contributions and to provide continuity of policy and practice, yet short enough to secure constant freshness of viewpoint.

Several MFIs have adopted multi-year (e.g., three years), staggered terms, which seem to provide the desired balance between continuity and renewal. In contrast, boards that renew annually—which is often the case in corporate settings—have more of the illusion of renewal than is actually the case. These experiences have shown that one-year terms tend to evolve into permanent terms. Finally, rotation of terms should be established to ensure continuity on the board. In practice, then, the board might have only one-third of the terms expiring at any time.
**Board Performance Evaluations.** A complementary process to setting terms and term limits is evaluating board performance, a practice that is relatively new to this field. In fact, often, little attention is given to the performance of the board or of individual directors until a crisis occurs.\(^{21}\) The success of board evaluations depends on the following factors:

- Setting the right criteria for evaluating board members;
- Securing the right party to conduct the evaluation, such as an outside advisor with expertise in this area; and
- Having the political will and the structures within the board to carry out the recommendations from the board evaluation.

At a minimum, there should be an attendance requirement for board and relevant committee meetings. Individuals who do not attend the prerequisite number of meetings would not have their positions renewed when their term ended, unless extenuating circumstances existed.

One approach to performance review is to encourage directors to conduct a self-review. This allows the director to analyze whether his or her participation continues to be mutually beneficial. In addition to self-review, or as an alternative, the board should consider if it is as effective as it should be. To address this issue, the board, as a whole, can begin by asking the following questions:

- Has the board properly defined the vision for the institution and is it thinking strategically about the institution’s future?
- Does the board have a thorough understanding of the context in which the organization is carrying out its activities?
- Is the board functioning properly—are meetings held regularly and run efficiently, do discussions allow for different viewpoints to be expressed, do the management and the board communicate openly?

A detailed checklist should be developed to assess these broad questions and to address agreed-upon evaluation criteria. This checklist can be used, either by board members or by an external advisor, to evaluate the board’s performance.

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**Structure**

The relevant areas for discussion of board structure include the separation of the roles of board chair and CEO, the role of the chair, and board committees.

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\(^{21}\) Demb and Neubauer, p. 161
Separating the Positions of CEO and Board Chair

There are many persuasive reasons for splitting the positions of CEO and board chair. First, it avoids concentrating power in one person, who, if playing both roles, would be responsible for the strategic and operational activities of the institution. Separation ensures the voicing of two opinions and underscores the fact that the CEO reports to the board. The chair serves as an intermediary between the CEO and the outside directors. The chair should maintain a degree of detachment that allows him or her to question basic assumptions about the institution. Separating these positions also facilitates a regular performance review of the CEO and avoids any risk that the CEO will preside over a discussion of his or her own future.

To ensure that such a split is functional for an institution, both the CEO and the chair must play a strong leadership role and be equally involved in fulfilling their respective responsibilities. Although both individuals must provide direction, it must be clear that one represents the board and the other represents management.

A potential disadvantage of this split, however, is the possibility that the chair and CEO will develop a relationship that is too close or too distant. In the first case, the chair could become the spokesperson for the CEO’s objectives and begin to sidestep important issues that contradict the CEO’s position. In the second instance, the chair and CEO may not find an effective way to work together, either because mutual trust has been eroded or because they compete with each other.

Role of the Chair

In general, the chair of the board is responsible for the smooth operation of the board, including setting meeting agendas and calling and presiding over meetings. For microfinance, the chair’s job is made more challenging by the likely presence of diverse viewpoints representing the dual mission of the institution. Ultimately, the chair must ensure that the board reaches consensus in a way that is congruent with the institution’s mission and that best allows full and free participation.

Accomplishing this task requires effective meetings, which depend, in part, on the quality of the relationships among the participants. When group members are supportive of each other, they are encouraged to participate in discussions, ask clarifying questions, share ideas and opinions, and listen without judgment. Many boards organize annual retreats for this purpose, as well as to plan for the year and to explore substantive issues in more detail. These retreats give directors a chance to share formal and informal time and to establish a camaraderie that

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22 It is very common in North American corporations for the roles of Chair and CEO to be combined, yet the recent trend in the governance literature strongly advocates for a separation of the two. A separation is the norm in the nonprofit world where there is a division of labor, with a paid executive functioning as CEO alongside a part-time, usually unpaid, chairperson.

will assist them in being more effective in future board meetings. If organized well and facilitated properly, a board retreat will help build an enthusiastic and tightly knit board.

Committee Structure

The use of committees to accomplish certain tasks is based on two key premises. The first premise avers that smaller, focused groups can be more efficient than larger ones. The second posits that smaller groups can discuss issues with greater depth and, if the committees are well configured, with greater expertise than can the full board. Board committees should be used to improve the quality and efficiency of the board by defining ways to address an issue that the board then considers in making a decision. Boards can assign considerable responsibility to committees; however, committees should never make a policy decision for the full board. For committees to be effective, their work, role, responsibilities, and mandates must be clearly outlined.

Committees are also a powerful mechanism for increasing the interaction between outside and inside directors. Through committees, board members have the opportunity to play an active role in addressing the issues that the institution confronts without becoming involved in its operations.

The two main types of committees are standing committees and special committees. Special committees, which are not outlined in the organization’s bylaws, are established for a specific purpose and are disbanded when they have completed their task. For example, an MFI that is undergoing transformation can establish a special committee to take the lead in this process.

Standing committees may include an executive committee; an audit and finance committee; a nominating committee; a human resources committee; and, in the case of non-profits, a fundraising committee. These are detailed below.

**Executive Committee.** Many boards have Executive Committees made up of board officers, the chairs of the other board committees, and one or two others considered important to this committee. This committee, when functioning effectively, plays a key role in directing the activities, discussions, and decisions of a board. The Executive Committee:

- Discusses issues in preparation for a full board discussion;
- Makes decisions that the board has assigned to it, such as setting the salary of the CEO, and addresses policy matters that the board has delegated to it;
- Highlights agenda topics that the full board should discuss; and
- Establishes an initial level of consensus on difficult issues that the board must address.

Executive Committees meet often, and because they play an important role in the overall functioning of the board, should exist in all or most boards.
Nominations Committee. The nominations committee nominates new board members who are independent of management and sufficiently skilled and brings these candidates for full board consideration and vote. Variations in the nomination process exist within the microfinance world. For example, in mutually owned financial institutions and some nonprofits, particularly those in Asia (e.g., ASA and BRAC in Bangladesh), the board comprises clients who are elected as representatives of various regions. In government-owned MFIs, such as Bank Rakyat Indonesia (BRI), the board is appointed by the Minister of Finance.

The nomination of new directors has unique importance in NGO microfinance institutions, in which the CEO often hand-picks the board of directors. Through this nominating committee, the board can play a decisive role in selecting new directors to ensure that they are independent and skilled. However, this should not discourage the CEO from contributing suggestions for new directors. To achieve a close working relationship between the board and CEO, the CEO must be involved in recruiting directors. Sometimes, boards have the CEO serve as an ex-officio member of the nominating committee, allowing that individual to engage in discussions with committee members as candidates are considered.

This committee can also play an active role in evaluating the performance of the board, its committees, and individual directors. The nominating committee could determine whether directors assess their own performance or the performance of their peers, or if the board contracts with an external consultant to assess the board’s performance. This committee would then assume responsibility for coordinating the assessment process and removing any inactive directors.

Audit and Finance Committee. This is an important committee for a microfinance institution, as it empowers a board to fulfill its risk assessment responsibilities (as discussed in Chapter Two). Additionally, this committee provides oversight for safeguarding the institution’s financial resources. Both internal and external auditors should report directly to the audit and finance committee. Although it is the responsibility of management to design and implement an effective internal control system, the audit committee can have the role of overseeing the control procedures. This committee reviews the proposed budget carefully and, in some cases, may make budget suggestions to the staff before the budget is considered by the full board.

Human Resource or Compensation Committee. The human resource committee works closely with the institution’s Human Resource Development Department and provides oversight for personnel matters. Its role becomes crucial when the institution experiences a staff-related problem, such as a lawsuit or grievance against the institution. This committee also supervises the orientation of new directors and seeks ongoing exposure of current directors to topics relevant to the institution and the microfinance field.

Fundraising (or Resource Mobilization) Committee. Most nonprofit organizations have a fundraising or resource mobilization/development committee to oversee the solicitation of funds for the institution’s operations and special projects. Although the entire board is responsible for the organization’s performance, the fundraising committee is meant to
actively engage in obtaining funds. In most nonprofit microfinance institutions, the CEO is responsible for soliciting funds and may call on board members to open doors or to carry out the fundraising activity themselves.

**PROCEDURES**

A well-organized microfinance board consisting of highly qualified and committed individuals will be limited in its effectiveness unless it establishes clear procedures and processes of communication. The following outlines the major types of documentation that a board should have in place or maintain over time.

**Board Documentation**

Board documentation consists of written record or minutes of the outcome of the board’s meetings. Board minutes provide a record of the issues considered by the board, the main points of its discussion, the motions made, and the resolutions the board approved. Boards vary widely in the level of detail in recording their proceedings. In some cases, board meetings are taped and the minutes are transcribed from the tape. Other boards may choose to record only the salient points and resolutions in a highly abbreviated manner. Regardless of the level of detail, board minutes, which include the four areas listed above, must be kept if the board is to function effectively.

**Constitution/Articles of Incorporation and Bylaws.** These records may be combined into a single document. In the case of a nonprofit, the constitution is a statement that provides the basic authorization for the institution’s existence. The bylaws define the rights and obligations of various officers or groups within the corporate structure and set rules for routine matters such as calling meetings. They also include directives that define the structure and procedures of the board. In the case of a for-profit organization, the articles of incorporation must include information about the types of equity securities the corporation is authorized to issue to raise funds. These articles also may include other restrictions or specify governance rules in more detail. As the institution evolves, its bylaws will require revisions, including changes in the area of governance. It is important to keep the bylaws up to date.

**Statement of Policies (or Board Policy Manual).** Policies, which can be defined as broad or overarching statements related to conduct, strategy, and operation that guide the activities of an institution, are a matter for board concern and decision making. Policy decisions should be recorded in the minutes that are distributed to board and senior management. Policies should be explicit, current, literal, centrally available, brief, and encompassing. Policy making requires an understanding of where the line between the board and management lies. How far reaching should an effective board policy be? How detailed? The board should establish such

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24 The following guidelines are based on legal requirements in the United States.
26 Carver, 1990, p. 42.
broad policies governing the institution as necessary to cover continuing or recurrent situations in which consistency of action is desirable.  

Monitoring An Institution’s Performance

In addition to the discussion on CEO performance in Chapter One, several factors contribute to effective assessment of the institution’s performance. Financial information and other measures of performance need to be presented clearly, consistently, and regularly so that warning flags may be seen and serious problems anticipated. Similarly, the board needs to be able to ensure that the information is not hidden or distorted. For example, if one of the institution’s branches is experiencing a deterioration of its portfolio, the board, with management, must respond quickly to this issue.

In the case of nonprofit MFIs that operate with a combination of subsidies and commercial funds, the financial information provided to the board should reflect the institution’s real level of self-sufficiency. Such information is necessary to ensure that decisions are made based on the real financial standing of the institution. This issue is particularly important as institutions seek to access increasing levels of commercial funding for their portfolios.

Although the financial status of an institution can be assessed with effective reporting, in general, qualitative issues related to performance are harder to measure. Job satisfaction among staff, compensation issues, and characteristics of the institutional culture are some of the factors that contribute to the effective functioning of the institution. Board members must find ways to ensure that they can assess such factors to determine the overall performance of the institution.

Consideration of the above principles and practices of board membership, structure, and procedures will contribute to the effective execution of the oversight functions of an MFI board. Maintaining such effective governance, however, is a task that requires ongoing care and attention. A board’s ability to respond to such challenges by adjusting its composition, structure, and procedures will determine its long-term success.

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27 Houle, p. 92.
CHAPTER FOUR
NEXT STEPS IN ADDRESSING MICROFINANCE GOVERNANCE

This document represents only a first step toward addressing the governance of microfinance. It has highlighted the main governance issues for the field and attempted to provide some guidance in the practical implications of these issues as they relate to board membership, structure, and procedures. The next step is to access the experiences and perspectives of selected microfinance boards worldwide to build on the information presented here. With this additional input, gathered through surveying microfinance board directors and executive managers, a more informed analysis will result to direct effective governance practices.

The following three areas must be part of any such further analysis. These three areas cut across the topics presented in this document related to microfinance governance issues and to issues of board membership, structure, and procedures.

CONFLICTS OF INTEREST

A particular challenge facing microfinance boards is the ability to fulfill their Duty of Loyalty. Regardless of the ownership structure, boards face various forms of conflict of interest. Related-party transactions, one example of conflict of interest, finds board members engaging in an activity that benefits one institution on whose board they serve to the detriment of another institution on whose board they also serve. Another example is the practice of nepotism, or hiring family members to fulfill a function when other individuals might be better qualified to perform that function and demand equal remuneration. Yet another example of conflict of interest arises when board members misappropriate the resources of the institution, whether they be the institution’s human resources or its property. Expensive trips by board members that benefit the institution only minimally, but that are covered by the MFI, constitute an example of such conflict of interest.

Other areas of conflict of interest involve the practice of reciprocal board service, which could result in board members being unable to place the institutional mission of the board above other interests, thus limiting the oversight provided. Conflicts of interest also arise when institutions with common board members begin to compete. This situation can arise when, for example, an existing NGO creates a regulated entity yet continues to operate in the same markets as the newly created institution, led by a group that serves on both boards. The challenges that emerge from these situations need to be explored to understand how they can be overcome.

OWNERSHIP IN MICROFINANCE

Issues of ownership, and hence governance of MFIs, continue to evolve with the increasing integration of the private sector into microfinance. Significant experience with the issues of microfinance ownership has already been amassed within the field. It would be useful to
analyze the models of ownership that have emerged and to synthesize and disseminate the lessons learned from these models.

For example, the issue of client or employee ownership in microfinance is of interest to many in the microfinance field, but the experience of institutions that have addressed these issues needs to be documented and disseminated. Further, the structure of ownership, whether it is a majority or minority position, and the implications for governance deserve greater attention.

Another topic to investigate and document is the evolution of private ownership in industries such as health care, in which many institutions like MFIs struggle with balancing the dual goals of serving a social mission and seeking sustainability and profit. What lessons can the microfinance field learn from other more mature industries that have dealt with some of the same ownership and governance issues facing MFIs?

**Dynamic Nature of Microfinance**

As has been mentioned throughout this document, the microfinance field is facing rapid change as a result of increased competition, a movement toward the commercial model of microfinance, and increased participation by governments. This change directly affects the governance of MFIs on the following levels:

- **Composition of the board.** A board’s composition must reflect the set of skills and characteristics that board members need to ensure that the board is able to provide effective governance in this changing environment.

- **Effective functioning of a board.** In order that a microfinance institution’s board be able to respond effectively to this evolving field, certain key areas of board functioning must be addressed. These include board development (new director orientation and continuing education), mechanisms such as terms that allow boards to change and grow, board documentation, and the performance evaluation of the board. Surveys that address how institutions have dealt with these issues and the results they have had would make an important contribution.

- **Role of leadership by microfinance boards.** With the continued maturation of the microfinance field, it will become increasingly important and appropriate that boards and individual directors of MFIs provide leadership. Those board directors who are responsibly fulfilling their role as a director will be best positioned to shape both the institutions they oversee and the context in which their institutions operate.

As the experiences of additional institutions are incorporated into the dialogue on microfinance governance, other areas for investigation will undoubtedly be identified. Similarly, a broader pool from which to draw solutions to governance issues, old and new, will emerge to inform this very important topic in the microfinance field.
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