Internal Account Management
A Toolkit for Village Banks

Catholic Relief Services Microfinance Unit
The SEEP Network

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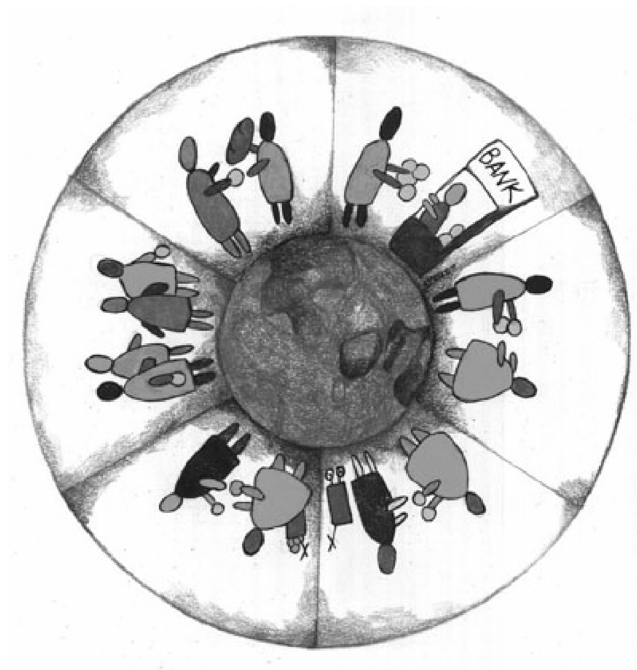

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Foreword

As I write this, I've just returned from Africa. There I saw small amounts of borrowed capital make dramatic improvements in the lives of the world's self-employed poor. Despite limited education and a daily struggle to survive, these microentrepreneurs, predominantly women, grow successful small businesses that enhance the lives of their families.

The village bank's internal account plays a crucial role in the economic development of these families and their communities by increasing the pool of available capital and extending the number of eligible borrowers. Yet it imposes its own challenges on practitioners: to increase field capacity; keep pace with the demands of program growth without sacrificing quality; and distribute power, decision-making and control to those most affected—the clients.

To successfully meet these challenges, practitioners require systems and models that they can adapt to suit their unique circumstances. *Internal Account Management: A Toolkit for Village Banks* provides just such a system. It charts the essential steps necessary to manage the internal savings of community groups and includes practical case studies and user-friendly procedures. In short, it makes clear the process by which agencies and their village banks can manage group or community funds—easily, accurately and efficiently.

Catholic Relief Services (CRS) is proud to have collaborated with members of the Small Enterprise Education and Promotion (SEEP) Network Poverty Lending Working Group to design, develop and publish this toolkit. We thank our colleagues for contributing lessons and best practices and we hope that many similar materials follow.

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Baltimore, MD USA, September 1999

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Special thanks go to Candace Nelson for having contributed most of the training activities described in Section Two. These activities are the key to helping village banks use the tools in this manual. Without her efforts this manual would not be complete. Appreciation also goes to Jimmy Harris of DAI, and Elaine Edgcomb and Dana de Kanter of the SEEP Network for their unflagging support and encouragement.

The tools and exercises that make up this manual were largely contributed or created by various members of the SEEP Poverty Lending Working Group. Kathleen Stack and Ellen Vor De Bruegge of Freedom from Hunger contributed the discussion guide and case studies on managing and safeguarding internal account funds, the internal account loan feasibility analysis, the tough love case, the member audit guidelines and parts of the audit tool set. Jack Young of Freedom from Hunger created the monthly trouble report. John Bronson of Project HOPE contributed the guidelines for collection on delinquency; Dave Larson and Ken Graber developed the savings training tools. Bill Farrand of Catholic Relief Services, the grantholder, created the internal account recordkeeping tool set, and Michael McCord of FINCA/Uganda created parts of the audit tool set.

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Thanks also to Shirley Lunde of Lunde Consulting and Sheryl Henry for layout and editing, and Tim Peterson and Jim Heskett for graphics.

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Contents

Introduction

Over the past two decades, microlending programs have demonstrated remarkable success in breaking the cycle of poverty among the world's self-employed poor. The largest microcredit agencies have been joined by literally hundreds of smaller agencies at work in countries around the world. Village banking programs now control tens of millions of dollars in lending capital and have contributed to the growth and development of more than 15 million low-income entrepreneurs, primarily women.

As a consequence of this rapid growth in microlending, the development of best practices and practical tools for managing various lending activities has not always kept pace. This is particularly true for the internal account—a principal distinguishing feature of the village banking methodology. While the internal account represents the key to self-sufficiency for many of the world's poorest, its power and potential depend on the skill with which it is managed.

Material in this toolkit represents the collective experience of the SEEP Poverty Lending Working Group and their village banking programs in creating and managing internal account funds. Catholic Relief Services and the SEEP Network hope that this toolkit provides valuable insight into policies and practices for effective internal account management—and that it will stimulate the development of similar practical field tools that support and enhance the practice of village banking.

Audience

The *Internal Account Management Toolkit* is designed for agency practitioners who work with internal accounts. It provides guidance and practical tools for your use in developing, overseeing and auditing the internal account programs of the village banks you manage. It also includes tools that you can provide to bank members who can then use them in managing their internal accounts.

To effectively train village bank members in internal account management, your agency staff must first have an understanding and appreciation of the issues, policies and practices involved. This toolkit includes a series of lessons—also targeted to agency personnel—to provide training in internal account management, as well as in the use of the various tools. You can use these same lessons to train village bank members in internal account management.

All of the materials in this toolkit assume that you are generally familiar with the fundamentals of village banking. If you wish to review the village banking methodology and the state of the practice, please refer to *Village Banking* by John and Mimi Hatch, 1989, and *Village Banking, the State of the Practice,* Nelson *et al.,* 1996.

Conventions

The toolkit incorporates a number of naming and labeling conventions.

The use of the abbreviated form "bank" always refers to a village bank. Similarly "bank member" or simply "member" refers to a member of a village bank. In order to avoid potential confusion, any references to commercial banks or other formal financial institutions are clearly distinguished wherever they appear in this document.

This toolkit includes more than 50 tools necessary to the practice of village banking. They include both of the following:

- *functional tools* that practitioners and bank members routinely use in managing their internal accounts, and
- *educational tools* that inform agency staff and bank members about village banking concepts or the use of functional tools.

Each tool in the toolkit represents a basic element or building block designed to address a single policy or practice—a loan contract form or a savings exercise, for example.

Because many of these tools address a similar function or process within the village bank, they are aggregated into "tool sets," such as payment records, disbursement records, agency audits, internal controls, and savings practices, which consist of two or more tools. In practice, you can combine and repackage the basic tools in any way you wish. (Refer to the introduction to Section Two for additional information on tools, tool types and tool sets.)

Organization of the Toolkit

The *Internal Account Management Toolkit* is organized into two sections: a policy manual and the toolkit itself.

Section One: Policy Manual

The policy manual defines the internal account and provides insight into its management and operation. It includes the following chapters:

- "Chapter 1: Overview of the Internal Account" defines a village bank's internal account and external account, outlines the objectives of the internal account, and compares the historical role of the internal account with its current role in microlending;

- "Chapter 2: Strategic Relationships and Decision-making Authority" discusses the division of decision-making authority between your agency and its village banks, and the contributions of implementing agencies and formal financial institutions to village bank operations;

- "Chapter 3: Policy-making Guide for the Internal Account" outlines the various policy options available to your agency and its village banks in managing the bank's internal account, and includes recommendations where appropriate.

Section Two: Toolkit

The second section provides more than 50 tools—forms and instructions, checklists, discussion guides, exercises, analyses and diagnostics, and lessons—in 19 tool sets for use in managing your village banks' internal accounts. The tools can also be used in training agency staff and bank members on internal account issues.

This toolkit categorizes tool sets according to overview, lending, savings, recordkeeping, and audit policies and practices, as listed below. (Refer to Summary of Tools in the introduction for Section Two for a detailed list of tools. The tools are also identified in the table of contents and the index.)

Overview of Internal Account Management tool sets:

- Managing the Internal Account, an Overview
- Using the *Internal Account Management Toolkit*

Lending Policies and Practices tool sets:

- Lending Strategies and Safeguards
- Lending Practices and Loan Terms in the Bylaws
- Loan Analysis and Approval
- Delinquency and Collection
- Managing the Cash Reserve

Savings Policies and Practices tool sets:

- Savings Practices

Recordkeeping Policies and Practices tool sets:

- Keeping Records for the Internal Account, an Overview
- Lending Documents
- Loan Disbursement Records
- Payment Records
- Dividend Records
- Cash Flow
- Financial Status Bar Chart

Audit and Internal Control Policies and Practices tool sets:

- Internal Controls
- Agency Audits
- Agency Mini-audits
- Bank Member Audits

An appendix provides a suggested agenda for a five-day training seminar on internal account management that is designed for agency staff. Using this agenda, your agency can sponsor a training of trainers workshop based on the tools in this toolkit plus experiential field training.

Finally, the manual includes a glossary and an index.

How to Use this Toolkit

The *Internal Account Management Toolkit* is designed to provide you with *all* of the resources you require to develop or enhance your agency's village banking program, train your staff, train your village banks' management committees and members, and manage and audit your village banks' internal accounts.

For each of these activities you can select from among the toolkit's policy discussions and functional and educational tools to build your own unique solution. (Refer to the introduction to Section Two for additional information on tools, tool types and tool sets.)

As a starting point, the following chart is designed to help you build or adapt a set of tools for a specific activity from among the resources in the toolkit:

Activity / Objective	Suggested Procedures and Tools
Review industry best practices for the internal account	Read "Chapter 3: Policy-making Guide." Review the recommendations included as part of the Internal Account Diagnostic Tool.
Identify all available tools and tool sets relevant to an internal account management policy area or category	Review Figure 15: Summary of Tool Sets and Tools in the Introduction to Section Two of the toolkit for a comprehensive listing of all tool sets and tools. Review "Chapter 3: Policy-making Guide" and note the tools and tool sets listed with each policy section. Review the tool sets identified for each policy issue as part of the Internal Account Diagnostic Tool. Refer to the Index and review entries for the following key words: lending policies, savings policies, recordkeeping policies, audit policies (or another key word to identify a specific policy area).
Locate a specific tool or tool set	Refer to the Table of Contents to review a complete list of all the tools and tool sets provided in Section Two, organized by major category. Refer to the Index and review entries for the following key words: tool, tools, lesson, lending policies, savings policies, recordkeeping policies, audit policies (or another key word to identify a specific tool or topic).

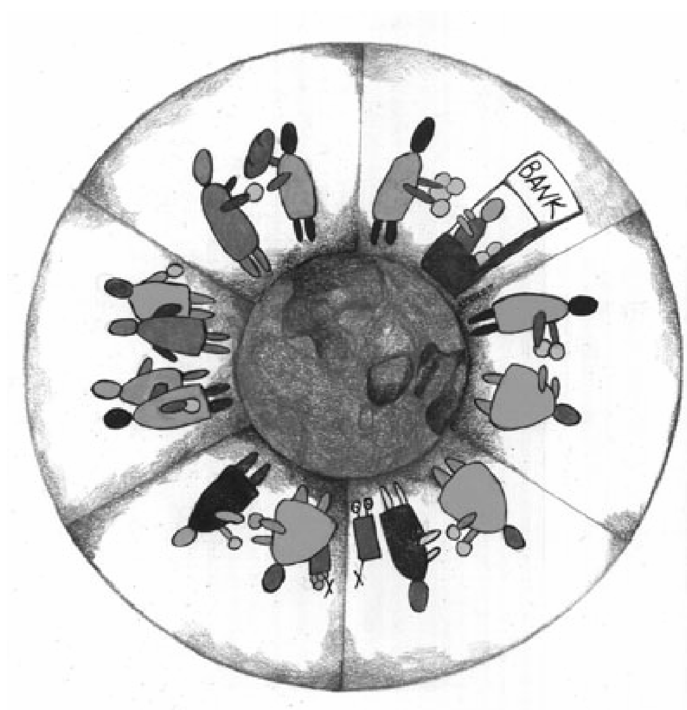
Develop and implement a process to train your agency's *training* personnel on using this toolkit	Your training personnel use the same lessons and tools to learn the components of this toolkit, as they will use to train others in internal account management. Ask your training personnel to read the Training Seminar Materials appendix and review the sample agenda for a five-day seminar on internal account management. This sample agenda includes all of the lessons in the toolkit. Your training staff should carefully review the elements of each lesson, including the related forms, sample data and the solutions to sample problems. Similarly, your staff should review all of the supplemental training tools (discussion guides and exercises) from the toolkit. Individually or in a group, ask your training staff to practice using each of the lessons and other training tools until they are sufficiently familiar with them that they can present them to others.
Design and conduct your own internal account seminars for your agency's staff members or the management committee and members of a village bank	Your training personnel develop seminars for your agency by leveraging their own experiences in learning the tools in this toolkit. Using the sample agenda in the Training Seminar Materials appendix as a starting point, they can adapt the seminar components to suit the needs of village banks in your region: • Eliminate unnecessary tools and lessons. • Add educational tools (discussion guides and exercises) where appropriate to supplement the lessons. • Adapt the examples and sample problems. • Refine the order of presentation of the individual sessions and the seminar schedule as necessary.

Develop a set of standard bylaw terms and policies for your agency's village banking program	Review the "Lending Policies and Practices" section of "Chapter 3: Policy-making Guide" and note the tools and tool sets listed with each policy section. Review the tools in the tool set "Lending Practices and Loan Terms in the Bylaws." If your agency has standard policies that you require to be incorporated into the village bank bylaws, include these requirements on the blank forms of the Bylaw Decision Tool. Also review the tools in the tool set "Loan Analysis and Approval." Adapt the tools as necessary.
Guide a new village bank in developing and implementing bylaws, and other policies and procedures to govern its operations	Incorporating the standard bylaw terms and policies you developed for your agency immediately above, present the appropriate lessons in the tool sets "Lending Practices and Loan Terms in the Bylaws" and "Loan Analysis and Approval."
Develop a set of standard internal account loan documents for your agency's village banking program	Review the "Loan Documents" section of "Recordkeeping Policies and Practices" in "Chapter 3: Policy-making Guide" and note the tools and tool sets listed with each policy area. Also review the "Loan Guarantees" section of "Lending Policies and Practices." Review the tools in the tool set "Lending Documents." Adapt the tools as necessary.
Guide a new village bank in implementing the use of your standard internal account loan documents	Incorporating the standard documents you developed for your agency immediately above, present the appropriate lessons in the tool set "Lending Documents."

Develop a set of standard internal account recordkeeping tools for your agency's village banking program	Review the "Recordkeeping Policies and Practices" section in "Chapter 3: Policy-making Guide" and note the tools and tool sets listed with each policy area. Review the tools in the tool sets "Loan Disbursement Records," "Payment Records," "Dividend Records," "Cash Flow" and "Financial Status Bar Chart." Also review the "Internal Controls" tool set. Adapt the tools as necessary.
Guide a new village bank in implementing the use of your standard recordkeeping tools	Incorporating the standard record set you developed for your agency immediately above, present the appropriate lessons in the tool sets "Loan Disbursement Records," "Payment Records," "Dividend Records," "Cash Flow," "Financial Status Bar Chart" and "Internal Controls."
Develop a standard internal account audit program for your agency	Review the "Agency Audits" section of "Internal Control and Audit Policies and Practices" in "Chapter 3: Policy-making Guide," and note the tools and tool sets listed with each policy area. Review the tools in the tool sets "Agency Audits" and "Agency Mini-audits." Adapt the tools as necessary.
Audit a village bank	Based upon the standard internal account audit program you developed for your agency immediately above, train your audit staff using the appropriate lessons in the tool sets "Member Audits," "Internal Controls," "Cash Flow" and "Financial Status Bar Chart." Develop an audit plan to schedule the audits after reviewing the materials in the "Agency Audits" section in "Chapter 3: Policy-making Guide." Conduct each audit according to plan using the tools in the tool sets "Agency Audits" and "Agency Mini-audits."

Develop a standard internal audit program for your agency's village banks	Review the "Internal Audits by Bank Members" and "Internal Controls" sections of "Internal Control and Audit Policies and Practices" in "Chapter 3: Policy-making Guide," and note the tools and tool sets listed with each policy area. Review the tools in the tool sets "Member Audits" and "Internal Controls." Also review the tools in the tool sets "Cash Flow" and "Financial Status Bar Chart." Adapt the tools as necessary.
Guide a new village bank in implementing the use of your standard internal audit program	Incorporating the standard internal audit program you developed for your village banks immediately above, present the appropriate lessons in the tool sets "Member Audits," "Internal Controls," "Cash Flow" and "Financial Status Bar Chart."
Conduct a short, single-topic training during a village bank meeting	After selecting a topic, review the available lessons and other education tools available to you using the Table of Contents or the Index (key word of "tool").

Section One: Policy Manual



Chapter 1: Overview of the Internal Account

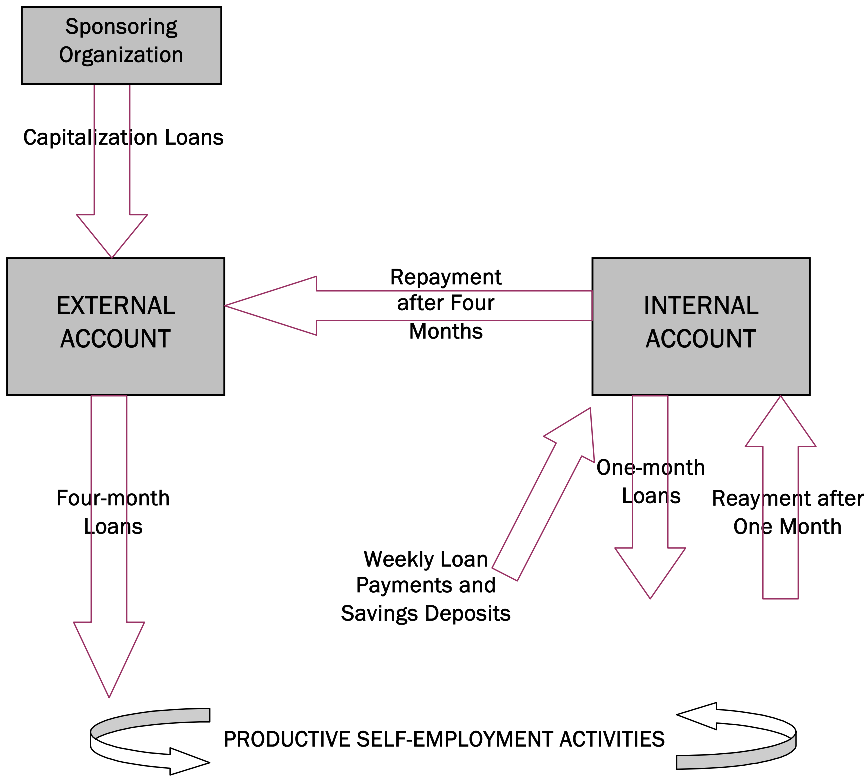
Many village bank funds include both an external account and an internal account.

- The external account consists of funds borrowed from the implementing agency and, generally, member repayments that are deposited with the village bank until they are repaid to the lending agency;

- The internal account consists of funds owned by the village bank and bank members (savings, fees, fines and other earnings). Some village banks also include bank member repayments on external account debt until such time as these borrowed funds are repaid to the implementing agency.

Figure 1 illustrates the mechanics of the internal account and its relationship to the external account.

Figure 1: The External and Internal Accounts of a Village Bank



Characteristics of the External Account	*Characteristics of the Internal Account*
Funds loaned by the sponsoring organization	Member savings Other self-generated income External Account loan payments (temporary) for one to four months
Interest on External Account loans accrues exclusively to the sponsoring organization	Interest on Internal Account loans accrues exclusively to the village bank

Structure of a Village Bank's Internal Account

The relationship between internal and external accounts distinguishes village banking from many microfinance solidarity-group or group-guarantee lending methodologies. It offers members an opportunity to save and accumulate assets; and is a key element of self-sufficiency of the members.

Ultimately, each village bank's vision dictates the bank's internal account management policies and fosters practices that enhance the vision.

Internal Account Components

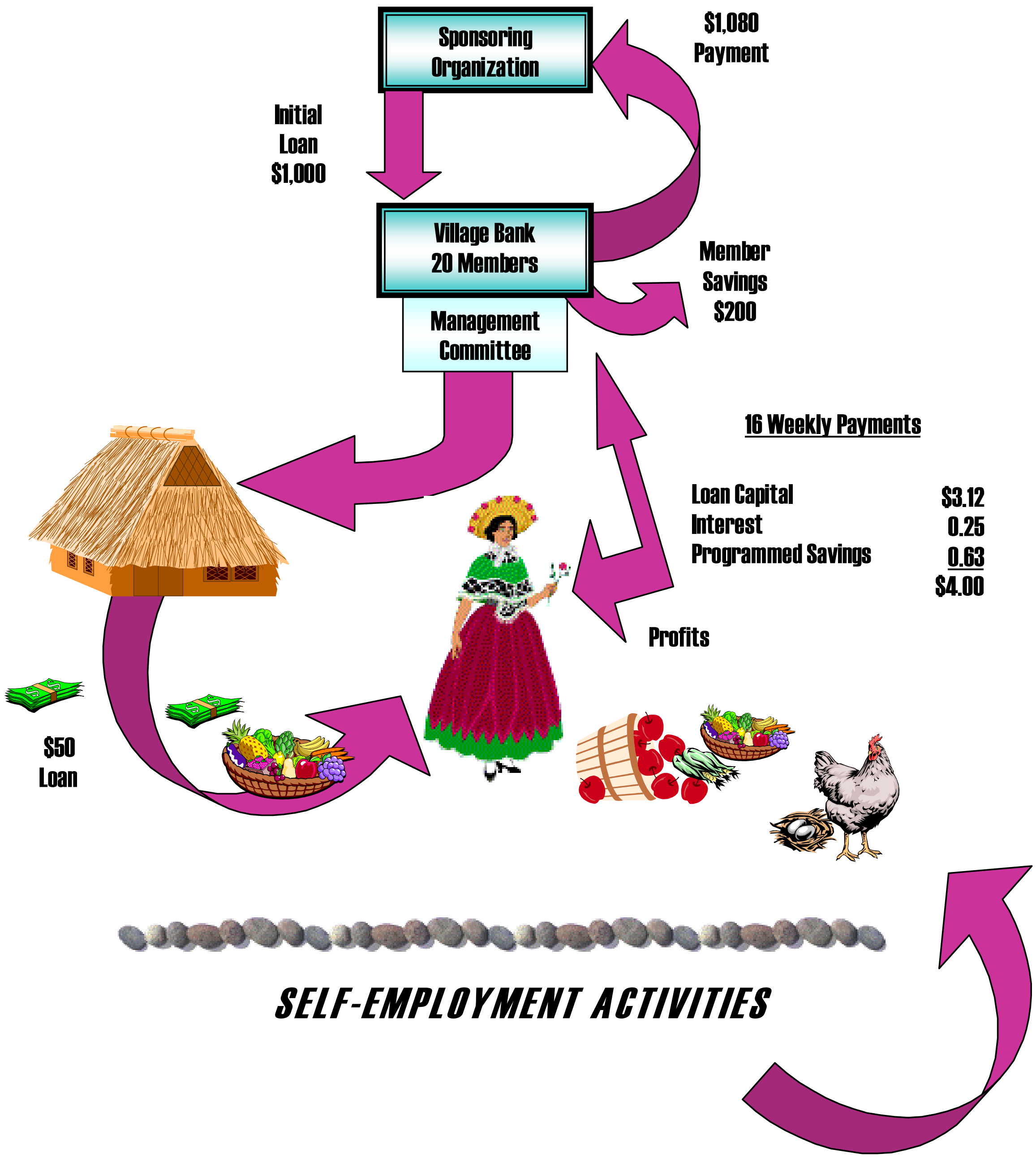
Generally, a village bank's internal account includes funds from the following sources:

- *savings* of bank member borrowers and nonborrower savers,
- *interest income* generated from lending savings to members and nonmembers,
- *fees and fines* levied by the village bank,
- *additional income* generated from bank investments or other activities.

A village bank's internal account might also include *external account payments* made by bank members on loans that are not yet due from the village bank to its lender. (Often, members make payments to the village bank more frequently than the bank is required to repay the external account lender, perhaps weekly on a monthly external account loan.) This practice creates additional risk and, therefore, is not recommended for all village banking programs.

In most programs, savings make up the vast majority of internal account funds.

Figure 2: How a Village Bank Works



Internal Account Mobilization

Each village bank is entrusted to manage savings and other internal account funds according to guidelines established by the bank's members. Use of bank funds for investment or lending purposes is referred to as *internal account mobilization*.

Income earned by a village bank from internal account mobilization is added to the members' internal account fund and contributes to the village bank's equity. Banks on-lend these funds, distribute dividends and pay for such expenses as supplies, management committee fees, transportation and commercial bank account charges.

Some village banks also use their members' external account loan payments for internal account lending. These internal account loans must be repaid before the bank's external account loan payment is due. Such a practice greatly increases the bank's lending potential and the interest income for village bank members. However, mobilizing external account payments in this manner does involve additional risk and, therefore, is not uniformly adopted by all village banking programs.

Role of the Internal Account

Historically, there have been four principal objectives for the internal account:

- to provide an *additional loan fund*, owned and operated by bank members. The fund provides loans to supplement the external account borrowing including loans for consumption and additional working capital, loans of shorter or longer duration than those available from the external account, and loans to nonmembers. This fund also covers emergency needs of the members;

- to encourage *assets and capital accumulation* at the village bank and individual member levels in order to eventually reduce or eliminate the need for external account lending. This releases external account funds for use by other individuals and communities;

- to promote *empowerment of, and solidarity among, members* through the mobilization and control of monetary resources;

- to develop *financial and business skills* of members through training through self-management of resources at the village bank and member-business levels.

In current practice, the first objective of internal account management has proven to be the most important. Banks pursue the other objectives with varied levels of interest.

Provide Additional Loan Funds

Village banks that encourage internal account lending consider the practice a positive service that they can offer to their members and, in some cases, to the wider community. Internal account funds supplement working capital and provide a source of funds for specific consumption or emergencies.

Internal account lending policies, loan amounts, and conditions run the gamut from tight control to complete access to funds.

Lending remains the most popular use of internal account funds for the following reasons:

- member savers earn a high return on their savings in the form of interest and/or dividends,
- the community has access to working capital not otherwise available,
- member savings are secured against theft—which is particularly important in countries where no formal banking organizations are available.

This objective also generates income for bank members and safeguards their savings.

Accumulate Assets

Replacing external account loan capital with accumulated savings (internal account funds) was once an important goal of internal account management. Asset accumulation is encouraged on an individual basis, where members save for future security. Savings incentives usually relate to increased loan size or higher returns in the form of dividends.

Today, agencies are likely to maintain village banks as long-term clients, eliminating any need for the internal account to replace the external account. Agencies encourage—and usually require—savings as a source of long-term funding. Savings provide members with an asset base and provide the village bank with a source of funds for possible future transition into a deposit-taking financial intermediary. Member savings in the internal account also represent a form of collateral for the village bank and the agency. If a member cannot make her external account loan repayment, she may have the option of borrowing from her savings. Finally, a strong savings base generally translates into program sustainability for the agency, in part, because of the reduction in risk to the external account.

This is vastly different from the original savings model, where savings *replaced* agency funds as a source of capital for the village bank. In fact, there is a trend away from the *graduation* concept for village banks. (Graduation is that point at which a village bank has accumulated sufficient assets or working capital to no longer require borrowed funds.)

There are several reasons for this trend away from village bank graduation:

- Many village banks do not achieve the savings goals described in the original village banking model. Therefore, they are not able to satisfy the loan requirements of their members without agency funds;

- Often, village bank members prefer not to manage their own autonomous banks; they are too busy or insufficiently skilled to assume the additional responsibility. They prefer to receive continued financial services from the agency;

- Agencies require a sustainable source of income to cover the costs of organizing village banks, training their members and providing ongoing financial and management services. Interest income from external account loans provides such a dependable income stream to cover the agency's operational and financial expenses.

There is, however, a need for a mechanism to graduate bank members whose financial requirements are no longer met by the village bank. To serve these persons, the agency should either develop alternative loan products or transition the members to institutions that provide the required financial services.

Empower Members and Foster Solidarity

Instilling a sense of empowerment and solidarity among members is a strong motivating factor in internal account management. The internal account plays a special role in creating feelings of ownership and responsibility among members charged with managing these group funds.

However, many agencies find it difficult to balance policies that engender empowerment with those that provide necessary internal controls. In actual practice, success depends in large part on the implementing agency's level of control and the village bank's management capacity.

Each agency's vision dictates the relative emphasis it places on empowerment versus security concerns. While some believe that a highly developed sense of ownership and empowerment is the best defense against mismanagement, this practice cannot guard against fraud perpetrated by a committee member or an agency staff member. Security policies require training programs in sound financial decision-making, auditing practices and audit follow-up.

Develop Financial and Business Skills

Capacity building remains a major objective of internal account management and, as noted in the previous section, is a prerequisite to empowerment and solidarity. However, most internal account capacity building has been of the *learn by doing* variety. Most agencies have focused resources on business-skill development and village banking operations as they relate to the *external* account.

Internal account methodologies, policies and procedures have not evolved at the same rate as those for the external account. Internal account training and capacity building—if any—often consist of no more than agency-mandated policies that are based on a village bank's original bylaws. Bank members and management rarely have an opportunity to create policies and the agency rarely follows up on implementation. This is a result of the fact that materials to develop financial and business skills for the internal account simply did not exist, until now.

Effect of Bank Lifecycle on Internal Account Management

The relative importance of the internal account, and the policies and practices required to manage it, vary over the life of a village bank.

The lifecycle of a village bank consists of three distinct phases—*honeymoon*, *counseled* and *mature*. The tools in this toolkit address internal account management issues that arise during all three phases of village bank development.

Honeymoon Phase

The *honeymoon* phase usually extends from the period during which the group is formed through the end of the third cycle. Characteristics common to this phase include the following: groups learn the mechanics of village banking, individual loan amounts are small and are usually repaid on time, all savings are deposited as required, and the internal account balance is modest.

Your promoters must dedicate significant time to the village bank to assist in establishing controls and guidelines the group will apply throughout this phase. However, you will find it relatively easy to monitor internal account lending if, in fact, the bank issues loans during this phase.

Counseled Phase

The *counseled* phase, where problems most commonly arise, extends from the beginning of cycle four through the end of cycle seven. During this phase, turnover in group membership or reassignment of promoters creates new dynamics within the group. The complexity of recordkeeping increases due to the increased number of internal account loans, distribution of dividends, and early withdrawal of savings. Delinquency and defaults may increase as loan sizes grow or as new members with less experience begin to borrow.

This phase is critical to the long-term development of a village bank. It is essential that your promoters provide assistance to the bank in developing procedures and adapting policies to reflect changes, establish recordkeeping capacity and continue to provide ongoing education for group members.

Mature Phase

The *mature* phase generally begins with cycle eight, but the start of this phase depends in large part on how well the bank manages its operations during the two previous phases.

If members receive training in solidarity, asset management, recordkeeping, loan approval, dividend policies, risk analysis and auditing during the initial phases, they should be able to manage the internal account by the start of the mature phase. Your promoters can concentrate on auditing and monitoring activities at this point.

Without sufficient training and supervision, however, bank members are susceptible to fraud perpetrated by other members or by promoters. After such an experience, an agency may respond by exerting increased control over savings and the internal account. Members then may be unwilling or unable to self-manage and may continue to depend heavily on agency support. This can result in added cost to the agency and, in some cases, lead to a decision to eliminate lending from the internal account altogether. Alternatively, the agency may allow the internal account to continue but provide little or no supervision, thereby increasing risk in both the external and internal account. Without guidance, members may use internal account savings to make delinquent external account payments, lend to high-risk borrowers or fail to notice instances of fraud.

Lesson 1: Managing the Internal Account, provides a useful handout for understanding and analyzing types of village banks.

Chapter 2: Strategic Relationships and Decision-making Authority

Two organizations can play a significant role in the operation of a village bank's internal account: the bank's implementing agency and the formal financial institution (if any) with which it maintains a banking relationship.

The Role of the Implementing Agency

The agency's role in internal account management is often one of two extremes, depending on the degree of mobilization of the internal account and the financial sophistication of the agency's overall banking program. Some agencies impose few policies on the village bank and provide minimal oversight, while others maintain extremely tight control over activities in the bank's internal account.

Roles most often seen in internal account mobilization are:

- *Tight agency control,* wherein the agency develops strict internal account control policies limiting bank members' access to the internal account. This approach has the advantage of lowering or eliminating risk. On the other hand, if these controls are too prohibitive, members earn negative returns on required savings when they are prohibited from on-lending their funds, and opportunities for exercising self-management and solidarity are diminished;

- *Little or no agency control,* wherein the internal account is introduced without substantive monitoring by the implementing agency. While some banks may choose to mobilize their internal account funds under these circumstances, they only have bylaws or traditional lending practices as a guide. The lack of supervision can result in unsound financial practices within the bank, placing the implementing program's external account portfolio at risk;

- *Little or no mobilization,* wherein the internal account is considered to be a vehicle for member savings, rather than a loan fund. Members benefit from complete access to savings. However, there is little or no oversight of internal account lending and self-management skills, and solidarity among members is poorly developed. Moreover, savings are discouraged and, therefore, produce low or nonexistent returns to savers; or

- *Internal account funds are deposited in a formal financial institution.*

Decision-making Authority over Lending Policies: Bank versus Agency

Ultimately, when developing its internal account policies, every agency must balance its objectives with those of the village bank. While retaining decision-making authority at the agency level can reduce risk, authority delegated to the bank promotes a sense of empowerment and encourages the development of management capacity.

Most internal account lending programs use a mixture of policies imposed by the agency with procedural decisions made at the village bank level—as the matrix in Figure 3 illustrates. This matrix indicates whether the agency or village bank is most often responsible for decision-making in each policy area, along with the reasons.

Figure 3: Matrix of Decision-making Authority for Internal Accounts

Issue	Agency Decides	Comment	Bank Decides	Comment
Lending Policies and Practices				
Lending				
Initiation (when to start lending)	4	Agency often standardizes for ease of overall program management and training schedules.	4	Unless no formal financial institution is available, village banks often prefer to postpone internal account lending until adequate funds area accumulated. If imposed waiting period is too long, earnings may be less than desired and sense of ownership decreases.
Eligibility		Agency often provides guidance during bylaws training with regard to eligibility criteria.	4	Bank most often decides what criteria should be used to select borrowers for internal account loans.
Duration	4	Agency usually requires end of cycle as maximum duration.		Banks have flexibility within agency guidelines.
Interest		Agency may monitor to discourage banks from charging usurious or negative rates. Training is advised, but standardizing rates is unrealistic as economies differ drastically.	4	Members decide rates based on local economy, membership status, purpose of loan, length, amount and overall risk. The practice increases members' financial management skills, ownership and return.

Issue	Agency Decides	Comment	Bank Decides	Comment
Repayment Schedule		Agency may need to provide training in credit analysis.	4	Bank decides frequency based on purpose of loan and borrower's financial situation, which is best known by members. Provides opportunity for financial management and achieving social objectives of internal account.
Amount	4	Agency often provides general guidelines (such as ratios and loan caps), which require more monitoring; or agency may leave decision to village bank entirely with no restrictions; but agency should provide adequate credit analysis training in either case.	4	Within parameters, bank members decide on loan levels based on knowledge of borrower and loan purpose; banks may divide funds equally according to need or make several large loans. In either case, credit analysis training is advised.
Guarantees		Agency often requires guarantees for larger loans. Decision is generally made by bank with training in credit analysis by agency.	4	Banks often impose physical collateral or personal guarantees. Agency guidelines may influence guarantee policy but should not impose a policy as it hinders financial self-management and group responsibility for loans.
Loan Analysis and Approval		Agency often informed but is not part of decision. Agency helps in monitoring internal account to assess risk and training needs. Credit appraisal training is an important agency task.	4	Banks should have ultimate decision in all loan approvals (within certain agency-imposed guidelines). Otherwise, members' decreased motivation may reduce ownership, responsibility and general interest in internal account lending.
Delinquency and Collection		Agency provides guidance and training on techniques for controlling and eliminating delinquency and in effectively collecting loans past due.	4	Banks establish guidelines in bylaws indicating procedures to follow in cases of delinquency and specify collection procedures in cases of default.

Issue	Agency Decides	Comment	Bank Decides	Comment
Cash Reserves	4	Agency usually has guidelines or specific requirements that consider the status of external and internal account repayments and provide a standard to strengthen overall portfolio and safeguard savings.		Banks vary on this issue. An externally imposed rate may unduly inhibit internal account mobilization if bank is performing well. However, this may be justified for overall portfolio quality. High reserve policies may result in negative returns due to inflation. Low reserve policies may put savings or external account at risk.
Savings Policies and Practices		Agency may influence bank decisions or guidelines on accessibility to savings in order to decrease risk on external account and maintain minimum levels of savings. Although policies are generally decided by bank, training by agency in the importance of saving should be provided.	4	Bank normally decides the conditions under which savings may be withdrawn and the frequency of withdrawals. If agency imposes restrictions on savings, bank members may save at lower rates knowing they have limited access to their funds.
Recordkeeping Policies and Practices		Agency usually standardizes internal account records for audit and overall monitoring purposes.		Forms and systems should be geared to enhance information gathering and promote bank self-management without outside assistance.
Lending Documents	4	Agency requires uniform credit applications and contracts. Documentation formalizes loan and audit trail.	4	Formal contracts usually are not imposed by bank, since they may be difficult and/or time consuming for less literate borrowers to complete.
Disbursement Documents		Agency works with bank to develop streamlined disbursement recordkeeping practices.	4	Bank may find documentation of internal account disbursements difficult unless it receives sufficient agency orientation. Forms require significant application of human resources.

Issue	Agency Decides	Comment	Bank Decides	Comment
Payment Documents		Agency works with bank to develop streamlined repayment recordkeeping process.	4	Bank may find documentation of internal account repayments difficult unless it receives sufficient agency orientation. Forms require significant application of human resources.
Dividend Practices				
Calculation	4	Often standardized formulas are introduced to facilitate audit and insure fair distribution. Agency should encourage calculation at bank level to stimulate village bank self-management.	4	Members may find imposed formulas complex or have a preferred calculation system. Agency should promote simple calculations that work for the group.
Distribution		Distribution encouraged by agency to promote increased membership, provide return to savers and reduce nonperforming equity. Agency should provide thorough training.	4	Banks usually decide if they wish to distribute dividends. While distribution is recommended, some banks opt to build group equity for other purposes. This is part of an investment strategy and should be left to the village bank.
Financial Reports	4	Agency may impose requirements for cash flow and use of tools such as the financial status bar chart.		Banks may ignore reports if they are too complex to prepare or the reason for producing them is not well understood.

Issue	Agency Decides	Comment	Bank Decides	Comment
Internal Control and Audit Policies and Practices				
Internal Controls	4	Agency may impose basic controls (such as dual signatures, separation of duties, transactions restricted to meeting dates). Basic financial controls should be introduced to bank and be monitored. If controls are required, an enforcement mechanism is needed. Agency may restrict access to loans or impose penalties as an additional control mechanism.	4	Bank often has its own control techniques in addition to agency controls (such as verbal reporting, spot checking by members). Banks may ignore controls if they are too complex or the rationale is not well understood.
Agency Audits	4	Agency establishes schedule, tools and criteria for bank.		Bank may request agency audit of internal account activities; however, this is not a common practice.
Internal (Bank Member) Audits		Training in conducting internal audits is recommended.	4	Bank should set internal audit policy to check on agency and management committee. Tools should be used at bank level and require minimal promoter assistance.

This toolkit describes those policy options that foster sound internal account management while providing for security, access and return of member savings, minimal risk to the external account, and a strong sense of solidarity and empowerment among members.

"Chapter 3: Policy-making Guide for the Internal Account" discusses recommended or best practices for each of the policies in the summary above. These recommendations are based on an in-depth understanding of current internal account practices combined with the experiences of a number of implementing agencies around the world. Ultimately, your agency must decide which policies and practices are best suited for your own unique culture, lending environment and clientele.

Impact of Internal Account Lending on Sustainability of the Agency's Program

Some agencies view internal account lending as competition for their external account loans, thus reducing the sustainability of their village banking programs.

While the internal account rarely replaces the external account, it can reduce the demand for external account loans significantly once a bank accumulates sufficient funds to satisfy member needs.

In general, your agency may have little financial incentive to promote internal account lending as the interest income on these loans accrues to the village bank and the availability of these loans can detract from external account borrowing—further reducing your revenues. In addition, the burdens these loans impose on your agency in terms of developing appropriate lending policies and practices, training members in their use, and monitoring loan activity is costly and time-consuming. Internal account lending, because of the resultant possibility of over-borrowing by bank members, can also increase risk in your external account loan portfolio.

On the other hand, internal account mobilization provides the community with a tangible increase in lending capital that is managed according to the needs of the members and the community. Many argue that participation in a bank promotes empowerment and the authority to make informed decisions regarding the group and that individual equity is a powerful skill and confidence builder. External account lending does not provide this same hands-on experience, since your agency dictates policy and the village bank acts more as a collection agency.

Competition created by internal account lending can pressure agencies to improve services and make these services less costly to the bank member customer.

In establishing your agency's policy regarding internal account lending, you balance your need to provide quality, sustainable financial services with the bank's need to develop capacity and equity.

You can adopt the following policies to minimize the time you spend managing internal account lending programs and to maximize the return to both your agency and the village bank:

- *increase the competitiveness of external account loans.* As your agency achieves economies of scale and improves its own management systems, you should be able to reduce interest rates to remain competitive. You can also offer additional loan products designed to meet the needs of specific members or the community in general, thus increasing the demand for your external account loans;

- *increase the village bank's initial training in internal account management.* Agencies can decrease the amount of promoter services a bank requires by providing banks with thorough and systematic training on all aspects of internal account management, including loan approval, recordkeeping, dividends and internal controls. Ongoing training assumes that high turnover for key individuals will be kept at a minimum;

- *charge fees for agency services.* Many agencies charge their village banks a fee for promoter services related to the internal account portfolio;

- *split interest income in return for agency services.* Some agencies receive a portion of the village bank's internal account revenue in return for promoter services and oversight. This option requires thorough discussion by both parties before it is implemented, since it may be more appealing to the agency than to a village bank that prefers autonomy.

Internal Account Lending and Program Sustainability - The CRECER Experience

Freedom from Hunger's Bolivian partner, CRECER, has witnessed very active internal account lending because of flexible internal account lending policies, active promotion of internal account borrowing, and the absence of formal deposit-taking institutions in many of the very rural regions serviced by the agency. Although internal account loans carry higher interest rates than external account loans, dividends on earnings from these loans are distributed regularly at the end of each loan cycle. This practice lowers the effective interest rate for bank members and provides a strong incentive for borrowing.

CRECER has experienced competition between external account and internal account lending; in some of its village banks, internal account lending has outpaced external account lending. Although these village banks still require promoter assistance and other services from the agency, CRECER's interest income to fund the services has declined. As a result, the internal account had the potential to threaten CRECER's institutional viability.

Despite this threat, CRECER has experienced rapid growth—reaching nearly 13,000 borrowers with full operating self-sufficiency for the last six months of 1998. One reason is that the internal account provides CRECER with a competitive edge over other rural lending institutions in Bolivia. Borrowers are attracted by the opportunity to earn high returns on savings and loan repayment installments. Also, CRECER charges a sufficiently high interest rate on external account loans to recover costs.

Significantly, CRECER's internal auditors discovered that village banks with exceptionally high demand for internal account loans were charging a lower interest rate than was being charged for external account loans. This is contrary to CRECER's credit policy manual, which stipulates that the interest rate on the internal account loan fund must be equal to or greater than the external account interest rate. This policy was enforced and the problem was corrected.

Finally, CRECER has instituted stricter requirements that limit the use of external account loan repayments for internal account lending. The newest policy requires village banks in peri-urban areas—those with access to formal financial institutions—to deposit loan repayments in an account with a financial institution.

The Role of a Formal Financial Institution

In many areas of the world, formal financial institutions—such as credit unions, development and rural banks, and postal systems—offer village banking and internal account management services. Where financial institutions are available, village banks have the opportunity to safeguard internal account funds in the formal institution and to benefit from passbooks and bank statements provided by these institutions to validate their own accounting records.

In countries or regions that lack sufficient financial institution infrastructure, village banks must take full responsibility for securing and safeguarding bank funds.

Partnering with a Formal Financial Institution

Partnering between a village bank and a formal financial institution (generally a credit union or rural bank) often assumes one of the following two forms:

- The *agency* offers village banking services but, because of legal restrictions, the financial institution manages village bank deposits. Under this scenario, your agency encourages its village banks to open deposit accounts with formal financial institutions for the bank's external account loan repayments, member savings, earnings and cash reserves;

- The *financial institution* offers village banking services and manages village bank deposits. Under this scenario, your village banks are required to maintain accounts with the financial institution for regular deposits of loan repayments, member savings, and other internal account funds.

In either case, all transactions are conducted between the institution and representatives of the village bank—not individual bank members.

The primary motivations for village banks to maintain all or a substantial portion of their internal funds in a formal financial institution are the following:

- increased security,
- regular access to savings,
- the opportunity to maintain regular and/or term deposit accounts with institutions that have established sound financial practices.

From the institution's perspective, regular deposits of village bank funds (such as external account loan repayments) contribute to the development of long-term, sustainable services. The funds appear as savings on the institution's balance sheet and have a positive effect on its cash flow. If the institution itself offers village banking services, carefully managed internal account lending programs increase village bank and member assets and make the institution's deposit services even more necessary.

However, it is important to understand that partnering with a formal financial institution can restrict a village bank's internal account management options—primarily because risk management is a major concern for these institutions. In addition, internal account lending can compete with the institution's savings mobilization efforts. As a result, formal financial institutions (especially credit unions) do not encourage internal account lending and often prohibit lending of external account loan repayments. However, some credit unions or rural banks do allow internal lending when a village bank reaches its third or, in some cases sixth, cycle. Others negotiate with village banks to allow internal lending of a portion of the bank's internal account fund.

There are other potential disadvantages for village banks that deposit funds in a formal financial institution. Most often, village banks earn lower returns on savings deposits than on internal account lending. Also, savings accessibility is limited by the distance of the institution from the village bank and the business hours during which the institution operates. Formal financial institutions in fragile economies do sometimes fail, and village banks risk losing funds. Also, some formal financial institutions may offer low or no interest on savings (possibly even a negative return after adjusting for inflation).

Despite the potential drawbacks, village banks may choose to keep their funds in these institutions for the following reasons:

- security is of the utmost importance,
- the village bank has little or no internal account lending activity,
- members do not want the burden of managing large amounts of internal funds,
- village bank members become dedicated members of their credit union and want to build their savings to contribute to credit union growth and the eventual availability of additional credit union services.

Your agency can help to balance the potentially conflicting objectives of village banks (to increase member assets through high-return investments) and formal financial institutions (to maintain viable lending and savings programs). For example, you can encourage financial institutions to provide more attractive savings products for village bank members. One possible method involves evaluating the incentive structures of internal account lending schemes.

Ultimately, a well-managed internal account fund contributes to the financial well being of the village bank and the financial institution.

Unique Challenges where No Institution Is Available

Countries with inadequate financial-institution infrastructure face unique challenges in implementing their village banking programs—particularly in terms of internal account management. Without safe deposit-taking institutions, the following issues arise regarding security, access and return of member savings, as well as managing activity in the internal account portfolio:

- where to keep unabsorbed balances from the internal account,
- how to protect cash balances from inflation,
- how to create audit trails without formal bank statements, and
- how to handle reserves.

Figure 4: World Relief, Cambodia, Safeguards Village Bank Savings

World Relief Cambodia provides an example in which the agency safeguards savings for village banks.

Cambodia has a rudimentary banking infrastructure that is insufficient in many rural areas. Often banks do not accept

Options to Secure Fund Balances and Reserves

Village banks that exist in economies that lack formal financial institutions face unique management challenges. Providing security for savings balances and cash reserves is a key problem. As a result, most agencies do not impose reserve requirements on village banks in such environments.

Possible options for safeguarding internal account funds and cash reserves include the following:

- lending out the entire balance in the internal account to bank members and members of the community, so there is no cash to secure;
- distributing dividends on a regular basis to reduce the cash in the internal account;
- investing internal account funds in fixed assets such as livestock, gold, grain or other inventory;
- entrusting small amounts of the internal account balance to a number of trustworthy bank members or officers;
- relying on the agency to safeguard internal account funds at the agency's office or other secure location.

Lending internal account funds remains the most popular security technique. However, in considering your options, you might weigh the possible advantages of this approach (security and interest income) against the risk of loss due to bad debts. In former Soviet Republic programs such as FINCA/Kyrgyzstan (which operate in an all-cash economy with a high incidence of fraud and failing commercial banks) some village banks divide the internal account funds into many small loans and require guarantors and frequent repayments on these loans to help minimize risk from default.

Alternatively, banks can invest all or part of the internal account in marketable securities. KMBI, Women's Opportunity Fund's partner in the Philippines, regularly invests in commodities to generate a return and provide security. This strategy has the added advantage of serving as a possible hedge against inflation, although it can be cumbersome for both members and the agency to monitor the asset.

In some cultures, it is traditional to entrust a member of the community with the fund balance. Often, the member providing this service earns a fee; however, the practice varies.

Some agencies offer safekeeping services to their bank members, in which case the agency must absorb the risk for both external and internal accounts. In some cases, it is possible to purchase insurance, but this can be costly unless the agency holds significant amounts of cash.

Audit Tools for Internal Account Loans

Village banks operating without access to financial infrastructure also face additional challenges in recordkeeping and auditing. It is more difficult to monitor internal account activity without commercial bank statements and receipts to validate against the village bank's records and account books.

Instead, village banks must devise additional internal controls, which can, in turn, be supported by documentation from the implementing agency. Such internal controls can include the following:

- requiring signatures from both the borrower and a committee member on all internal account loan contracts;
- issuing serially numbered receipts for all loan disbursements and loan repayments, copies of which are kept by both the borrower and the management committee;
- issuing serially numbered receipts for paid-off loans, copies of which are kept by the borrower, management committee and your promoter;
- issuing serially numbered requisitions, signed by the management committee and reviewed by selected bank members, for all items purchased with internal account funds;
- maintaining a cashbook for all transactions (backed by receipts and requisitions) that is signed by the management committee and verified by your promoter or a bank member.

Chapter 3: Policy-making Guide for the Internal Account

This policy-making chapter introduces the original framework developed to guide village bank practices and discusses internal account policy options in four general categories: lending, savings, recordkeeping, and internal controls and audits.

Because the vision of the agency and village bank influences internal account policy, some sections discuss a number of options, along with the rationale behind each. For those cases where clearly defined best practices exist, the discussion includes guidance on implementing the recommended policy.

Original Framework for Policy Evaluation

John Hatch, founder of FINCA International and creator of the original village banking methodology, developed five basic questions (Figure 5) as a framework for designing internal account management guidelines and policies. Today, these questions continue to play a significant role in village bank management.

However, the original internal account guidelines largely left recordkeeping, internal controls and security measures in the hands of the village bank. Each bank created an internal control system (or policy) best suited to its unique situation, skill level, and membership. Thus, the resulting internal account monitoring systems varied from village bank to village bank.

Figure 5: John Hatch's Internal Account Management Questions

Who can borrow from the internal account?

For what purpose can an internal account loan be used?

What are the interest rate and duration of the internal account loan?

What happens in the case of noncompliance by borrowers?

Will the village bank generate dividends, and if so, how?

The implementing agency was not expected to track a village bank's internal account; all such monitoring was left solely to the discretion of the bank.

It was thought that self-management of self-created systems generated a stronger sense of ownership and solidarity among the members and encouraged development of superior management skills.

Over the years, programs for internal account management produced mixed results. Many problems stemmed from variability in policies and systems. The lack of standards made agency audits difficult, if not impossible. Other problems arose from a lack of bank-member training in financial and fund management, financial policy options, and accounting and recordkeeping. This lack of financial sophistication often translated into poor communications, both among members and between the bank and its implementing agency. Insufficient information regarding internal account performance and portfolio status increased the risk of default on external account loans and put member savings in jeopardy.

As a result of these historical experiences, it is no longer considered sound financial management to allow village banks to craft unique policies and systems.

Today's practitioners strive to find ways to ensure that agency policies protect member savings deposits and effectively manage internal and external account debt. Such policies assist village banks in effectively managing funds, empowering individual members and increasing security and return for its members. Yet, they also provide flexibility so that each village bank can mold its practices to suit the unique demands of its community.

Summary of Policy-making Issues

To effectively manage its internal account, a village bank must establish policies and practices governing lending, savings, recordkeeping and auditing activities.

The Internal Account Summary and Diagnostic (Figure 6) categorizes the major internal account management policy issues discussed in this policy manual and summarizes the recommended practices, preparatory steps, decision-making processes and suggested tools that relate to each issue.

This diagnostic is intended as a guide to the components of the toolkit as well as a quick reference for internal account practitioners.

Tool References

Internal Account Diagnostic Tool
Using the Diagnostic to Analyze the Internal Account (Lesson 3)

Figure 6: Internal Account Summary and Diagnostic

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Lending Policies and Practices						
Lending						Managing the Internal Account, an Overview
Initiation (when to start lending)	Initiate internal account lending when bank chooses to do so, after key procedures and bylaws are in place and members are trained.	Conduct bylaw training with members and introduce recommended policies.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws
		Adapt loan terms based on local experience and vote on final policies and procedures.	1 2 3			
		Adopt review and monitoring schedule and procedures.	1 2 3			
Eligibility	Initially, make loans exclusively to members; subsequently, loans can be made to members and nonmembers when internal account fund is sufficiently large.	Conduct bylaw training with members and review procedures for establishing eligibility.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Duration	Loan terms should not exceed the end of the external account loan cycle.	Review recommendations and establish policies and procedures in bylaws after soliciting local input on lending experience and practices.	1 2 3	4		Lending Practices and Loan Terms in the Bylaws
Interest	Flexible interest rate policy is determined by bank, with variations based on loan amount, term, purpose, type, guarantees and collateral; policy should be competitive with local market rates.	Introduce recommended lending terms and establish policies and procedures in bylaws after analyzing local market.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws
Repayment Schedule	Repayment should occur monthly, at a minimum.	Review repayment recommendations in accordance with local practice; incorporate policies and procedures in bylaws.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws
Amount	To minimize risk, no more than 25% of total loan fund should be placed in a single loan.	Introduce concept of risk and incorporate risk control policies in bylaws.	1 2 3	4		Lending Practices and Loan Terms in the Bylaws
		Establish regular review and monitoring process.	1 2 3			
Guarantees	Require collateral if loan amount is large; personal guarantee at discretion of bank members.	Review recommendations and establish policies and procedures in bylaws.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Loan Analysis and Approval	A majority of bank members should approve all internal account loans; additional loans should not be approved for members with existing loans.	Train members in credit and risk analysis; develop loan approval criteria and a loan review process; test criteria and process during initial loan cycles and adjust as necessary.	1 2 3		4	Loan Analysis and Approval Lending Practices and Loan Terms in the Bylaws

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Delinquency and Collection	Establish policies and control procedures aimed at avoiding delinquency. Monitor troubled loans.	Review delinquency and collection recommendations. Train members in monitoring troubled loans, delinquency practices and control, and collection procedures.	1 2 3 1 2 3		4	Delinquency and Collection Lending Practices and Loan Terms in the Bylaws
Cash Reserve	Establish a cash reserve from inception, unless bank has no access to a secure, deposit-taking institution; establish a conservative amount initially, then adjust amount based on performance, management capacity and inflation.	Review management capacity against standard performance indicators and set policy based on indicators. Conduct reserve training, stressing purpose of reserve and management practices. Create procedure to review reserve amount based on portfolio performance.	1 2 3 1 2 3 1 2 3	4		Managing the Cash Reserve

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Savings Policies and Practices						
Savings Practices	Establish programmed (commonly, 20% of external account loan amount) and voluntary savings policies, as well as limitations, if appropriate, on member withdrawals. Caution members from borrowing against savings, allowing exceptions on a case-by-case basis only.	Review recommendations and train members on importance of savings to the internal account and the community. Solicit input from members on access policy. Identify risk by analyzing bank policies for mobilizing savings. Create policy on savings requirements, security and access.	1 2 3 1 2 3 1 2 3 1 2 3		4	Savings Practices

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Recordkeeping Policies and Practices						
Record-keeping Practices	Establish recordkeeping practices that are simple for members to maintain independently, and sufficiently comprehensive to provide required data for effective management by agency and bank.	Review recommendations, documents and recordkeeping procedures with members.	1 2 3	4	4	Keeping Records for the Internal Account, an Overview
		Adjust policies to fit member capacity.	1 2 3			
		Train members in recordkeeping practices.	1 2 3			
		Open commercial bank account, if possible.	1 2 3			
Lending Documents	Loan applications (for particularly significant or nonmember loans), loan contract with payment schedule, guarantee or collateral forms.	Review documents and practice procedures for their use and implementation at bank level.	1 2 3	4	4	Lending Documents
		Establish recordkeeping review and monitoring procedures.	1 2 3			

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	Recommendation	Preparatory Steps		Agency	Bank	Tool Set(s)
Disbursement Documents	Passbook for borrower; loan disbursement summary form for bank.	Review documents and practice procedures for their use and implementation at bank level.	1 2 3	4	4	Loan Disbursement Records
		Establish recordkeeping review and monitoring procedures.	1 2 3			
Payment Documents	Passbook for borrower, individual internal account loan records and payment activity summary for the bank.	Review documents and practice procedures for their use and implementation at bank level.	1 2 3	4	4	Payment Records
		Establish recordkeeping review and monitoring procedures.	1 2 3			
Dividends	Base dividend calculations on beginning-of-cycle savings amount to create a savings incentive.	Train members on purpose of dividends and recommended practices.	1 2 3	4		Dividend Records
	Disburse dividends at the end of each cycle to simplify management and provide frequent returns for bank members.	Review dividend forms and ask members to calculate distribution to test understanding and capabilities. Adjust practices as necessary.	1 2 3			

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Financial Reports	Produce a cash flow and a financial status bar chart at the end of each bank meeting.	Train members to prepare a cash flow statement. Train members to prepare a bar chart.	1 2 3 1 2 3	4		Cash Flow Financial Status Bar Chart
Internal Controls and Audit Policies and Practices						
Internal Controls	Require multiple signatures to authorize and approve transactions. Use separate accounts for savings, interest income, and reserves. Retain adequate source documentation for all transactions, and use serially numbered documents. Use ink for all financial records. Transact all business in cash and during bank meetings. Rotate persons assigned to deposit cash and restrict access of account signatories to accounting records.	Train members on purpose of internal controls. Discuss specific controls with members; adjust as necessary. Develop system for members and promoter to validate controls on regular basis.	1 2 3 1 2 3		4	Internal Controls

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Agency Audits	Agency audit staff or independent contractors conduct audit program, including: Comprehensive, scheduled audits by agency at least annually; Spot (unannounced) audits using quick and easy tools; Mini-audits when full audits are not practical or possible.	Train members on purpose and definition of agency audit; review agency procedures. Conduct one audit; evaluate results and adjust procedures as necessary.	1 2 3 1 2 3	4		Agency Audits Agency Mini-audits
Internal (Bank Member) Audits	A program of routine (at each meeting) and spot audits conducted by bank members.	Train bank members in member audit practices and to verify records using cash flow and financial status bar chart.	1 2 3		4	Bank Member Audits Cash Flow Financial Status Bar Chart

Lending Policies and Practices

Bylaws govern the management of the village bank's internal account. They provide an objective policy guide for members when issues arise.

Initially, village bank members should collectively discuss the various policy options to incorporate into the bylaws and, ultimately, reach agreement on a set of bylaws for their bank. Bylaws are meaningful only if they are understood, followed and enforced by the group who collectively agree upon them. The consensus they represent provides transparency and empowerment to the group.

Historically, village bank members determined lending policies and loan terms using a series of guided questions. As a group, they decided on loan duration, repayment schedules, interest rates and loan amounts—which were then codified in the bank's bylaws.

While village banks still address these same issues in their bylaws, your agency may have policies regarding the internal account that it wishes to standardize for all village banks, or may require that loan terms fall within certain predetermined minimums and maximums. These required terms reduce high-risk lending practices that jeopardize savings and repayments to the external account. However, bank members have discretion within these ranges, so you will find wide variations in loan terms from bank to bank.

For many of the policies and procedures established in the bylaws, the group may wish to decide only on broad parameters. For example, the loan term section of the bylaws may state minimum or maximum parameters only. Individual borrowers will have specific terms within these parameters.

Bylaws should be updated regularly over the life span of the village bank. Procedures and rules established during the initial formulation of the bylaws should be reviewed at the end of each cycle to see if they are still timely and fit the needs of the village bank. Systematic review of bylaws is also another way of building ownership, solidarity and empowerment among members.

Tool References

Lending Strategies and Safeguards
Loan Policy Discussion Guide
Selecting an Interest Rate
Selecting a Repayment Schedule
Establishing Sanctions
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Lending and Account Mobilization

Internal account lending is by far the most common investment mechanism for village banks. The major advantages are as follows:

- higher returns to members (if the village bank distributes dividends);
- additional community credit (funds rotate within the community, they are not tied up in fixed assets or bank deposits).

Tool References

Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Lending External Account Repayments

The original village banking methodology channeled external payments through the internal account loan fund in order to expand funds available to members. This allowed the bank to serve the additional credit requirements of bank members and the community, and increased the bank's overall return on the internal account.

While some agencies still use this approach, the associated risks have led many agencies to completely separate the external account from the internal account. Some agencies now require external account loan repayments to be kept on deposit in a commercial bank as they are repaid. Or, they require the bank to pay regular loan installments to the institution, rather than in a lump sum payment at the end of the loan cycle.

In general, banks should only use external account loan repayments for internal account lending when:

- the bank has limited access to banking infrastructure in order to secure funds, and/or
- external account loan repayments to the agency are scheduled on a monthly basis (at minimum) and the internal account repayment schedule is more frequent.

Tool References

Lending Strategies and Safeguards

Advantages

Supplementing the internal account with external account payments has a number of advantages. Overall, it is a more efficient cash system as repayments do not lie idle in an account at the village bank or agency and an almost automatic turnaround is possible.

The specific advantages of using external account payments as part of the loan fund include the following:

- *it increases the amount of internal account capital available.* This makes funds available to a wider group of borrowers (possibly including those in the community who are not members of the bank) or for other quick-return investments;

- *it increases return to members.* Members earn a return on the float for the agency's funds. Interest and investment income earned from external account payments are generally considered village bank equity which, in turn, can be distributed to members as dividends;

- *it enhances security of external account payment.* Many agencies channel external account payments through the internal account to reduce the risk of theft. These village banks usually repay the agency on an end-of-cycle or monthly basis;

- *it reduces the cost of collection.* Agencies that channel external account payments through the internal account avoid the costs associated with frequent collection.

Disadvantages

Disadvantages of this practice include the following:

- *increased risk to the external account and the agency.* The village bank is responsible for the entire external account debt at the end of the cycle (rather than just for the final payment). At the same time, the bank must effectively manage a larger internal account loan portfolio, fueled by external account payments. The agency's risk also increases when members assume additional debt that is not reduced until the end of the loan cycle;

- *increased complexity in recordkeeping.* Maintaining records that accurately distinguish internal account funds from external account funds temporarily channeled through the internal account has proven difficult for many village banks. Recordkeeping is already complex due to variations in loan terms and amounts;

- *negative impact on the agency's program sustainability.* The agency cannot generate income by relending external account repayments during a loan cycle; instead, the repaid funds are retained in the village bank's internal account. However, the agency's income only suffers if its program is otherwise capable of rapidly reinvesting external account loan repayments. FINCA is one of the few programs that manages highly efficient cash systems in which external account repayments are almost immediately relent to new or existing banks. This practice has been critical to FINCA's high sustainability rates.

Mitigating Risk of Lending External Account Repayments

For those agencies that allow their village banks to channel external account payments through the internal account loan fund, the following may mitigate risk:

- *increase village bank reserve requirements.* Given a larger portfolio, it is reasonable to require the village bank to maintain a larger percentage on reserve. A staggered or shifting cash reserve, as described later in this chapter, also may be appropriate in certain cases. However, a reserve requirement is not a viable option unless the village bank has ready access to a secure deposit-taking institution;

- *increase frequency of external account loan repayments to the agency.* This practice decreases risk to the village bank and the agency by reducing the amount of external account funds held in the internal account until the end of the cycle. A mid-cycle repayment requirement of between 30% and 50%—or even a monthly payment requirement—decreases risk while still allowing members to leverage external account funds;

- *decrease internal account loan duration or increase payment frequency*. Instead of increasing payments to the agency, the village bank could require frequent internal account payments or shorter loan terms. This would ensure a steady cash flow to the village bank and continue to free up funds for broader community and/or members use.

Note: The following material assumes that external account payments are not part of internal account lending, unless otherwise stated.

Initiation

Your agency should work collaboratively with its village banks to determine the most appropriate time for each bank to start its internal account lending program.

For purposes of efficiency and accountability, agencies often prefer that their banks have certain basic
banks begin lending. Likewise, bank members should
anagement, including recordkeeping and auditing

ınd procedures to govern the following before it can

ıbers and nonmembers: interest: guarantees, if any;
elinquency and default consequences;

ıntil a bank reaches its second, third or even fourth
sire to do the following:

y increasing the management ability of the group

ernal account portfolio before lending internal

village bank must satisfy before it can begin
outlines the FINCA/Uganda criteria, established
oans began to affect repayments to the agency's
roved successful in enhancing performance in both

everal cycles before they begin lending for similar
builds the internal account, thus permitting more

mediately, either out of necessity (in cases where
secure their funds), or:

Figure 7: FINCA/Uganda: Internal Account Loans Cycle 2, Week 8

Absolutely no village bank may use savings for internal account loans during the first two cycles. Most groups should not use the internal account until after cycle three.

After reviewing a village bank's performance in loan repayment, attendance, and savings, a promoter may recommend that the bank's members be trained in internal account lending at the end of cycle two. The bank is not required to offer internal account loans and should be discouraged to do so if conditions are not suitable for success.

FINCA/Uganda must be informed in writing of the intent to use the internal account for lending.

Note: Groups should be denied permission if their performance is not above average, as determined with reference to the following:

- On time weekly repayment: 90%
- Overall average attendance: > 85%
- On time monthly payment to FINCA: 100%
- Savings for each client: 20% or more
- Accurate and timely records
- Arrears at end of cycle: 0%

The promoter assesses leadership and solidarity to ensure transparent administration.

- develop confidence in their members or systems while the loan fund is relatively small,
- immediately apply the training they receive in loan and risk analysis,
- face issues that become more difficult with larger amounts at stake,
- establish control, thereby reducing paternalism on the part of the implementing agency.

Tool References

Lending Strategies and Safeguards
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Eligibility

Loan-eligibility policies often change over the life of a village bank
restrict internal account loans to members, due to limited availabili
solidarity among the members. As the balances in their internal acc
their members, village banks often begin to lend to other persons in

Village banks generally find it more profitable to lend to both their
persons in the community at large. This eligibility policy also reduc
your agency. As a result, it is the recommended policy for long-term
Lending to nonmembers accomplishes the following:

- spreads risk among borrowers who do not have existing ex
- may be necessary to mobilize idle funds, increase returns to risks in locations where there are no deposit-taking institution
- increases returns as nonmembers are often charged higher
- extends availability of loan capital to the community; and
- may bring in poorer members of the community who initia fledged members.

Figure 8: Eligibility Policies around the World

CRS/Burkina's partner Wend Penga Association lends only to nonmembers to ensure that community members who are not part of the village bank have access to its services.

FINCA/Uganda also lends to nonmembers in order to reduce risk, but requires all internal account borrowers (members and nonmembers) to save with the village bank.

Women's Opportunity Fund's partner, AGAPE, lends small amounts from the internal account to test a potential member's repayment ability before she is offered an official membership.

ADRA limits lending to members until a bank enters its third cycle, at which time members are thoroughly trained in internal account practices.

Many agencies, however, limit internal account lending to members. In other cases, the village banks themselves choose to limit eligibility. Their reasons are financial and social, since the policy does the following:

- potentially decreases risk, due to the fact that member borrowers are also investors in the internal account fund and are therefore personally affected by internal account delinquencies;
- relies on member solidarity to ensure repayment;
- gives members priority access to limited loan capital.

Tool References

Lending Strategies and Safeguards
Loan Policy Discussion Guide
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Duration

Most agencies require all internal account loans to be repaid by the end of the village bank's external account loan cycle. This policy reduces risk, as follows:

- it allows the agency and the village bank to more easily examine the bank's financial status at the end of the cycle, while there are no loans outstanding in the accounting records;
- it prevents borrowers from taking out internal account loans to repay external account debt;
- it prevents member borrowers from assuming new, external account debt based on group savings, which are, in actuality, at risk as outstanding internal account loans.

This policy is particularly important to reduce risk for village banks that include external account repayments as part of the internal account loan fund.

Some agencies, such as FINCA Kyrgyzstan and Nicaragua, impose even stricter requirements by limiting the duration of a bank's internal account loans to one month or less. Kyrgyzstan instituted the policy because its banks operate without access to secure deposit-taking institutions and therefore lend out 100% of their accumulated savings at each meeting. FINCA/Nicaragua also limits access to savings; as of March 1997, 3% of its total savings were outstanding as internal account loans. According to FINCA, both of these country programs experience low delinquency rates—only 2.7% delinquency in Kyrgyzstan and 0% in Nicaragua.

FINCA/Malawi has instituted a similar staggered-duration policy. In its second cycle, a bank's internal account loans are limited to terms of one month or less. In cycle three, the limit is two months. In cycle four, the limit is three months, and for all subsequent cycles the maximum loan length is four months (equal to the external account's loan cycle). Malawi allows borrowers to use internal account loans to repay external account debt, but promoters strongly discourage the practice.

Tool References

Lending Strategies and Safeguards
Loan Policy Discussion Guide
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Interest

Many agencies find it cost-prohibitive to establish and monitor internal account interest rates for their village banks. As a result, the village bank, with appropriate training and guidance from the agency, largely determines these rates.

In general, the rate should not be so high that credit becomes cost-prohibitive for low-income populations, or so low that the bank's savers earn negative returns on their savings. Within this range, most banks consider the following issues when establishing the bank's interest rate policies:

- *amount of loan.* Larger loans generally receive more favorable rates;
- *length of loan.* In most cases, longer loans receive more favorable rates;
- *purpose of loan.* Productive or emergency loans may earn lower rates, while consumption loans earn higher rates. In some cases, emergency loans may even be interest free;

- *membership.* Members are generally charged more favorable rates than nonmembers;
- *member guarantees.* Loans that are guaranteed by members receive more favorable rates;
- *collateral.* Collateralized loans receive more favorable interest rates;
- *competing interest rates.* Interest rates should be competitive with local market rates; and
- *type of loan.* Internal account nominal interest rates are generally higher than external account rates.

The interest from its internal account loans provides a bank with income to cover its operational expenditures (such as management committee fees, books, transportation, banking fees) and to pay dividends to its members. The opportunity to manage this income fosters capacity building within the bank.

Tool References

Lending Strategies and Safeguards
Selecting an Interest Rate
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Repayment Schedule

Although agencies generally require that all internal account loans be repaid before the end of the cycle (as previously noted), within that restriction, village banks have considerable discretion. Banks generally establish a variety of payment plans based on the purpose of the loan and the borrower's individual circumstances.

While it is not possible to recommend only one repayment plan, a bank should consider the following when crafting its repayment schedules:

- *borrower's repayment history* for both external account or internal account loans;

- *borrower's financial situation;*

- *purpose of the internal account loan* (emergency, working capital, or consumption items) and how often borrowers can reasonably be expected to make payments on such loans. Most families, for example, find it difficult to repay emergency loans over a short repayment schedule. Working capital loans often have repayment schedules similar to those of external account loans (monthly or weekly payment periods), whereas the schedules for fixed asset or other consumption loans may require less frequent payment periods or even a balloon payment. Balloon payments are also fairly common for emergency loans;

- *village bank's social and economic objectives* for the lending program;

- *overall state of the internal account,* which can determine liquidity requirements and whether or not the repayment schedules must generate frequent inflows of funds into the account. For example, a bank which mobilizes external account repayments as a significant portion of the internal account loan fund requires higher liquidity and more frequent inflows of funds into the account than does a bank which does not mobilize external account repayments;

- *ability of the village bank to manage multiple repayment schedules.* For less sophisticated management committees, it may be preferable to establish one or a very small number of standard repayment schedules that apply to all loans. As the bank's experience and level of business sophistication increases, it can gradually expand the number of repayment schedules it offers.

CRS' village banks in Thailand and Cambodia adopted a repayment schedule that calls for monthly interest payments and a single balloon payment of principal. KMBI Women's Opportunity Fund's partners (KMBI in Colombia and AGAPE in the Philippines) implemented weekly or biweekly payment schedules. FINCA Uganda requires a minimal monthly payment but permits more frequent payments. CRECER, Freedom from Hunger's Bolivian program, requires a borrower to prepay interest when the loan is disbursed and to make a balloon payment of principal at the end of the cycle.

Tool References

Lending Strategies and Safeguards
Selecting a Repayment Schedule
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Amount

To encourage diversity and limit risk, village banks should never invest more than 25% of their total internal account loan funds in any one loan. In addition, many agencies impose restrictions on the *total* amount of internal account loans that are available for on-lending.

Some agencies, whose banks lend exclusively to bank members, link the total of internal account loans to the total of members' savings. In CRS/Ecuador for example, members' internal account loans are limited to between 110% and 120% of total accumulated savings. FINCA Malawi and World Relief Cambodia also limit internal account loans based on savings. World Relief uses a ratio of 1:3 (a dollar in savings leverages three dollars in loans)—a system not unlike the credit union approach.

Other agencies, such as FINCA/Uganda, limit total lending to 25% of the *total internal account*—they do not link lending limitations to just the member savings portion of the internal account fund.

Unfortunately, most agencies have done little to train their village bank members in methods that can be used to assess individual loan requests and there is no consensus on a recommended policy governing internal account loan amounts. It is vital for your agency to teach bank members how to make these loan decisions, based on an analysis of the bank's financial condition.

In determining loan amounts, the bank members and agency should consider the:

- total amount of funds available,
- economic status of loan applicants,
- total number of loan applicants,
- purpose or intended use of each loan,
- loan applicant's borrowing history (as initial loans are generally small, until the borrower has proven to be responsible and reliable).

Some village banks, in order to maximize interest income, simply attempt to satisfy *all* internal account loan requests. If the funds are insufficient, they may evenly divide the available funds among the applicants or ask the management committee to prioritize the potential borrowers.

Tool References

Lending Strategies and Safeguards
Loan Policy Discussion Guide
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Loan Guarantees

In situations where group solidarity and peer pressure have proven insufficient to ensure repayment, banks adopt other guarantees. Examples include:

- personal guarantee by a bank member,
- collateral for larger loans,
- formal loan applications and contracts suitable for use in legal proceedings,

- savings requirements,
- higher interest rates for nonmembers,
- borrower restrictions limiting loans to individuals known in the community and considered low risk.

Personal guarantees can strengthen solidarity among members although they have the potential to be misused through favoritism or nepotism. Guarantees are generally considered more appropriate for larger loans.

Tool References

Lending Strategies and Safeguards
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Loan Analysis and Approval

Village banks commonly require the approval of a majority of the membership in order to grant a loan. This policy reinforces ownership and maintains transparency.

Some banks also ask their management committees to prescreen loan applicants. FINCA/Uganda's village banks elect a special internal account loan committee, separate from the management committee, for this purpose.

Banks often require borrowers to repay their outstanding internal account loans before they can receive a new loan (referred to as a single-loan requirement). Often, this policy simply means that the borrower refinances the existing loan or repays the loan and increases the size of the new-loan request accordingly. Nevertheless, the practice is recommended to reduce risk, particularly for village banks that include external account repayments as part of the internal account loan fund.

A small number of agencies involve the village bank's promoter in the bank's approval process. This practice is not recommended because it undermines the efforts to build capacity and empowerment among the members. While it can potentially decrease the number of high-risk loans and reduce favoritism, the opposite may also be true if the promoter has close ties to the community or the bank's management committee. The practice also increases costs to the agency.

Existing loan-approval practices are generally *inadequate* to ensure quality loans. Risky loans are often approved because approval practices fail to consider:

- the security and financial advantages of lending,
- time constraints and lack of risk analysis tools,
- familiarity with fellow members' businesses (which tends to devalue the formal loan assessment process),
- deference or peer pressure (although some use secret ballots or ask the borrower to leave the room while the loan request is discussed),
- a general lack of understanding of the loan approval process.

Tool References

Loan Analysis and Approval
Analyzing Loan Feasibility (Lesson 5)
Tough Love (Lesson 6)
Loan Approval Exercise

Delinquency and Collection

The internal account represents a village bank's largest asset and, when lent out, its primary source for income. However, because there is a chance that borrowers of internal account funds will not repay their loans, the internal account involves risk. The exact amount of this risk changes continually as the bank disburses new loans and payments become due on existing loans.

Minimizing risk involves the following:

- measuring and monitoring portfolio indicators such as the portfolio outstanding, number of loans outstanding, portfolio at risk, and average loan size,
- tracking delinquencies,
- establishing sound collection practices.

Tool References

Delinquency and Collection Checklist
Collecting Delinquent Loans (Lesson 7)
Troubled Loan Report
Preparing the Troubled Loan Report
Reporting on Troubled Loans (Lesson 8)
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Cash Reserves

A village bank's cash reserve represents an informal loan loss reserve for its internal account lending program. Reserves provide a safeguard for both the village bank and the agency. As such, they are recommended for all village banks with the exception of those banks located in regions without access to secure, deposit-taking institutions.

Criteria for Setting Reserves

Reserve requirements and the impact on the size of reserves are summarized in Figure 9.

Figure 9: Criteria for Setting Loan Reserves

Reserve Rate Criteria	Criteria Level	Reserve Level
Management skills of village bank committee and/or members	Basic skills Increased skills	Higher reserve Lower reserve
Internal account and external account portfolio performance	Poor performance Better performance	Higher reserve Lower reserve
Risk of theft to the agency and the village bank	Increased risk of theft or higher security risk	Lower reserve
Other economic indicators (such as inflation)	Increased inflation	Lower reserve

Reserve Options

Generally, reserve requirements range anywhere from 2% to 50% of the internal account loan balance. High reserve requirements restrict access to the internal account, thereby insulating both bank members and your agency from risky lending practices. AGAPE, Women's Opportunity Fund's Colombian partner, requires a 50% reserve, as does FINCA Nicaragua.

However, for banks operating in inflationary environments or without access to secure deposit-taking institutions, a high requirement may be inappropriate. Maintaining a large reserve during a period of high inflation generates negative returns, unless the reserve is invested in high-return financial instruments.

Some agencies impose a staggered or variable reserve requirement in an attempt to link the size of the reserve with bank management's capacity, portfolio performance and environmental conditions. CRS/Haiti, for example, has adopted a fluctuating reserve policy based on internal account portfolio performance. This relatively sophisticated approach requires an adjustment to the size of the reserve each cycle. It requires risk-analysis training for bank members and agency promoters—an investment that should prove cost-effective over the long run.

FINCA/Malawi has adopted a staggered policy that requires a 75% reserve for the village bank's first internal account loan cycle. This requirement is reduced by 25% for each successive loan cycle. By cycle five, the reserve is reduced to zero and members have total access to the bank's internal account. This policy shifts from one extreme (a 100% reserve) to the other (a 0% reserve) based on the assumption that members' management abilities increase each cycle, thus reducing risk to the agency. FINCA/Malawi's reserve policy has generally proven effective, except during periods of high inflation (a 60% annual inflation rate in 1996, for example).

Other agencies have adopted a somewhat lower, constant reserve amount. Low reserve requirements (generally from 2% to 10%) allow more lending capital to circulate among bank members and the community, thereby increasing interest income to the bank and enhancing access to credit. Agencies that adopt this low-reserve policy tend to view the reserve as an emergency fund rather than a bad debt fund.

Tool References

Guidelines for Managing the Internal Account's Cash Reserve
Establishing a Cash Reserve (Lesson 9)
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Savings Policies and Practices

Agencies encourage—and usually require—savings as a source of long-term funding. The requirement for mandatory member savings is generally stated as 20% of the current external account loan amount. Agencies and village banks have had relatively limited experience with voluntary savings and their impact on internal account practices. However, it is fair to say that voluntary savings programs introduce a new set of management requirements.

Savings provide members with an asset base and provide the village bank with a source of funds for possible future transition into a deposit-taking financial intermediary. While most agencies currently do not manage savings deposits, many consider this capability to be a major growth opportunity and are developing capacity. The transition to a formal financial institution also brings the agency under regulatory scrutiny, which can lend credibility and confidence to its savings activities.

Tool References

Savings Practices (Lesson 10)

Agency Considerations for Mandatory Savings

Member savings in the internal account represent a form of collateral for the village bank and for y agency.

Some agencies allow a village bank or bank member to borrow against savings—to accrue internal account debt—to repay external account debt, when necessary. Generally recommended on a case-by-case basis. Most often, identifying such situations is the bank' responsibility, although some agencies issue their own guidelines. These guidelines protect m savings and the agency's external account investment.

Most agencies discourage this practice, however, by requiring that all repaid by the end of each cycle. Such a requirement prevents over-lev loan when the bank has internal debt or insufficient savings. If the siz depends, even in part, on accumulated savings, outstanding internal account debt places the external account loan at greater risk.

It is even riskier for a bank member to use an internal account loan to repay external account debt when external account payments make up a portion of the bank's internal account loan fund. In such

Figure 10: Using Savings to Repay a Loan

Cycle 4:	
External account loan	200
Savings	100
Internal account loan (to repay external account loan)	75
Cycle 5:	
External account loan (reduced by 75)	125
Savings (after internal account loan)	25
Internal account loan	0

situations, the bank should require the member to have savings equal to or greater than the amount of the internal account loan. This provides the bank with the option of reducing the member's next external account loan by an amount equal to the internal account debt.

By reducing the next external account loan by the amount of the internal account loan (or savings withdrawn to repay the external account loan), the member's savings remains in relative proportion to the external account debt (Figure 10).

Member Considerations for Mandatory Savings

Bank members' concerns with regard to their savings generally involve the following:

- security,
- access to funds when necessary,
- earnings rates which, at the very least, maintain principal value.

Members must recognize the impact their savings have on overall village bank operations and internal account portfolio quality. Educating them in management practices as well as how savings contribute to the village bank's financial system are key to building robust and lasting programs.

Savings policies span a continuum ranging from mandatory required amounts with highly restricted access, to voluntary deposits with total access. In practice, many programs operate in more than one place on this continuum.

Security

Savings security encompasses all aspects of sound internal account management.

Minimum practices include the following:

- cash reserve requirements, if a depository institution is available,
- member training in loan analysis,
- mandatory adherence to internal controls,
- regular bank and agency audits,
- physical security of cash (lock box or account at a commercial bank).

Access

Traditionally, village bank members have limited access to their savings (both mandatory and voluntary amounts). However, the current trend is to provide members with greater access to savings. Experience in the microfinance sector demonstrates that savings rates do not decrease— and often actually increase—with greater accessibility to funds.

In general, the greater the members' access to savings (mandatory o members require in both the management of individual savings and bank operations. Such training leads to greater appreciation for tra effective loan analysis.

Figure 11: Policy Options for Access to Savings

Only upon resignation
When members resign, usually at the end of a cycle. Upon resignation, member no longer participates in lending or savings activities

Only at end of cycle

The most restrictive access policy allows members to withdraw savings only upon resignation from the bank. These groups view village bank deposits not so much as current savings, but as investments, similar to buying shares for which there may be a penalty for early collection. The implementing agency or lender views savings as built up collateral and therefore will usually not issue larger loans without sufficient savings on deposit.

Advantages of this policy include the following:

- a potentially larger loan fund for the community,
- increased security for the external account,
- reduced length of the meeting for members and fewer duties for the committee since there are fewer withdrawal transactions to process,
- a higher return to members, if savings are lent out.

Possible disadvantages include the following:

- negative returns in environments with high inflation,
- decreased motivation to save beyond the required minimums to provide liquidity in emergency situations,
- increased drop-out as a means to access savings, and
- in general, mandatory savings raises effective interest rates on loans without increasing income to the institution.

Some agencies and village banks have modified this policy by allowing members to withdraw savings at the end of a cycle. Freedom from Hunger promotes withdrawable savings. The frequency is left to the village bank to determine based on its capacity to manage these transactions. Freedom from Hunger recommends maintaining an obligatory reserve of 5% on the loans outstanding. World Relief Cambodia restricts resignations at mid-cycle to prevent a run on the bank if things are going badly. In addition, all members must approve an early withdrawal of savings and the withdrawing member forfeits all interest. End-of-cycle withdrawals are permitted without penalty, but the maximum loan amount for the next cycle is reduced by the amount of the withdrawn savings.

Advantages of access policies that permit savings withdrawals at the end of a cycle include the following:

- additional flexibility for members while maintaining security benefits,
- fewer withdrawal transactions than with more flexible options, thereby reducing meeting time for members and duties of committee,
- greater stability for the internal account loan fund during the cycle than would be the case with more flexible access options.

Disadvantages of access policies that permit savings withdrawals at the end of a cycle include the following:

- the internal account fund can fluctuate widely between cycles; and
- the maximum amount of external account lending is generally reduced by the amount of withdrawn savings, thereby affecting the agency’s program sustainability.

Advantages of access policies that allow savings withdrawal at any time during the cycle include the following:

- access and flexibility for the member, and
- incentive to save.

Disadvantages of access policies that allow savings withdrawal at any time during the cycle include the following:

- with member access comes increased cost to the bank, which must manage withdrawals and recordkeeping, and
- access to savings may lower member need to borrow, therefore, less revenue may be generated by the bank.

Village banks can reduce risk in their internal and external accounts—and provide an incentive to members to remain in good standing—by permitting only those members with no outstanding internal account loans to withdraw their savings. However, this policy also creates offsetting disincentives to borrow from the internal account and to save at full capacity.

Some village banks allow additional withdrawals under emergency situations. This is convenient for members and encourages additional savings, although this practice still provides a savings disincentive relative to more flexible policies. In addition, the internal account can experience significant fluctuations if members withdraw large amounts to cover emergencies.

Very few village banks with significant internal account lending activity allow members to withdraw savings at will; the internal account loan fund can become unstable if many members withdraw funds at one time. An unlimited-withdrawal policy increases costs to members both in terms of meeting times and committee oversight. In the event of delinquency, it also increases risk for both the internal and external accounts.

Earnings

Earnings from savings are most often returned to the bank members in the form of dividends that are distributed at the end of each cycle, or are reinvested in the internal account as bank equity.

Voluntary Savings

Most agencies have had relatively limited experience with voluntary savings programs and the impact these programs have on internal account management. Not all members can afford to contribute to a voluntary savings program but, for those who can afford it, the program provides a convenient investment alternative.

The major options for managing voluntary savings include depositing member funds into a commercial savings account and on-lending internal account funds to bank members and the community at large. While the commercial savings account option provides the lower return, this choice is highly liquid, very secure and simple to monitor. The on-lending option provides a higher return, but is less liquid, less secure and more complex to monitor.

If voluntary savings are totally accessible and included as part of the internal account loan fund, the fund can be very difficult to manage. Therefore, some agencies require banks to deposit voluntary savings in a secure bank account (rather than lending them out), where they can be withdrawn as needed. However, it is more common for village banks to lend out voluntary savings and restrict withdrawals to the end of a cycle.

Recordkeeping Policies and Practices

Recordkeeping practices for the internal account, though potentially cumbersome and costly if not well designed, represent the most effective means of monitoring lending activity and reducing risk. They also provide an early warning of trouble in the external account.

Your agency should adopt a standardized recordkeeping system to be used by all of your village banks. However, before implementing this system for a specific village bank, discuss the system with the bank's members and management committees—and implement any small revisions or customizations—to foster a sense of ownership and capacity.

An effective recordkeeping system captures information on borrowers, initial loan amounts and other loan terms, disbursements, and borrower repayments. It manages dividends and produces necessary financial reports. Importantly, it is sufficiently simple that bank members (after an initial training period) are able to maintain and audit the system without your assistance—yet detailed enough to capture essential portfolio and financial data.

Tool References

Keeping Records for the Internal Account, an Overview
Keeping Records for the Internal Account (Lesson 11)

Loan Documents

Loan documents include applications, loan contracts with payment schedules, plus any written guarantees or descriptions of collateral.

The use of formal written applications tends to inhibit what borrowers need most—fast, flexible loans. The practice often requires promoter assistance, which further increases costs to your agency. As a result, written applications are generally not recommended, unless the loan amount is particularly significant or the borrower is not a member of the village bank. Interviews and oral presentations by the borrower are generally more effective loan analysis tools than are written applications.

Loan contracts, on the other hand, are essential to effective internal account management. Contracts formalize loan amounts and other loan terms, including interest rate, payment schedule, fees and duration. They also help to standardize the lending process and discourage lending where the purpose of the loan is unclear or the means of repayment is uncertain.

Most agencies supply village banks with a standard loan contract form. Although the toolkit includes the loan contract as a separate document, you can also incorporate the contract in the member passbook.

In addition to loan contracts, some programs require collateral or guarantors to reduce the risk of nonpayment. CRS/Ecuador requires collateral only from nonmembers because they usually do not save with the bank. While the use of formal loan documents is not commonplace among agencies, the practice is effective. On the other hand, agencies that advocate an informal loan process do so to simplify operations for the village bank and to encourage borrowing by those who might be discouraged by applications and guarantees.

Figure 12: The Pros and Cons of Loan Applications and Guarantees

Pros	Cons
Formalizes internal account lending practices Discourages risky loans Increases likelihood of timely repayment	May inhibit borrowing by needy or illiterate persons Guarantor process may be subject to nepotism or favoritism May provide a false sense of security unless accompanied by effective training

Tool References

Loan Contract
Payment Plan
Preparing a Loan Contract and Payment Plan
Using the Loan Contract and Payment Plan Form (Lesson 12)

Disbursement and Payment Records

The simplest and most efficient way to manage internal account loans is to state clearly expectations for loan payment dates and the amounts on disbursement and lending documents.

The loan contract includes a repayment schedule. In addition, the toolkit includes a disbursement summary and payment activity summary for the village bank, detailed individual account loan records for the bank's recordkeeping, and a passbook form for the borrower.

Tool References

Loan Disbursement Summary
Preparing a Loan Disbursement Summary
Using the Loan Disbursement Summary Form (Lesson 13)
Passbook
Preparing the Passbook
Individual Internal Account Loan Record
Preparing the Individual Internal Account Loan Record
Payment Activity Summary
Preparing the Payment Activity Summary
Using the Loan Payment Forms (Lesson 14)

Dividend Calculation and Distribution

You can provide a savings incentive and ensure a return to village bank members by encouraging your village banks to calculate and disburse dividends (representing the accumulated earnings of the bank) to bank members on a regular basis.

Tool References

Dividend Calculation Form
Dividend Distribution Form
Preparing the Dividend Calculation and Distribution Forms
Using the Dividend Forms (Lesson 15)
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Calculation

Dividends represent distributions of village bank profits that were generated by internal account lending programs, bank fees and fines, and other income-generating activities. Banks can distribute all or a portion of these profits to members as dividends.

Dividend amounts paid to each member are generally calculated based on each member's savings in relation to total bank savings as outlined by the following formulas:

Earnings to be Distributed / Internal Account Total Fund = Dividend Factor

Dividend Factor x Member Savings = Dividend Amount to Member

The recommended value for member savings in the above equation reflects the beginning-of-cycle balance. This number is simple and readily available and encourages members to save during the current cycle in order to increase their dividend allocations in the following cycle. It distributes profits fairly among the bank's members.

Formulas that factor in the amount of time each member has invested savings in the village bank are considered less appropriate.

Distribution

The most appropriate time to disburse dividends is at the end of the cycle. This practice has the following advantages:

- it provides a frequent return to savers because most cycles are between three and six months in length,
- it removes disincentives for the bank to accept new members by minimizing group equity,
- it is a simple and efficient time to distribute dividends as it is a natural time to close the village bank's accounting books.

Alternatively some agencies—including CRS/Thailand and Project HOPE—recommend that their village banks distribute dividends at the end of each year. As a result, members receive a sizable annual dividend. However, this practice discourages banks from accepting new members and may actually provide a lower return depending on inflation and other economic factors.

Financial Reports

While village banks do not normally produce formal income statements and balance sheets for the internal account, they should prepare a cash flow and a financial status bar chart at the end of each meeting to reconcile cash and provide members with a visual picture of the financial status of the internal account.

The cash flow and financial status bar chart also double as audit tools for village bank members.

Tool References

Cash Flow
Preparing a Cash Flow
Using the Cash Flow Form (Lesson 16)
Financial Status Bar Chart (Lesson 17)

Internal Control and Audit Policies and Practices

Internal control and audit policies ensure that the village banks you manage follow standard business practices and also safeguard against loss or misappropriation of funds. Audits verify that village banks and members actually exist and help to identify and solve business problems.

Virtually all agencies have implemented internal controls and auditing programs for the internal and external accounts of the banks they manage. The programs vary, however, in terms of the timing and types of audits conducted and in the persons responsible for conducting them.

Internal Controls

Internal controls are business practices that, when followed consistently, ensure the following:

- proper authorization for all transactions,
- accuracy and auditability of accounting and lending records,
- that funds and other assets are safeguarded from fraud or other misuse.

As such, they play a vital role in internal account management.

Internal controls create transparency, and are easily put into practice by village bank members. Your agency contributes by helping the bank to develop the appropriate controls, and by verifying their use during an agency audit.

Village banks have been particularly creative in developing and adapting the controls they use to accommodate existing infrastructure and cultural realities. Wherever possible, village banks should incorporate statements, receipts or other documents issued by formal financial institutions into their recordkeeping and internal control procedures.

Typical internal controls include the following:

- requirements for more than one signature to authorize or approve transactions;
- use of separate accounts for savings, interest, and cash reserve amounts;
- maintenance of joint accounts with the agency;
- adequate documentation for all transactions, such as the incorporation of bank statements into recordkeeping and reconciliation practices;
- use of serially numbered documents;
- required use of ink for all recordkeeping; use of white-out or correction fluid is prohibited;
- separation-of-duty restrictions to limit account signatories to members without access to accounting records;
- requirements that all transactions take place during a village bank meeting.

By far the most common internal control (almost universal in its implementation) is the requirement for multiple signatures to authorize cash and bank transactions. Typically, such transactions include loan disbursements, repayments, savings deposits, withdrawals and advances from the internal account to pay for bank expenses. Generally, this control requires the signature of a management committee member plus the member making the transaction. Under certain circumstances, a transaction may also require a signature from another committee member or a member at large.

FINCA/Malawi also requires two signatures to make a deposit. The two depositors are selected from among the bank members at each meeting and, at the end of each meeting, these two members deposit the savings collected during the meeting into the group account.

Tool References

Internal Controls (Lesson 18)

Agency Audits

The most common approach to auditing a village bank involves audits designed and conducted by the implementing agency. Half of the agencies contributing to this toolkit conduct annual, cyclical, monthly and/or spot audits of their village banks. Typically, these audits verify that all required internal controls are routinely practiced, reconcile the bank's books and compare accounting records with supporting documentation for a sampling of transactions. Audits are often designed only to examine the external account; however, auditing the internal account also provides valuable insight.

Tool References

Auditing a Bank, an Agency Overview (Lesson 19)
Operations Audit for Agencies
Preparing the Operations Audit for Agencies
Using the Operations Audit for Agencies Form (Lesson 20)
Operations Audit for Agencies, Findings and Recommendations Report
Preparing the Operations Audit, Findings and Recommendations Report
Financial Status Audit for Agencies
Preparing the Financial Status Audit for Agencies
Using the Financial Status Audit for Agencies Form (Lesson 21)
Village Bank Health Checklist, for Agencies

Types of Audits

Your agency's audit program should include each of the following:

- *Comprehensive, scheduled audits*, conducted for each village bank at least once each year. If your audit program includes more than 3,000 borrowers and the banks are located in remote sites, consider auditing only a portion your village banks at any one time. Use a random sample to choose the banks for each round of audits;

- *Less-comprehensive mini-audits*, scheduled at the end of each cycle, provide an opportunity to reconcile the village bank's accounting records;

- *Spot audits* as necessary, to supplement scheduled audits. Inform your village banks that you could conduct a spot audit at any time. Spot audits have proven especially important and effective in monitoring internal account activities of village bank and agency personnel. They are an important practice when you suspect that a bank is experiencing problems that are not addressed during regular visits. (FINCA Kyrgyzstan uses spot audits regularly to verify promoter reports, since all transactions are made in cash and there is no banking infrastructure.)

General Audit Recommendations:

Typically, a comprehensive audit includes all of the following activities:

- reconciling village bank records with bank statements, receipts and other source documents,
- reconciling village bank records with passbooks and other borrower documents,
- reconciling promoter and agency staff reports with village bank records and bank documents,
- verifying use of internal control procedures and practices,
- auditing a random sampling of transactions for accuracy and timeliness.

For scheduled audits, provide the village bank with a list of items to be reviewed beforehand. This ensures that the necessary paperwork and people are available when you need them. The list should detail the books and records you require and provide a general outline of the schedule. However, village banks should not be told the exact content of the audit. Audits are an instructional tool for the village bank as well as a control device. It is important that village banks view audits as a helpful process, not simply a "watchdog" intervention.

For spot audits, do not give prior notice of the audit. Your auditors should simply arrive at a predetermined (or randomly selected) village bank and explain to the members that they will be conducting a short audit during the meeting.

If you do not hire external auditors, or have an internal auditor on staff, do not have your loan officers or promoters audit the banks for which they are normally responsible. Such an action can jeopardize their working relationships with these banks. (In the same vein, each village bank should have access to an independent auditor for discussing issues that they are not comfortable reviewing with their promoter or loan officer.)

If you do use external auditors, the tools in this toolkit serve as a guide for your agency in communicating your requirements to the external auditors; who will likely have their own forms and procedures.

During any audit, use random sampling techniques to identify the transactions and members audited.

Random Sampling Methods

A random sampling method is an unbiased method of selecting banks, transactions, borrowers and bank members for audit purposes. You can use any of the following methods, or other more culturally appropriate means, to generate a random sample:

- place the names of all village banks (or other items) into a hat and pick the required number of banks for the sample;
- make an alphabetical list of all village banks (or other items), and choose every other bank, or every third or fourth bank, until you have the required number of banks for the sample;
- randomly assign each village bank (or other items) a number between one and six, and roll dice to choose the number to sample.

After you have selected your sample, don't change it—even if some of the items you selected are more difficult or less accessible than others you could have selected.

Figure 13: Summary of Audit Practices

Audit Practices for a Village Bank's Internal Account	
When	*Cyclical and annual.* Recommended minimum to identify problem areas and provide follow-up. *Spot.* Effective in minimizing misuse of funds. *Monthly.* Logistically difficult and costly but keeps records and transactions accurate and provides a high level of transparency.
Who	*Agency auditors (staff or contract personnel)*. Provide a regulatory service in the oversight of the internal account. However, frequent misuse of funds by staff and even auditors indicates that additional checks are necessary. *Internal auditors (village bank committee or member)*. Provides ongoing oversight, as well as a check on the implementing agency. Having the group regularly conduct its own audit builds capacity, ownership and empowerment. Training in sound audit techniques is an up-front cost but pays off in decreased costs of fraud and supervision.
What	Typically, the internal account should be audited for the following: ▪ reconcile internal account books with a sample of passbooks (randomly chosen), ▪ reconcile internal account books with any bank statements (if available) and receipts kept by the village bank group, ▪ review for accuracy as well as timeliness (whether internal account balances were deposited promptly), ▪ review transactions and operational procedures to see if control systems are followed, ▪ reconcile promoter or staff reports with internal account books, receipts, passbook, cash available and bank statements, if available.
How	Standard audit tools range from short one-page checklists to detailed questionnaires with specific criteria for sampling and performance ranges. Audits conducted by agency staff represent the traditional approach. Internal audits conducted by village bank members are generally more participatory and focus on ways to impart accounting information to the group and provide necessary village bank documentation. These audits are new to internal account management, but satisfy a recognized need if village banks are to assume ownership of internal account management.

Internal Audits by Bank Members

Bank members can conduct routine or spot audits of village bank accounts and records to minimize the opportunity for fraud on the part of committee members and promoters. These audits have the added advantage of increasing the accounting expertise of village bank members.

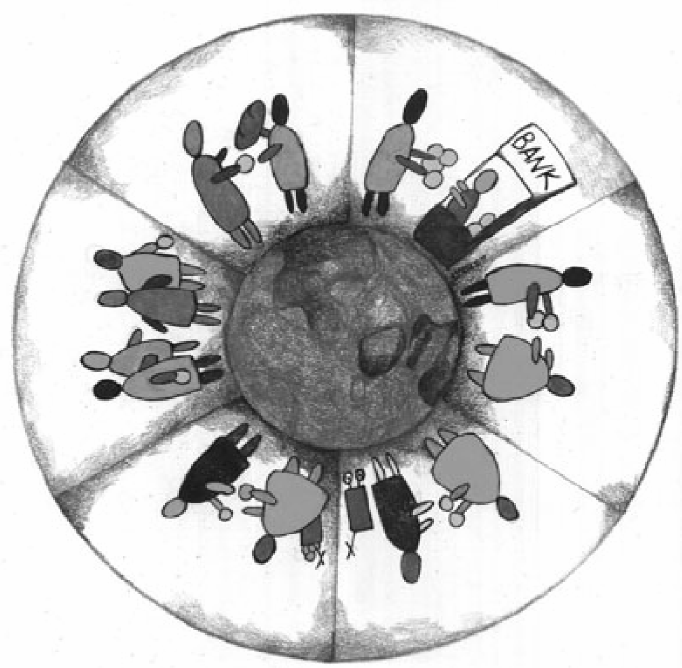
Member audits generally consist of the following activities:

- verifying the accuracy of amounts by comparing member passbooks and village bank records,
- comparing receipts and other source documents with village bank records,
- reconciling the village bank's cash on hand at the end of every meeting.

Tool References

Audit Procedures for Bank Members
Preparing the Audit Procedures for Bank Members
Auditing a Bank Member Audit Guidelines (Lesson 22)
Cash Flow
Using the Cash Flow Form (Lesson 16)
Financial Status Bar Chart (Lesson 17)
Bylaws Decision Tool
Bylaws Discussion Guide (Lesson 4)

Section Two: Toolkit



Introduction

The tools in this section of the toolkit are designed for your use in implementing, overseeing and auditing the internal accounts of your agency's village banks, as well as in training agency staff and bank members on internal account issues. Some tools, such as the agency audit forms, you will use yourself. Others you will, in turn, provide to the management committee and members of your village banks for their use.

Classifications

The more than 50 tools in this toolkit include those in both of the following categories:

- *functional tools* that practitioners and bank members routinely use in managing their internal accounts, and
- *educational tools* that inform agency staff and bank members about village banking concepts or the use of functional tools.

To provide you and your fellow practitioners with the most flexible and adaptable toolkit possible, each tool represents a basic element or building block designed to address a single policy or practice—a loan contract form or a savings exercise, for example. Because many of these tools address a similar function or process within the village bank, they are aggregated into sets, such as payment records, disbursement records, agency audits, internal controls, and savings practices, which consist of two or more tools placed contiguously within the document. Thus, you can easily locate the specific tool, be it a form or an exercise that you require for a specific purpose.

In practice, you can combine and repackage the basic tools in any way you wish. For example, if you are hosting a seminar on recordkeeping practices for village banking, you might wish to use all of the tools in all of the tool sets in the Recordkeeping Policies and Practices section. If your promoter plans a lecture on savings at one of her village banks, she can pull the set of tools applicable to savings. Alternatively, if she has limited time available, she can easily locate a single, short exercise on the importance of savings.

Tool Types

Each tool set includes two or more tools. Functional tools in the tool kit include forms, checklists, instructions, guidelines, analyses and diagnostics. Educational tools include discussion guides, exercises, and lessons. Within the context of this toolkit, a lesson is distinguishable from other educational tools only in that is represents a session in the suggested workshop or seminar agenda (see the Appendix).

For your quick reference, the table of contents entries and the titles for each of the tools indicate the tool type in parentheses following the title.

These various tool types are defined in Figure 14.

Figure 14: Overview of Tool Types

Tool	General Description
Functional Tools:	
Form	Document to collect or report information according to a predefined organization and content. The user enters the specific values. The toolkit provides a blank copy of the form for your use.
Checklist	Variation of a form—with check boxes rather than blanks for entered values. The toolkit provides a blank copy of the checklist for your use.
Instructions	Set of directions to provide guidance on preparing a form or checklist. Each includes a copy of the related form or checklist with numbers that link each field to narrative text that describes its content and purpose.
Analysis	Includes guidelines, diagnostics, matrixes and other charts designed to aid in analyzing an aspect of a village bank's internal account.
Educational Tools:	
Discussion Guide	Training tool that leads participants through a series of questions or brainstorming sessions that encourage participants to debate internal account management issues.
Exercise	Game, role play or other group-participation activity designed to provide information about a vital internal account management issue.
Lesson	Training tool, distinguishable from other training tools in that it is a component of the seminar/workshop agenda provided in an appendix to this toolkit. Each lesson presents training on one or more issues related to internal account management. Some lessons provide guidance in using one or more forms or checklists; others educate participants on vital topics or issues.

Most of the tools in this toolkit have been tested. However, all of the lessons are new. Other newly developed tools include the Guideline for Managing the Internal Account's Cash Reserve, Financial Status Bar Chart, Recordkeeping and Internal Controls, and Internal Account Diagnostic Tool.

If you intend to host seminars in internal account management, either for your agency's staff or for members of your village banks, you may wish to refer to the appendix to this toolkit. It provides a sample agenda based on the toolkit's lessons, additional lessons for experiential training, and seminar evaluation forms for your use. Also refer to the "How to Use this Toolkit" section in the Introduction to the manual.

Adjust the curriculum, training design and even the tools to suit your agency's requirements and lending environment.

Summary of Tools

The *Internal Account Management Toolkit* includes a three-lesson Overview and 19 tool sets categorized according to the following:

Figure 15: Summary of Tool Sets and Tools

Tool Set Name	Tools in the Tool Set	Type
Overview of internal Account Management		
Managing the Internal Account, an Overview	Managing the Internal Account, an Overview	Lesson 1
Using the Internal Account Management Toolkit	Using the *Internal Account Management Toolkit* Internal Account Diagnostic Tool Using the Diagnostic to Analyze the Internal Account	Lesson 2 Analysis Lesson 3
Lending Policies and Practices		
Lending Strategies and Safeguards	Lending Strategies and Safeguards	Discussion Guide and Exercise
Lending Practices and Loan Terms in the Bylaws	Loan Policy Discussion Guide Selecting an Interest Rate Selecting a Repayment Schedule Establishing Sanctions Bylaws Decision Tool Bylaws Discussion Guide	Discussion Guide Exercise Exercise Exercise Form(s) Lesson 4
Loan Analysis and Approval	Loan Feasibility Analyzing Loan Feasibility Tough Love Loan Approval Exercise	Analysis Lesson 5 Lesson 6 Exercise
Delinquency and Collection	Delinquency and Collection Checklist Collecting Delinquent Loans Troubled Loan Report Preparing the Troubled Loan Report Reporting on Troubled Loans	Checklist Lesson 7 Form Instructions Lesson 8
Managing the Cash Reserve	Guidelines for Managing the Internal Account's Cash Reserve Establishing a Cash Reserve	Guideline Lesson 9

Tool Set Name	Tools in the Tool Set	Type
Savings Policies and Practices		
Savings Practices	Moving Away from the Cliff Exercise A “Crummy” Lesson Four Lessons in Savings Savings Practices Guidelines for Savings Requirements	Exercise Exercise Exercise Lesson 10 Guideline
Recordkeeping Policies and Practices		
Keeping Records for the Internal Account, an Overview	Keeping Records for the Internal Account	Lesson 11
Lending Documents	Loan Contract Payment Plan Preparing a Loan Contract and Payment Plan Using the Loan Contract with Payment Plan	Form Form Instructions Lesson 12
Loan Disbursement Records	Loan Disbursement Summary Preparing a Loan Disbursement Summary Using the Loan Disbursement Summary	Form Instructions Lesson 13
Payment Records	Passbook Preparing the Passbook Individual Internal Account Loan Record Preparing the Individual Internal Account Loan Record Payment Activity Summary Preparing the Payment Activity Summary Using the Loan Payment Forms	Form Instructions Form Instructions Form Instructions Lesson 14
Dividends	Dividend Calculation Form Dividend Distribution Form Preparing the Dividend Calculation and Distribution Forms Using the Dividend Forms	Form Form Instructions Lesson 15
Cash Flow	Cash Flow Preparing a Cash Flow Using the Cash Flow Form	Form Instructions Lesson 16
Financial Status Bar Chart	Financial Status Bar Chart Preparing a Financial Status Bar Chart	Lesson 17 Instructions

Tool Set Name	Tools in the Tool Set	Type
Audit and Internal Control Policies and Practices		
Internal Controls	Internal Controls	Lesson 18
Agency Audits	Auditing a Bank, an Agency Overview	Lesson 19
	Operations Audit for Agencies	Checklist
	Preparing the Operations Audit for Agencies	Instructions
	Using the Operations Audit for Agencies Form	Lesson 20
	Operations Audit for Agencies, Findings and	Form
	Recommendations	
	Report	Instructions
	Preparing the Operations Audit for Agencies, Findings	
	and	Form
	Recommendations Report	Instructions
	Financial Status Audit for Agencies	Lesson 21
	Preparing the Financial Status Audit for Agencies	
	Using the Financial Status Audit for Agencies Form	
Agency Mini-Audits	Village Bank Health Checklist, for Agencies	Checklist
Bank Member Audits	Audit Procedures for Bank Members	Form
	Preparing the Audit Procedures for Bank Members	Instructions
	Auditing a Bank: Member Audit Guidelines	Lesson 22

Contributing Agencies

The following organizations contributed tools to the toolkit:

- Catholic Relief Services
- Foundation for International Community Assistance International (FINCA)
- Freedom from Hunger
- Project HOPE
- World Relief International

Overview of Internal Account Management

Overview of Internal Account Management consists of two sets of tools:

- Managing the Internal Account, an Overview
- Using the *Internal Account Management Toolkit*

Tool Set: Managing the Internal Account, an Overview

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To provide an overview of the issues involved in managing the internal account
Frequency	As part of initial training
Description	Lesson in defining vision for the village bank and a group discussion on management issues by category

Overview of Tools

Managing the Internal Account, an Overview (Lesson 1)

This lesson introduces the issues involved in managing a village bank's internal account. It takes approximately three and one-half (3.5) hours to complete the lesson.

Before you begin the lesson, you will need the following handouts (one for each participant):

- Three Versions of the Internal Account (L1-1)
- Types of Village Banks (L1-2)

In addition, you should have the following materials available: flipchart paper and markers.

Managing the Internal Account, an Overview (Lesson 1)

Vision and Purpose of the Internal Account

Ask participants to focus on *why* the internal account exists. Ask them to list the purposes of the internal account on a flipchart.

Ask three volunteers to come forward; give each one a short description of a village bank to read aloud (Handout L1-1). Each village bank described in the handout has adopted policies and procedures that correspond to different visions of the internal account in village banking.

Instruct participants to listen carefully to each description. After all have been read, the participants should then choose the description that best fits their idea of what the internal account should be and organize themselves into groups according to their responses.

Ask participants in these small groups to discuss their chosen vision and how it affects the operating policies and procedures. They should be prepared to summarize the discussion for the group, emphasizing their reasoning for choosing their vision.

The discussion should cover the various examples of options and practices for savings, loan policy, loan approval and qualifications described in Handout L1-2.

Overview of Internal Account Management Issues

Brainstorm with participants on the problems, conflicts and challenges that they have confronted in working with the internal accounts of the village banks they assist. Write responses on flipchart.

Group these responses by category, such as bylaws, internal controls, loan approval, recordkeeping, dividend policies, monitoring and audit.

Ask the following questions:

- Are you managing you banks adequately in all of these categories?
- Is there a single policy for each category that everyone can simply learn and apply?
- What influences the various policy options that your agency pursues?

Have one or two participants summarize the discussion for the group, pointing out major internal account management issues that are important to them.

Handout L1-1: Three Versions of the Internal Account

The *Tight Ship* Bank

When this village bank finally met the criteria for internal account lending as established by its agency, it made its first few loans. During the first two lending cycles, the bank made loans only to members in good standing according the criteria that the promoter from the agency helped to define. Loan size, loan terms and interest rates were set by the agency, which made the management committee's job easier; committee members didn't have to debate among themselves or with bank members.

The management committee members work with their promoter to review each loan and, in the process, they learn how to evaluate the potential success of an applicant's business.

After each meeting, the promoter helps the bank treasurer complete the forms that make up the internal account recordkeeping system. It includes many forms to clearly document the loans given out and all the money paid back.

The *Sleeping Beauty* Bank

This village bank steadfastly collects savings from its members that are then placed in the internal account. Members deposit their savings each week according to the program rules; the more the members save, the more they are eligible to borrow from the external account.

The village bank safeguards member savings and the internal account serves as a guarantee fund for the external account, in the event of a crisis that prevents the bank from repaying its loan.

No loans are made from the internal account. This policy is safer and less confusing. It concentrates all borrowing activity within the external account. If members need to increase their loans, they must save. This way, everyone wins—members' savings grow and the agency assures its own income and sustainability through growing loan sizes.

The *Loose Cannon* Bank

This village bank's internal account never rests. Local demand for loans is so strong that as soon as money comes in, it goes out in new loans. Eager to maximize their income, members set interest rates higher than the rates they pay on external account loans—and nonmembers pay even higher rates.

The money seems to be rolling in. But the bank has made a few mistakes, such as lending more than a borrower is able to repay and lending to strangers without demanding some form of guarantee.

Slowly, after they experience a few delinquencies, the village bank members learn to be more cautious with internal account lending. When the promoter initially suggested that they develop passbooks and loan records for internal account loans like those they keep for the external account, they did not think that so much paperwork was necessary. But now that lending has expanded, they are beginning to worry about losing track of which borrowers have paid and how much they have paid. They have asked the promoter to train them to keep simple books and she agreed because she has been warning them of the dangers of not closely tracking these loans.

Handout L1-2: Types of Village Banks

Savings Options

Amount Required	Link to Internal Account Loan	Access	Reserve
30% of external account loan 20% of external account loan 10% of external account loan 5% reserve	Required Optional Not required	End of cycle Anytime For emergencies or upon withdrawal Linked to amount of external account loan that can be obtained	50% of internal account 10% of external account

Loan Policy Options

Eligibility	Purpose	Loan Term	Loan Size	Interest Rate	Guarantees
Any member Member in good standing Nonmember	Production Emergencies House repair	= cycle length > cycle length < cycle length	Tied to savings Tied to external account loan	= external account rate > external account rate < external account rate Higher for nonmembers	Guarantor Collateral

Loan Approval Options

Who Approves	Factors to Consider
Village bank management committee	Applicant's eligibility
Loan subcommittee	Intended use of loan
Promoter and loan committee	Health of business
All members by majority vote	

Village Bank Qualification Options

Cycle	Other Qualifications
Second	Attendance = ___%
Third	On-time payment on the external account
Fourth	Savings = ___%
	Recordkeeping
	Arrears at end of cycle = ___%

Tool Set: Using the *Internal Account Management Toolkit*

Audience	Village bank management committee, bank members, agency staff in training
Purpose	Training on the use of the *Internal Account Management Toolkit*, with an emphasis on using the diagnostic. Quick reference; training on analyzing issues related to internal account management; guide to selecting tools for internal account management and decision-making
Frequency	As part of initial training; as needed thereafter
Description	Two lessons outlining the contents and purpose of the *Internal Account Management Toolkit*, including the diagnostic

Overview of Tools

Using the *Internal Account Management Toolkit* (Lesson 2)

This lesson introduces the elements of the *Internal Account Management Toolkit*. It takes approximately one (1) hour to complete the lesson.

Before you begin the lesson, you will need one copy of each of the following:

- Copy of *Internal Account Management Toolkit* document
- Overhead or flipchart of the toolkit's table of contents

Internal Account Diagnostic Tool

The internal account diagnostic categorizes the major policy issues involved in managing the internal account and presents the related tools, preparatory steps, recommendations and decision-making authority for each.

Using the Diagnostic to Analyze the Internal Account Management (Lesson 3)

This lesson provides guidance on using the Internal Account Diagnostic Tool. It takes approximately three (3) hours to complete the lesson.

You should have a copy of the Internal Account Diagnostic Tool for each participant, plus flipchart paper and markers.

Using the *Internal Account Management Toolkit* (Lesson 2)

Activities

Show participants a copy of the *Internal Account Management Toolkit* and explain each section in detail. You may wish to have certain tools and forms on overhead transparencies or flipchart paper to enhance the presentation.

Tell participants that they will practice using all forms and other tools.

Internal Account Diagnostic Tool (Analysis)

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Lending Policies and Practices						
Lending						Managing the Internal Account, an Overview
Initiation (when to start lending)	Initiate internal account lending when bank chooses to do so, after key procedures and bylaws are in place and members are trained.	Conduct bylaw training with members and introduce recommended policies.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws
		Adapt loan terms based on local experience and vote on final policies and procedures.	1 2 3			
		Adopt review and monitoring schedule and procedures.	1 2 3			
Eligibility	Initially, make loans exclusively to members; subsequently, loans can be made to members and nonmembers when internal account fund is sufficiently large.	Conduct bylaw training with members and review procedures for establishing eligibility.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Duration	Loan terms should not exceed the end of the external account loan cycle.	Review recommendations and establish policies and procedures in bylaws after soliciting local input on lending experience and practices.	1 2 3	4		Lending Practices and Loan Terms in the Bylaws
Interest	Flexible interest rate policy is determined by bank, with variations based on loan amount, term, purpose, type, guarantees and collateral; policy should be competitive with local market rates.	Introduce recommended lending terms and establish policies and procedures in bylaws after analyzing local market.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws
Repayment Schedule	Repayment should occur monthly, at a minimum.	Review repayment recommendations in accordance with local practice; incorporate policies and procedures in bylaws.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws
Amount	To minimize risk, no more than 25% of total loan fund should be placed in a single loan.	Introduce concept of risk and incorporate risk control policies in bylaws.	1 2 3	4	4	Lending Practices and Loan Terms in the Bylaws
		Establish regular review and monitoring process.	1 2 3			

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Guarantees	Require collateral if loan amount is large; personal guarantee at discretion of bank members.	Review recommendations and establish policies and procedures in bylaws.	1 2 3		4	Lending Practices and Loan Terms in the Bylaws
Loan Analysis and Approval	A majority of bank members should approve all internal account loans; additional loans should not be approved for members with existing loans.	Train members in credit and risk analysis; develop loan approval criteria and a loan review process; test criteria and process during initial loan cycles and adjust as necessary.	1 2 3		4	Loan Analysis and Approval Lending Practices and Loan Terms in the Bylaws

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Delinquency and Collection	Establish policies and control procedures aimed at avoiding delinquency.	Review delinquency and collection recommendations.	1 2 3		4	Delinquency and Collection Lending Practices and Loan Terms in the Bylaws
	Monitor troubled loans.	Train members in monitoring troubled loans, delinquency practices and control, and collection procedures.	1 2 3			
Cash Reserve	Establish a cash reserve from inception, unless bank has no access to a secure, deposit-taking institution; establish a conservative amount initially, then adjust amount based on performance, management capacity and inflation.	Review management capacity against standard performance indicators and set policy based on indicators.	1 2 3	4		Managing the Cash Reserve
		Conduct reserve training, stressing purpose of reserve and management practices.	1 2 3			
		Create procedure to review reserve amount based on portfolio performance.	1 2 3			

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Savings Policies and Practices						
Savings Practices	Establish programmed (commonly, 20% of external account loan amount) and voluntary savings policies, as well as limitations, if appropriate, on member withdrawals. Prohibit members from borrowing against savings, allowing exceptions on a case-by-case basis only.	Review recommendations and train members on importance of savings to the internal account and the community.	1 2 3		4	Savings Practices
		Solicit input from members on access policy.	1 2 3			
		Identify risk by analyzing bank policies for mobilizing savings.	1 2 3			
		Create policy on savings requirements, security and access.	1 2 3			

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Recordkeeping Policies and Practices						
Record-keeping Practices	Establish recordkeeping practices that are simple for members to maintain independently, and sufficiently comprehensive to provide required data for effective management by agency and bank.	Review recommendations, documents and recordkeeping procedures with members.	1 2 3	4	4	Keeping Records for the Internal Account, an Overview
		Adjust policies to fit member capacity.	1 2 3			
		Train members in recordkeeping practices.	1 2 3			
		Open commercial bank account, if possible.	1 2 3			
Lending Documents	Loan applications (for particularly significant or nonmember loans), loan contract with payment schedule, guarantee or collateral forms.	Review documents and practice procedures for their use and implementation at bank level.	1 2 3	4	4	Lending Documents
		Establish recordkeeping review and monitoring procedures.	1 2 3			

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Disbursement Documents	Passbook for borrower, loan disbursement summary form for bank.	Review documents and practice procedures for their use and implementation at bank level.	1 2 3	4	4	Loan Disbursement Records
		Establish recordkeeping review and monitoring procedures.	1 2 3			
Payment Documents	Passbook for borrower, individual internal account loan records and payment activity summary for the bank.	Review documents and practice procedures for their use and implementation at bank level.	1 2 3	4	4	Payment Records
		Establish recordkeeping review and monitoring procedures.	1 2 3			
Dividends	Base dividend calculations on beginning-of-cycle savings amount to create a savings incentive.	Train members on purpose of dividends and recommended practices.	1 2 3	4		Dividend Records
	Disburse dividends at the end of each cycle to simplify management and provide frequent returns for bank members.	Review dividend forms and ask members to calculate distribution to test understanding and capabilities. Adjust practices as necessary.	1 2 3			

Key: 1 = Not Started 2 = In Process 3 = Completed			Level of Completion	Decision-maker		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Financial Reports	Produce a cash flow and a financial status bar chart at the end of each bank meeting.	Train members to prepare a cash flow statement. Train members to prepare a bar chart.	1 2 3 1 2 3	4		Cash Flow Financial Status Bar Chart
Internal Controls and Audit Policies and Practices						
Internal Controls	Require multiple signatures to authorize and approve transactions. Use separate accounts for savings, interest income, and reserves. Retain adequate source documentation for all transactions, and use serially numbered documents. Use ink for all financial records. Transact all business in cash and during bank meetings. Rotate persons assigned to deposit cash and restrict access of account signatories to accounting records.	Train members on purpose of internal controls. Discuss specific controls with members; adjust as necessary. Develop system for members and promoter to validate controls on regular basis.	1 2 3 1 2 3		4	Internal Controls

Key: 1 = Not Started 2 = In Process 3 = Completed			**Level of Completion**	**Decision-maker**		
Issue	**Recommendation**	**Preparatory Steps**		**Agency**	**Bank**	**Tool Set(s)**
Agency Audits	Agency audit staff or independent contractors conduct audit program, including: Comprehensive, scheduled audits by agency at least annually; Spot (unannounced) audits using quick and easy tools; Mini-audit when full audits are not practical or possible.	Train members on purpose and definition of agency audit; review agency procedures. Conduct one audit; evaluate results and adjust procedures as necessary.	1 2 3 1 2 3	4		Agency Audits Agency Mini-audits
Internal (Bank Member) Audits	A program of routine (at each meeting) and spot audits conducted by bank members.	Train members in member audit practice, and to verify records using cash flow and financial status bar chart.	1 2 3		4	Bank Member Audits Cash Flow Financial Status Bar Chart

Using the Diagnostic to Analyze the Internal Account (Lesson 3)

Overview of the Diagnostic Tool

The Internal Account Diagnostic Tool provides an overview of the issues and recommendations in the *Internal Account Management Toolkit*.

The Diagnostic is laid out in six main columns. The first column, Issue, corresponds to the general topics in the policy manual and the tool sets in the toolkit. The second column, Recommendation, summarizes preferred practices. Preparatory Steps itemizes the actions that your agency and the village bank can undertake to implement the Recommendation. The Level of Completion corresponds to the Preparatory Steps, indicating the progress made in implementing them. Decision-maker identifies the entity (agency or bank) that is generally responsible for policy-making. The final column, Tool Set, lists the tool sets that are appropriate for each issue. These tool sets are developed to assist your agency and the village bank in instituting recommended policies and practices and to train agency staff and bank members.

Discussion and Activity

Develop Issue sheets (flipchart paper with the following titles: Lending, Loan Analysis and Approval, Delinquency and Collection, Cash Reserves, Savings Practices, Recordkeeping, Internal Controls, Audits) and display them on the walls.

Give participants markers and ask them to distribute themselves more or less evenly around the room in front of the Issues sheets. Under the subheading on each sheet, participants should write one possible response or policy option. When finished with the current sheet, each participant should move on to the next and repeat the process until every participant has written a response on every sheet. When participants are finished, have them take their seats.

Review the options that participants have listed on each sheet. Select a few of these options and ask the authors to defend their responses. Then, for each issue on the sheet, take a vote on the options listed. Try to make a connection between the options that participants preferred and the internal account vision they articulated earlier.

Conclude by explaining that the displayed issues are the same as those that are addressed by the tools in this toolkit. Agencies and village banks use these tools to introduce and improve management practices.

Lending Policies and Practices

Lending policies and practices consist of five sets of tools:

- Lending Strategies
- Lending Practices and Loan Terms in the Bylaws
- Loan Analysis and Approval
- Delinquency and Collection
- Managing the Cash Reserve

Taken together, the tools in these tool sets provide the means for establishing policies that govern your village banks' lending operations as well as for monitoring and enforcing their internal account lending practices.

Tool Set: Lending Strategies

Audience	Village bank management committee, bank members; agency staff in training
Purpose	To generate discussion among bank members on lending strategies and safeguards; build long-term vision
Frequency	During initial training; as needed thereafter
Description	Three-part tool includes group discussion of lending strategies, a game and two case studies to stimulate conversation on safeguarding funds
Strengths	Provides an opportunity for members to voice ideas and concerns; requires little preparation; flexible; can be used by new bank or bank experiencing difficulties
Limitations	Requires a good facilitator to ensure focus and equal participation

Overview of Tools

Lending Strategies and Safeguards

The exercise *The Money Game* is an optional exercise to explain the components of the internal account. The exercise is followed by two case studies to stimulate discussion on the importance of safeguarding funds.

You will need flipchart paper and markers, and a stack of local currency.

Lending Strategies and Safeguards (Exercise)

The Money Game

An Optional Exercise to Define the Internal Account

Where does the money come from?

Select eight volunteers to come forward. Give each volunteer real cash and tell her that the money is for one of the following (adapt this list to fit each bank's policies):

- loan principal owed to the agency,
- loan interest owed to the agency,
- savings (compulsory and voluntary) paid to the village bank,
- penalty and fines,
- additional loan interest owed to the village bank.

Place two boxes on a table in the front of the room. Label one "Agency Funds" and the other "Village Bank Funds" (or use pictorial symbols to represent the organizations).

Ask each volunteer to come forward and place her money in the appropriate box.

When everyone has deposited the money, ask for a volunteer to count the money in the village bank box. Ask participants to list the various sources of money that make up the village bank funds.

What can members do with these funds?

Brainstorm the following three options:

- depositing in the nearest commercial bank,
- lending out in short-term loans,
- investing in a community-run business.

Divide participants into three groups and assign each group one of the above options. Ask each group to discuss the benefits and risks of the option. The group should answer the following questions in the process:

- What are the opportunities to earn a profit?
- What are the risks associated with the option?

Have each group prepare a brief presentation to sell it to the members.

Have the groups present the results of their discussions. Ask members to vote on the option they prefer.

What rules govern the use of the funds?

Explain that if the bank chooses to make loans from its internal account funds, it has a number of decisions to make about the rules governing its lending. For example, bank members must decide if nonmembers are also eligible for internal account loans. Brainstorm other rules that will help the bank to operate its internal account. List responses.

Explain that these rules are called bylaws. The bylaw discussion guide presents all the decisions members need to make and provides the options for each rule. The rest of the training session focuses on these decisions and tries to identify the rules participants want to establish for their banks.

Case Studies: Importance of Safeguards for the Internal Account

(The following copyrighted case studies are reproduced with the permission of Freedom from Hunger.)

Briefly describe the case studies below (or act them out).

Ask village bank members to identify issues in the case studies that they consider to be problems in their own internal accounts, plus those they feel are important to address before a bank begins internal account lending.

Case Study One

Village Bank A wanted to make money quickly and easily. The members were very excited about the big profits they and their fellow members would make. They knew that they could earn more by loaning money at 10% per month, rather than by depositing it into the commercial bank. So, every meeting they loaned out all of their savings and other internal funds; they maintained no cash reserve. They would lend to almost anyone. If not enough members asked, they turned to nonmembers who did not save with the village bank. They never asked for a business plan, collateral (no matter what size the loan), or a personal guarantee. Their primary concern was to lend the funds out each week in order to earn interest. They would never give to a member in need of funds for emergencies (illness, fire, crop failure) because they only wanted high interest-bearing loans. They never followed up to see how the money was spent. They allowed members to take out loans at rates that were four times as high as their external account loans. They even gave a loan to one member who gave it to her husband to buy a bicycle, although the loan was for more than the price of a bicycle.

Village Bank A’s delinquency rate on its loans was almost 50%. Of course, they were not sure of exactly how much they had lent out and to whom. Their records were on paper scraps and many had been lost.

Despite their high hopes, not only did these bank members fail to earn the profit they had hoped for, they also lost much of their savings.

Discussion Questions
Ask participants to answer the following questions:

- What did the bank do wrong?
- What bank practices may have been good ideas, but were poorly managed?
- How would you help this bank?

Case Study Two

Village Bank B also wanted to make money by investing the internal fund for the benefit of its members. But they decided to do it through carefully considered and closely managed loans. They were especially careful during the first cycle as they gained experience. Some members did not want to lend out anything, but others felt that a small amount could be lent out to test policies and potential members of the group. They did maintain a cash reserve (at the agency's request) for bad debts and emergencies. This money was needed once when a member suddenly died and her family could not repay her loan. Assigned members of the group followed up on all loans. This practice was to safeguard the funds and to help the borrower in case she needed assistance. The bank never gave a loan to a member if the member's existing external and internal account loan payments were not up to date. When the bank president needed money but was having trouble with her first internal account loan, the members carefully explained that although they could not loan her more from the internal account, they would help her find a way to repay her debt. They always carefully considered each loan request to see if the member could repay within the cycle and never gave one person too much of the fund. Members and nonmembers borrowed, but all had savings in the bank or some other type of guarantee. Accurate records were kept on each loan. The agency assisted the management committee with recordkeeping at first, but after a few cycles, the bank members were able to do it themselves.

This bank was a success. As confidence in the bank grew, more and more people in the community saved with the village bank. The bank members earned small but regular profits that grew over time, and their savings were secure.

Discussion Questions

Ask participants to answer the following questions:

- Why was this bank a success?
- What difficulties did this bank face and how did they overcome them?
- What bank practices do you agree with? Disagree with?

Conclude by stressing that to achieve the major dreams and goals of the bank, members need to agree on the rules that will govern the bank—the bylaws.

Tool Set: Lending Practices and Loan Terms in the Bylaws

Audience	Village bank management committee, bank members; agency staff in training
Purpose	To provide an overview of lending practices and detailed discussion of various loan terms to be determined in the village bank bylaws.
Frequency	Upon bank formation; as needed thereafter
Description	Set of short forms to guide discussion of bylaws; includes examples; lesson
Strengths	Simplicity, ease of use; comprehensive; allows implementing agencies to establish standard requirements
Limitations	Requires a good facilitator who is well versed in each option and able to direct the discussion without imposing personal preferences

Overview of Tools

Loan Policies (Discussion Guide)

This small-group discussion covers issues of internal account loan eligibility, purposes, duration and maximum loan amount.

Selecting an Interest Rate (Exercise)

This tool presents three case studies covering interest rate options, and includes a set of questions as a follow-up to each.

Selecting a Repayment Schedule (Exercise)

This two-part role play presents two opposing scenarios for establishing repayment schedules to encourage debate, and follows with a series of questions for the group.

Establishing Sanctions (Exercise)

This exercise includes a role play to help bank members establish late-payment policies that reflect the style of the village bank.

Bylaws Decision Tool (Forms)

This tool consists of a series of small forms designed so that members can fill in blanks or check boxes to determine policies for the bylaws.

If your agency has standard policies that you require to be incorporated into the village bank bylaws, fill in the forms prior to the bank member discussion, and clearly explain the impact of these policies during the meeting. However, when it is important that the village bank choose the policy in order to maintain a sense of ownership and responsibility, your agency should simply recommend practices.

Bylaws Discussion Guide (Lesson 4)

This lesson introduces the concept of bylaws and outlines the various lending policies governed by the bylaws.

It takes approximately three (3) hours to complete the lesson if it is presented as part of a larger training seminar. If you conduct the lesson during village bank meetings, you should only discuss two or three issues at each meeting.

Before you begin the lesson, you will need a copy of the Bylaws Decision Tool, for each participant. In addition, you (or your promoter) should be familiar with the information contained in the Internal Account Diagnostic Tool as a guide to recommended practices.

Loan Policies (Discussion Guide)

Begin by dividing the members into small groups and assign each group one of the following questions (each corresponds to a previously identified loan policy):

- Who is eligible for an internal account loan?
- For what purposes can internal account loans be used?
- What is the loan term (duration) for internal account loans?
- What is the maximum amount of an internal account loan?

Ask the groups to discuss the answers to the questions and to formulate recommendations.

Ask each group to present a brief report on its discussions and policy recommendations.

Now, ask for three volunteers to serve on a village bank loan committee. Tell them that their jobs are to review each of the following loan applications and decide whether or not to grant them a loan from the bank's internal account fund.

Ask for eight more volunteers to be the loan applicants. One by one, each will present a loan application. The loan applicants can read their descriptions or you can read each applicant's description as she comes forward.

The loan committee has five to ten minutes to discuss each application and then must announce a decision. While you ask the questions necessary to clarify the reason for the decision, ask an assistant to record the main reasons for acceptance or rejection on a flipchart.

Sonja

Sonja is a village bank member in good standing. She comes to every meeting and always pays on time and in full. She is hardworking and dependable. Now, she has a good opportunity to go into business with her sister-in-law and is asking for a loan of 200, which is twice the amount of her current loan from the external account.

Soledad

Soledad is the bank president's cousin; she has just moved to the town and is eager to set up a stall in the market. The bank president vouches for her honesty and eagerness to work hard.

Rosa

Rosa is a bank member who asks for a loan from the internal account to revive her business. Although bank members truly like Rosa, they are quite surprised to see her today because she has missed the last three village bank meetings. First, she went to visit her sick mother and, then, for the last two meetings, sent word that she was simply too ill to attend. In each case, Rosa sent her payment with a neighbor.

Angelina

Angelina's daughter has been sick for a long time, but Angelina is determined to continue coming to village bank meetings. She only misses a meeting if her mother cannot stay at home to watch the sick daughter. But she is not able to keep a food stall in operation at the market as she once did. She has missed three loan payments. Now, she is asking for an internal account loan to revive her market food stall. She plans to hire a girl to attend the stall for her.

Amalia

Amalia, a member in good standing, is asking for a loan to pay her children's school fees.

Maria

Maria, a member in good standing, is asking for a loan from the internal account for the same amount as her external account loan. She needs the money to expand her brick-making business.

Julia

Julia is a very dynamic member in good standing. Everyone is impressed with her clever business ideas. Now, she wants to take advantage of the carnival that is coming to town to make and sell special carnival t-shirts. If she gets the loan, it will be her second loan from the internal account. Her first loan is due in one month.

Mercedes

Mercedes is another member in good standing. She needs a loan equal in size to her external account loan. However, she needs to keep the money for longer than one cycle. Mercedes proposes to pay in full after two cycles.

After the loan committee announces its decision on each of the above applicants, you can choose to ask the observers if they agree with the decisions. This will take more time, but it engages the whole group.

Selecting an Interest Rate (Exercise)

"What interest rate should we charge?" Stories from Other Village Banks

Read the following case studies describing how other village banks have established the interest rates for their internal account loans.

After reading and discussing each story, ask the following basic questions to ensure that everyone understands the bank's policy.

- What interest rate did this village bank choose?
- Is this rate higher or lower than your agency's? Why?
- Does this bank charge one interest rate on all loans or different rates for different types of loans?

Take a vote to determine the interest rate policy that members like the best.

Divide members into groups according to their votes and ask each group to prepare a presentation that convinces the others of the superiority of the group's chosen policy.

Mothers United

When the village bank "Mothers United" decided to begin lending its funds to the community, it set its interest rate to be the same as the external account interest rate (or substitute appropriate terminology). Since the rate for agency loans is 2% a month, all borrowers from the internal account also pay 2% a month. This way, members believe, no one will be confused about the rate and everyone will easily accept it.

Women for Progress

The village bank "Women for Progress" has set its interest rate lower than the external account rate. The members are eager to make money and want to make it easy for members to borrow. They believe that the agency loans are strict enough. They want their internal account—which is, after all, their own money—to be a more flexible source of credit for members. However, for nonmembers, they set interest rates at two points above the external account rate.

Bank of the Future

"Bank of the Future" is also eager to make as much money as it can. But it does not want to take too much risk with members' savings. So it has decided to charge a higher interest rate than that for external account loans. It will also charge different rates for different types of loans: 4% on loans for business purposes; 5% for consumption and emergency loans. Nonmembers are charged an additional 1% to discourage people who may not be able to repay. Fewer people will borrow money, but those who do pay a higher rate, keeping the bank's income high.

Selecting a Repayment Schedule (Exercise)

Before the session, find two volunteers who are capable of portraying the role of a village bank president and explain their roles to them.

Ask them to act out a debate (as described below) during which each defends her assigned position.

Role for Bank President One

You believe that the management committee of your bank must maintain tight control over internal account lending in order to reduce the risk to members' savings.

You insist on weekly repayment of principal and interest because of the following:

- smaller, frequent amounts are easier to repay,
- weekly payments allow the management committee to discover problems early,
- weekly payments keep a steady flow of money coming back into the bank's internal account,
- less control is just too risky.

Role for Bank President Two

You believe strongly that your bank's internal account funds should be available to serve the varied needs of its members.

Your members have voted for maximum flexibility with internal account funds. You insist that internal account loans be repaid in one lump sum (a balloon payment) at the end of the loan term because of the following:

- access to savings is very limited, so loans for various purposes must be available to members,
- some types of loans are difficult to repay quickly, such as those for emergencies or fixed assets,
- members are already forced to make more frequent payments on the external account loan,
- no one will borrow if the terms of repayment are too strict.

Questions

After the debate, facilitate a discussion wherein participants talk about what they saw and heard. Use the following questions to help generate the discussion:

- How would you describe each approach?
- Is one approach stricter than the other?
- Which approach is more flexible?
- Which policy is riskier? Why?
- Which approach offers more flexibility to members?
- Which is more important to you: flexibility, access to credit or greater protection for your savings?
- What are other options for repayment that these two bank presidents did not consider?

Establishing Sanctions (Exercise)

"What can we do about borrowers who are not paying?" A Role Play

Brainstorm with participants on the various actions the village bank can take against those borrowers who do not make timely payments on their internal account loans. Discuss the advantages and disadvantages of each possible action.

Conduct two different role plays of a credit officer (or management committee member) visiting a delinquent borrower. In the first one, the credit officer is very terse and demands the money outright. In the second, the credit officer is polite, asks after the family and the business in an effort to find out why the member has not paid.

After the two role plays, discuss the differences with participants and ask them to choose the style they think will be the most effective for their banks.

Bylaws Decision Tool (Forms)

How does our village bank want to use the internal account funds?	Decision and Date
Discussion Points (*Check as many as apply)*	
Lend out as loans	____________________
Keep in bank for interest	____________________
Invest in group business	____________________
Other	____________________

If our village bank is going to lend out the internal account, when will we begin?	Decision and Date
Discussion Points	
When we have _____ amount per member in the internal account	____________________
Once the committee and members have received training in internal account loan analysis and monitoring	____________________
Immediately, due to lack of secure place for funds	____________________
Other	____________________

Loan Eligibility: Who can receive an internal account Loan?	Decision and Date
Discussion Points *(Check as many as apply)*	
Members in good standing	____________________
Community members	____________________
Needs reference or guarantee	____________________
No outstanding internal account loans	____________________
Agency staff is NOT eligible	____________________
Other	____________________

Loan Amounts or Levels: How much can a person borrow at one time?	**Decision and Date**
Discussion Points	
Borrowers must have ____ in savings	________________
Maximum of ____% of total funds available for one loan	________________
Can not exceed last or current external account loan	________________
Linked to loan purpose	________________
Other	________________

Loan Terms: Under what terms or conditions is a loan made?	
For Members:	
Duration	________________
Interest	________________
Repayment Schedule	________________
Fees	________________
Guarantee	________________
Other	________________
For Nonmembers:	________________
Duration	________________
Interest	________________
Repayment Schedule	________________
Fees	________________
Guarantee	________________
Other	________________

Dividends: Does our village bank want to divide up profits?	**Yes___ No ___**
If Yes, how are dividends calculated and distributed?	**Decision and Date**
Based on beginning savings	________________
Disbursed at end of cycle	________________
Other	________________

Audit: How often will members conduct an internal audit and how?	**Decision and Date**
Discussion Points *(Check as many as apply)*	
Members should have formal, but short, audits each cycle	____________
Members should conduct check on books at any time there is a question	____________
Use member audit guidelines	____________
Other	____________

What types of loans should be approved for an internal account loan?	**Decision and Date**
Discussion Points	
Working capital to supplement external account loans	____________
Emergency loans	____________
Consumption loans	____________
Other	____________

Delinquency: What will we do if someone does not repay her internal account loan?	**Decision and Date**
Discussion Points	
Freeze savings	____________
Send committee to borrower's house to investigate	____________
Require guarantor to pay if applicable	____________
Reschedule loan if appropriate	____________
Take legal action if appropriate	____________
Other	____________

Reserve: How much of our internal account will be reserved in cash?	Decision and Date
Discussion Points	
___% for the first year	____________
To be adjusted according to internal account performance and reserve	____________
Reschedule loan if appropriate	____________
No reserve due to security reasons	____________

Bylaws Discussion Guide (Lesson 4)

This lesson presents several policy options in the bylaws for group discussion.

Explain that bylaws govern the management of the village bank's internal account. They provide an objective policy guide for members when issues arise. However, the bylaws are meaningful only if they are understood, followed and enforced by the group who collectively agreed upon their implementation. Village bank members should collectively discuss the various policy options to be incorporated into the bylaws and, ultimately, reach agreement on a set of bylaws for their bank.

For many of these policies, the group may wish to decide only on broad parameters. For example, the loan term section of the bylaws may state minimum or maximum parameters only. Individual borrowers will have specific terms within these parameters.

Present each of the forms in the Bylaws Decision Tool on overhead or flipchart paper and discuss the options with bank members.

Then, present the sample exercise forms below, and discuss the implications of each choice, guiding members in establishing best practices and ethical lending behaviors.

Ask the following questions:

- Can these decisions be changed?
- How often?
- How long do you propose to work under these rules before they are changed?

Finally, complete the Bylaws Decision Tool based on the final policies agreed upon by the bank membership.

Example 1: Use of Internal Account Funds

This group has decided to lend out the internal account instead of keeping it in the bank or investing in a group business. If a village bank wanted to lend out some and invest some, they could check both options.

How does our village bank want to use the internal account funds?	Decision and Date
Discussion Points: *Check as many as apply*	
Lend out as loans	4
Keep in bank for interest	
Invest in group business	
Other	

Example 2:

This group decided to wait until there is a certain amount of money in the internal account and they want to have some basic training in internal account management. Other groups may wish to lend out all of the internal account right away since there is no safe place to keep funds.

If our village bank is going to lend out the internal account, when will we begin?	Decision and Date
Discussion Points:	
When we have 5.00 per member in the internal account	4
Once the committee and members have received training in internal account loan analysis and monitoring	4
Immediately, due to lack of secure place for funds	
Other	

Example 3:

Here the group has decided to lend to village bank members and community members at large. However, the program has chosen the policy that no staff are eligible for loans and no person with a previous outstanding internal account loan can get another one.

Loan Eligibility: Who can receive an internal account loan?	Decision and Date
Discussion Points: (check as many as apply)	
Members in good standing	4
Community members	4
Needs Reference or guarantee	
No outstanding internal account loans	4
Agency staff is NOT eligible	4
Other	

Example 4:

In this issue the village bank decided that to borrow from the bank, you must save with the bank and that the amount of the loan will depend on the purpose of the loan. This is a very broad policy that can then be tailored to individual cases. In this example, the program has decided the additional policy that no one loan can be greater than 25% of total funds available. Below each option, there is additional space to write in more detail.

Loan Amounts or Levels: How much can a person borrow at one time?	Decision and Date
Discussion Points:	
Borrowers must have 5.00 in Savings All borrowers must save with the bank	4
Maximum of 25% of total funds available for one loan	4
Can not exceed last or current external account loan	
Linked to loan purpose	4
Other	

Example 5:

The loan term issues are another example of where minimum or maximum policies are established but there is flexibility within the restriction. Often internal account loan terms vary with each case. This form allows them to set up broad or very specific terms for the internal account.

The Bylaws Decision Tool also contains decision boxes for dividend distribution, audit procedures, delinquency and reserves.

Loan Terms: Under what terms or conditions is a loan made?

For Members:	
Duration	No later than end of loan cycle
Interest	No more than 5%/month
Repayment Schedule	At least interest is paid monthly
Fees	10% of loan for late payment
Guarantee	For loans greater than X amount
Other	
For Nonmembers	
Duration	No later than end of loan cycle
Interest	No more than 7% a month
Repayment Schedule	At least interest is paid monthly
Fees	15% of loan for late payment
Guarantee	A personal guarantor is required
Other	

Tool Set: Loan Analysis and Approval

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To enhance loan evaluation and analysis techniques
Frequency	As part of initial training; as needed thereafter
Description	Series of questions and a role play to develop loan analysis skills; comparative analysis of external and internal account indicators
Strengths	Fosters objectivity and factual analysis among bank members; format encourages discussion among group members and borrowers
Limitations	Can be lengthy, therefore may only be appropriate for larger loan requests or when members are concerned about a borrower's ability to repay; not applicable to emergency or consumptive loans. Village banks that routinely divide the internal account and lend it out in equal amounts for security purposes should not use this tool because it is too time consuming.

Overview of Tools

Loan Feasibility (Analysis)

Over time, the loan approval process can evolve into an automatic-approval process. This can result from bank members' familiarity with the applicants' businesses, deference to the potential borrowers or lack of skills required to properly analyze loan requests. Whatever the reason, the process to approve an internal account loan requires a thorough analysis of the loan request, especially if the loan is a large one or the applicant has a bad credit history.

The Loan Feasibility Analysis guides the village bank's management committee and members in analyzing loan requests by evaluating both the viability of the applicant's business and her past payment performance. The questions can be used to evaluate applications for either internal or external account loans for productive purposes. The format of the questions encourages discussion, as opposed to automatic approval. If members are very confident of the applicant or are knowledgeable about her business situation, the discussion may be a short one. However, if the applicant is new to her business or members are unsure of her abilities, this analysis provides a way to begin the discussion.

This discussion can also help the applicant to analyze her business.

The management committee or a designated member can pose the questions to the applicant. All interviews should take place in front of the entire membership. The discussion can become quite lengthy; therefore your promoter or facilitator should try to limit each question to five minutes, unless the members feel that further time is absolutely necessary.

A formal analysis requires that the bank record the applicant's responses in writing (for literate members) or icons (for members who cannot read). If the applicant provides satisfactory answers, the committee can proceed to prepare the loan contract.

Analyzing Loan Feasibility (Lesson 5)

The role play and discussion guide in this lesson are designed to introduce participants to the process of evaluating internal account loan requests. It takes approximately two (2) hours to complete the lesson.

Handout L5-1: provides fictitious loan applicants for the role play. In addition, you will need flipchart paper and markers, or an overhead

Tough Love (Lesson 6)

It is often difficult for members to say "no" to each other. The Tough Love lesson explains why it is important to say no, even if it is difficult at times. It illustrates why bank members must be held responsible for their actions and also why members must, at times, take responsibility for each other's actions.

This lesson can be used in conjunction with loan analysis training and as a follow-up to bylaws training.

The lesson takes about thirty (30) minutes and involves role play. Specific instructions are built into the lesson.

Loan Feasibility (Analysis)

(The following copyrighted loan feasibility analysis material is reproduced with the permission of Freedom from Hunger.)

Questions

The following set of questions can be used as a guide for interviewing loan applicants. Village bank members should carefully consider an applicant's answers before approving a loan.

- What skills or experience do you have to make the business a success?
- Why do you think the materials needed for the business will be available when you need them?
- How can you show that this business will be profitable?
- To whom will you sell your product or service?
- Who is your competition?
- Will you be able to sell more if you receive the loan, and why?
- How does your business allow for regular loan repayments?
- What is your plan to pay back the loan if there is a problem with the business?

If the applicant provides satisfactory answers to each of these questions, the village bank should prepare a loan contract.

Applicant Response Summary

Bank members can us the following table to record an applicant's responses:

Category	Strong	Moderate	Weak	Don't Know
Skills/Experience				
Access to Materials				
Profitability				
Market and Customers				
Competition				
Contingency Plan				

Analyzing Loan Feasibility (Lesson 5)

Explain that you are an international expert from a very important organization and you want to understand how a village bank works. You are especially interested in the internal account and how the bank members manage it. Ask participants to imagine that they are all members of the village bank management committee.

You politely request permission of the "management committee" to ask them a few questions. Most of the answers will be "yes," "no," or "maybe." Anyone who has an answer may simply call it out.

Role Play Questions

Would you approve a loan if the applicant fits any of the following:

- can clearly show that the cost of materials is far less than the going price for her product;
- fails to present a business plan;
- is just starting a business for the first time;
- is a very important person in the village but doesn't have the skills necessary to operate the business;
- presents an idea for an interesting product, but doesn't know where or how she would sell it;
- does not have collateral;
- wants a loan to start a teacake business when three other bank members are already making and selling teacakes;
- doesn't really know how much it will cost to make her product;
- faces a lot of competition, but can explain clearly how her product is different;
- is the most powerful member of the village bank but resists giving out information about her business.

Discussion

Thank the management committee for answering your questions. Then step out of character and note anything odd about the process.

- Did everyone answer the same way?
- Are there definite right and wrong answers to these questions?
- Would a set of guidelines for approving loan requests be helpful?

Brainstorm with participants about the information bank members should know when evaluating a loan request. Remind people that in this instance, we are only interested in information about the business, not about the applicant's status in the village bank.

List responses on a flipchart. Group them by major categories, such as relevant experience, market and profitability.

Explain that the Loan Feasibility Analysis tool is a set of questions bank members should ask potential borrowers when evaluating a loan request. Present the tool on an overhead or flipchart.

Role Play

Divide participants into small groups and ask them to role play interviews between the management committee and the loan applicant for an internal account loan. (Agency practitioners can base their role playing on one of the fictitious applicants in Handout L5-1. Village bank members may prefer to conduct the interview in relation to their actual businesses.)

Based on the applicant's answers, prepare an applicant's response summary form (included on the Loan Feasibility Analysis tool).

Discuss and determine whether the loan request should be approved.

After the groups have carried out their interviews, discuss the experience with everyone by asking the following:

- How did it feel to ask these questions?
- Do you feel uncomfortable asking for such detailed information?
- Why is it important to know something about the business that the loan will support?
- Did anyone decide to turn down a loan request? Why?
- Has this ever happened in your village bank?
- What happens when someone's request is denied?
- Has your bank ever made a bad loan decision? What happened?
- What could your bank have done differently?

Handout L5-1: Fictitious Loan Applicants for Role Play

Loan Applicant One: Angela

Angela is a seamstress with her own sewing machine. For several years her business did well by making school uniforms for the local children. But now a shop in town carries factory-made uniforms for a lower price than Angela's. Angela proposes to change her business and make children's clothes from second-hand clothing that she buys in bulk. She wants a loan from the internal account to purchase the first bale of second hand clothing. Angela figures she can make 50 little girls' dresses from the first bale of clothing in three weeks time. If she sells all of these, she will double her money. Her sister, who lives in another town 50 miles away, has agreed to sell some of the dresses there. Angela has a deal with a vendor for delivery of the first bale of clothing, but she doesn't know how often he has second-hand clothing to sell, or what the bales contain specifically. Currently, he is her only contact for the supplies she needs. In addition to this income, Angela continues to get some orders for adult clothing, but not enough to sustain her family.

Loan Applicant Two: Beatrice

Beatrice is the village bank president's sister and a founding member of the village bank called "Progress." She contributed a great deal of her time and energy to the village bank and likes to call it "her little bank." She uses her loans from the external account to support a food kiosk, which she maintains in the market. It employs several young women in the village. Now, Beatrice wants to borrow from the internal account to go into business with her uncle who lives in another town. He wants to purchase cellular phones and set up phone booths where people can make calls for a fee. This is a novel idea about which Beatrice is really excited. However, she doesn't have much information about the cost of the phones or the fees to be charged for the calls. Beatrice can only assure her bank members that everything is moving ahead rapidly. She will get all the information they want soon. Meanwhile, her brother is still negotiating with the authorities for a permit for the phone booths; Beatrice insists that she needs the money today.

Loan Applicant Three: Miraji

Miraji uses her external account loan to finance her vegetable stall at the market in town. Now, she is asking for a loan from the internal account to raise chickens in time for the special holiday in three months time. She can use her mother's poultry house to raise the chickens and has an order for the full grown birds from a local hotel. Although Miraji hasn't taken care of chickens since she was a girl, her mother will help her. Her mother knows about feeding, medicating and keeping the poultry house at the right temperature. Miraji admits that her mother hasn't kept poultry in years and she is not certain what repairs the family poultry house might need.

Tough Love (Lesson 6)

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Defining Tough Love

Tell the group that the discussion will focus on the importance of saying no to another member's request for a questionable loan, even though it is sometimes difficult to do so.

Tell the following story (or make up another that is more culturally appropriate).

> *A three year old child is about to put her hand in the fire. The mother slaps the child hand away from the fire quickly to prevent her from being burned. The child begins to cry.*

Ask: Does the mother love the child? Why did she slap the child's hand?

Explain that there are two ways the child can learn the danger of fire: by putting her hand in the fire and getting burned or by having her hand slapped and being told that fire is dangerous.

Ask: Which method do you think is better for the child? Why?

Ask the group to suggest other examples of tough love that participants (as parents or friends) have experienced.

Discuss why it is sometimes hard to use tough love, but also why it is sometimes quite necessary.

Ask the members to name situations where they may need to say no to another member's ideas or actions.

The list might include the following:

- a loan request for a business activity that would not be profitable,
- absence from many meetings in a row without a good excuse,

- arriving late to the meetings week after week,
- skipping regular payments every other week,
- failing to make regular savings deposits.

Practicing Tough Love

Explain that this kind of tough love must be practiced during the loan analysis/approval and at other times during the loan cycle. Members must deny loans for ideas that are not profitable in order to protect the applicant and the other members from loan repayment problems. Members must also deny a loan request when the applicant is not following the rules and bylaws. Tough love keeps the village bank strong and eligible for continuing credit and other services from the agency.

Have the members form small groups. Explain that everyone is now going to practice tough love. Members of each group will be asked to manage a situation that might one day occur in their village bank. One representative from each group will be given a situation to present to her group. She will play the role of a village bank member who is not following the rules or bylaws. The group will have ten minutes to do the following:

- discuss the situation with the person playing the role,
- reach a decision about how they will manage the situation,
- report on how they plan to manage the situation.

Ask a representative from each group to come forward and assign each one of the following situations to enact. She is to return to her group and play the role of a member and present the situation she has been assigned (choose from the roles below):

- request a loan for a business activity that would not be profitable,
- be absent from many meetings in a row with no good excuse,
- come late to the meetings week after week,
- skip regular payments every other week,
- fail to make regular savings deposits.

The representative goes back to her group and presents the situation she has been assigned. Walk among the groups and offer to help if they are having trouble with the exercise.

After 10 minutes ask members to give reports, as follows:

- describe the situation,
- report their plan for managing it,
- describe how it felt to say “no” to another member.

After all groups have reported, ask participants what they might do to improve the practice of tough love (be respectful, establish clear policies and practices, be consistent in the application of rules and penalties).

Tool Set: Delinquency and Collection

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To develop noncompliance policies for internal account loans, and methods for monitoring and addressing late-payment issues
Frequency	Delinquency and Collection Checklist, Lessons: as part of initial training; as needed Troubled Loan Report: every cycle
Description	Delinquency and Collection Checklist: policy checklists and discussion guides for preventing loan delinquencies and managing existing delinquencies Troubled Loan Report: simple tool to report internal account loans not repaid at end of cycle, based on data from the village bank's account books and completed by the bank's management committee or promoter
Strengths	Delinquency and Collection Checklist: Short; practical; allows for additions and expansion based local experience Troubled Loan Report: Simple to complete; provides an internal control; informs bank members of borrowers' payment problems; provides promoters with information on future training requirements
Limitations	Delinquency and Collection Checklist*:* limited testing; may require more structure Troubled Loan Report: may not be appropriate for all cultural settings; may be too time consuming during meeting if the bank's books are poorly organized

Overview of Tools

Delinquency and Collection (Checklist)

This tool includes both a delinquency avoidance checklist and a list of possible actions to be undertaken in the case of noncompliance. Your promoter should discuss the following checklist with the village bank members in order to determine the adequacy of their policies and explain that any inadequacies may affect future delinquency rates.

The latter should be displayed at the village bank to inform members as to past and planned future collection activities. In theory, nonpayment is always unacceptable; however, the internal account often fulfills a social role as well as an economic one. In some circumstances the bank members may find it appropriate to support a member in need by refinancing or forgiving a delinquent loan.

When training members to use these checklists, you may want to conduct role plays to illustrate costs and benefits to both the bank and its borrowers. You can adapt this tool to reflect local customs, as necessary.

Collecting Delinquent Loans (Lesson 7)

This lesson presents a scenario for group discussion and includes a review of the Delinquency and Collection Checklist Tool. It takes approximately thirty (30) minutes to complete the lesson.

Before you begin the lesson, you will need one copy of the Delinquency and Collection Checklist Tool for each participant.

Create a copy of the follow-up steps from the checklist that you can present on a blackboard, overhead or flipchart.

You will also require a blackboard, overhead, or flipchart paper and markers.

Troubled Loan Report (Form)

The troubled loan report is a simple tool to track loans that are not repaid by the end of a cycle. It allows your program managers and promoters—and village bank's members—to view overdue loans, the total at-risk amount and any recent actions taken to collect those loans. It provides information on the total portfolio at risk, as well as the dates of late payments.

The report is prepared at least once per cycle by your promoter or the bank's management committee. It is based on the bank's internal account records. The information is updated at the end of the next cycle; loans that remain delinquent are carried over to a new report. When a borrower repays at midcycle, the most recent report is updated to show the date the loan was repaid and the number of days it was overdue.

The reports should be stored with the village bank's records and at your agency to monitor late internal account loans.

While village bank practices vary widely, your promoter should review the total amount of internal account loans disbursed during the cycle and the total amount repaid by the end of the cycle. All internal account loans should be due and repaid by end of cycle.

Reporting on Troubled Loans (Lesson 8)

This lesson discusses the issues and practices involved with late-payment monitoring and explains the use of the troubled loan report. It takes approximately thirty (30) minutes to complete the lesson.

Before you begin the lesson, you will need copies of the following handouts:

- Sample Payment Data / Friendship Village Bank (L8-1)
- Sample Data / Case Studies for the Friendship Village Bank (L8-2)
- Solution to Sample Problem, Troubled Loan Report (L8-3).

Delinquency and Collection (Checklist)

The best way to minimize the risk of delinquency is to implement sound policies and procedures. Does your village bank do the following?

Delinquency Avoidance Checklist	Yes	No
Minimize commingling of external and internal account funds	❑	❑
Follow a systematic process for loan analysis	❑	❑
Require that all loans be repaid by the end of a cycle	❑	❑
Require frequent payments on internal account loans if possible	❑	❑
Disallow multiple loans to a single borrower	❑	❑
Implement a monitoring system to track late payments	❑	❑
Require that all transactions take place at a meeting, and in cash	❑	❑
Use a loan contract , especially for nonmember borrowers	❑	❑
Charge fees or penalties for late payments	❑	❑

Follow-up to Noncompliance

The following are recommended actions for following up on delinquent loans:

Follow-up Steps in the Event of Delinquency or Noncompliance	Date Completed
Discuss the problem openly with all bank members at the first available meeting.	__________
Establish an immediate course of action at the meeting, so that it can be followed up on at the next meeting. The plan can always be modified later, if necessary.	__________
Freeze the delinquent member’s savings and restrict her access to future internal or external account loans, until the delinquency is fully repaid.	__________
See if borrower has other collateral that she can pledge until the delinquency is repaid.	__________
Work out a rescheduling plan with smaller payments and/or extended schedule. Any new terms should require specific performance on targeted dates and be closely monitored.	__________
If the borrower does not attend the meeting, the following steps should be taken:	
The management committee or other bank members should visit the borrower’s home.	__________
In the process, they should evaluate the borrower's home and business situation to discover the cause of the delinquency. This may require more than one visit.	

Follow-up Steps in the Event of Delinquency or Noncompliance	Date Completed
Visit 1: ______________________	
Visit 2: ______________________	
Visit 3: ______________________	
Report back to the bank as to nature of problem and the course of action to be taken	

If you do not receive payment after implementing the above recommendations, you have the following possible courses of action:

Possible Actions for Collecting Late Payments	
Reschedule	Negotiate a new payment schedule
Forgive	Repay loan using bank's reserves or member contributions
Write off	Repay loan using bank's reserves and prohibit member from future borrowing
Pursue legally	Contact implementing agency for advice; research local regulations for legal options. This can be more costly to the village bank and should be carefully evaluated in terms of costs and benefits

Collecting Delinquent Loans (Lesson 7)

Scenario for Discussion

Present the following situation:

> *Patricia received a large internal account loan during this loan cycle but did not attend the most recent village bank meeting; none of the other members know why. She had attended the past two meetings, but had been unable to make the internal account loan payments that were then due. During the last meeting, she also withdrew a portion of her savings, saying that she had a family problem. The village bank does not know why she needed the large internal account loan and how she planned to use the funds. Now, Patricia is quite delinquent in her payments, and she has very little money saved in the bank. Furthermore, the village bank is not certain where she lives.*

Discussion

Discuss what the village bank should have done differently. Write down the ideas as they are suggested. The following is a list of key points to consider:

- The best way to solve such a situation is to prevent it by establishing and following effective internal account loan policies;
- There are early warning signs to indicate that a payment problem is developing. By watching for these signs, a village bank can take action immediately;
- This bank did not perform a thorough analysis to enable bank members to understand why Patricia needed the loan and how she planned to use the funds;
- The bank did not collect sufficient personal information from Patricia regarding her home address (and did not confirm that she lived there). As a result, bank members could not locate her to discuss the problem;
- When Patricia first became delinquent on her loan, the bank did not take action;
- The bank allowed Patricia to withdraw savings even though she was delinquent on her loan. Consequently, bank members had very little collateral.

Review the above suggestions to determine how effective each one might have been in this situation. Build upon these suggestions by referencing the poster of follow-up steps from the checklist. Develop a list of delinquency and collection guidelines for the village bank to use.

Explain that internal account loan delinquencies place all members' funds at risk and potentially damage the personal dynamics that are key to a successful village bank. The situation requires swift action and sensitive handling of the conflict; it can sometimes involve legal issues.

Each situation must be handled separately based upon its own unique merits and characteristics. Therefore, the village bank may discover situations where its members choose to show tolerance and a willingness to work with a delinquent borrower.

Ask participants what the village bank should do when the internal account delinquency is caused by the following:

- death in the family of the borrower,
- natural disaster affecting the borrower,
- borrower who refuses to pay claiming the village bank is corrupt,
- borrower who can not be located.

Delinquency and Collection Checklist

Conclude the session with a review of the questions on the Delinquency and Collection Checklist.

If any participant responds in the negative to any of the questions on the first section of the form, discuss the reasons why she made this policy decision and how this decision may affect loan repayment.

Troubled Loan Report (Form)

(The following copyrighted Troubled Loan Report is reproduced with the permission of Freedom from Hunger.)

Village Bank Name ______________________ Week No./Cycle ______________

Village Bank ID No. ______________________ Date ______________

Late Internal Account Loan Repayments to the Village Bank

Name	ID Number	Amount at Risk	Days Overdue	If Repaid, Date Repaid	Action Taken
TOTALS					

Prepared By ______________________ Date ______________

Bank President ______________________ Date ______________

Preparing the Troubled Loan Report (Instructions)

Village Bank Name	D	Week No./Cycle	D
Village Bank ID No.	D	Date	D

Late Internal Account Loan Repayments to the Village Bank

Name	ID Number	Amount at Risk	Days Overdue	If Repaid, Date Repaid	Action Taken
D	D	D	D	D	D.
TOTALS		D.			

Prepared By	DD	Date	DD
Bank President	D.	Date	D.

Instructions for Preparing the Troubled Loan Report

Enter the information described below on the troubled loan report:

Field	Instructions
D	Name of the village bank.
D	Current week (or month) in the cycle, and the bank's current cycle number.
D	Number of the village bank, if one has been assigned.
D	Date the report was prepared.
D	Names of all internal account borrowers who have not repaid their loans in full by the end of the cycle.
D	Borrower identification number assigned by the bank, if borrower is a member.
D	Outstanding (unpaid) balance of the loan at the time the report is prepared.
D	Number of days between the date of the last actual payment and the date of the *next* scheduled payment meeting after the date this form is prepared. For example, assume a village bank has a four-month cycle with weekly payment meetings. The bank prepares this form during the fourth meeting of the cycle. It includes information on a borrower with a two-month loan taken out at the beginning of the cycle and who failed to make payments after the first weekly meeting. The Days Overdue for this borrower should be listed as 21 (seven days each for the two payments missed during the second and third meetings, plus the seven days that will pass until the next meeting, since payments can only be made during meetings).
D	Date actually repaid (completed at any time during the course of the following or subsequent cycles).
D.	Brief description of actions taken by the village bank or your agency to address the delinquency.
D.	Total amount of all unpaid internal account loans as of the end of the cycle.
DD	Signature of your promoter (or a committee member, after adequate training) and date.
D.	Signature of the bank president (or another committee member) and date.

Reporting on Troubled Loans (Lesson 8)

Objectives

Review the importance of on-time loan repayments and the possible follow-up actions for delinquent loans.

Practice using the troubled loan report for purposes of the following:

- ensuring internal control over late internal account loan repayments,
- formalizing communication and tracking regarding troubled loans.

Activities

Review the village bank's policies for loan repayment and delinquency.

Ask the participants whether late payments are ever acceptable. List the reasons why they are or are not acceptable (risk of loss, fewer funds to reinvest, cost to the village bank) and discuss each in turn.

Show the participants a blank troubled loan report and review the instructions for completing this form.

Show a sample of a completed payment summary (Handout L8-1) in which three borrowers have loan installments overdue. Ask the participants the following:

- What is the name of the first borrower with an overdue internal account loan?
  [Answer: Sumali]
- Can we determine the original internal account loan amount from the information on this form?
  [Answer: No.]
- Where can this information be found?
  [Answer: On the borrower's individual internal account loan record and in the borrower's passbook.]
- How much is overdue?
  [Answer: The total amount of principal and interest found in the Arrears columns of the payment activity summary form – 30.00.]
- How many days is this loan overdue?
  [Answer: The number of days found in the Arrears Days column of the payment activity summary form – 21.]
- How do we determine the number of days in arrears?
  [It is the number of days that have passed since the last meeting in which a payment was due and the next scheduled payment meeting after the meeting in which this form is completed.]

Continue with the other two borrowers who are in arrears. Ask the same or similar questions of the participants.

Provide the participants with Handout L8-2 describing the situation of three internal account borrowers with balances in arrears. Ask the participants to sit in pairs to review the information provided. They should then fill out a troubled loan report and, when finished, compare their completed report with another group or two. Any discrepancies in the report should be discussed and any errors corrected. (See Handout L8-3 for the solution.)

Ask one or two members of the group to present a completed form to the entire group.

Handout L8-1: Sample Payment Data, Friendship Village Bank

Payment Activity Summary

Village Bank Name Friendship Cycle No. 4 Date 03/31

		Loan Payment Record					Arrears			
Borrower Name	Borrower ID No.	Total Due	Principal	Interest	Total Paid	Outstanding Balance	Arrears Days	Principal	Interest	Fines
Balance Forward			47.30	9.40	56.70	123.50				
Sumali	01	16.20	0.00	0.00	0.00	16.20	21	30.00		2.16
Minerva	02	12.50	10.00	2.50	12.50	0.00				
Toni		20.00	4.00	0.00	4.00	16.00	14	42.00	3.30	1.81
Sarah	07	29.20	7.50	1.50	9.00	20.20				
Lynne	12	45.60	0.00	0.00	0.00	45.60	14	80.00	4.50	3.82
Totals This Meeting		123.50	21.50	4.00	25.50	98.00				
Balance to Date			68.80	13.40	82.20		49	152.00	7.80	7.79

Village Bank President ______________________ Date __________

Village Bank Treasurer ______________________ Date __________

Handout L8-2: Sample Data, Case Studies for the Friendship Village Bank

The village bank Friendship is in its fourth cycle. The bank has been experiencing repayment problems and has decided to begin using the troubled loan report to better track late payments on internal account loans. Although the information on late payments is recorded on the payment activity summary, the troubled loan report allows the management committee and bank members to see at a glance those internal account borrowers with late payments, the total amount at risk in the internal account and the number of days payments are overdue. In addition, this form allows the members to record payments made by borrowers who are in arrears and any actions taken with regard to the delinquent payments.

Today is Friendship's fifth weekly payment meeting. Of the 30 members attending the meeting, 10 have outstanding internal account loans. Three of these internal account borrowers are in arrears.

Sasha

Sasha is member 18 of the Friendship village bank. She has never before fallen behind in her payments to the bank, either in the external or internal account. This is her second internal account loan. Sasha borrowed 20.00 from the internal account during the first bank meeting of this cycle to supplement her external account loan. She used her money to buy bricks to finish renovations on her house. She thought the income from her fruit stand at the market would be sufficient to cover the payments of the additional loan. However, her community is experiencing high unemployment and many people have temporarily taken work in neighboring cities to earn a living. Her business has suffered because of this, and she is unable to make payments on her internal account loan. To date, Sasha has paid only 6.00 in principal and 1.20 of the 3.20 she owes in interest. She made her last payment on her internal account loan during the second weekly payment meeting. No one from the village bank has visited Sasha to find out why she has been unable to pay her loan.

Janet

Janet is not a member of the Friendship village bank. She is the village bank treasurer's cousin. This is her first loan from the bank. She used her cousin's influence to obtain a two-month loan of 50.00 during the second bank meeting this cycle to buy used clothing for resale. Unfortunately, Janet has never sold clothing before and knows little about pricing and inventory control. She often takes clothing from her inventory for personal and family use—she even gives clothing to her friends as presents. Janet did not attend this meeting of the village bank because she did not have the required payment. Janet's only payment was 8.00 in principal and 2.00 in interest made during the third bank meeting. The treasurer, when asked, did not know why Janet was unable to attend today's meeting, nor did she know why Janet could not repay her loan.

Silvia

Silvia is Friendship bank member 20. She obtained a 45.00 one-month loan during the first payment meeting to buy more chicks for her egg selling business. So far, things have gone well for Silvia; however, her husband needed money last week for a trip to visit his ailing mother in another community and Silvia gave him the money she intended to use to pay off her internal account loan. So far she has paid all of the interest on her loan and owes only 15.00 in principal. The bank Treasurer visited Silvia yesterday, and Silvia told her she had a family emergency and would be unable to attend the meeting this week. She promised to pay the remaining due on her loan at the next bank meeting.

Handout L8-3: Solution to Sample Problem, Troubled Loan Report

Village Bank Name	Friendship	Week No./Cycle	Week 5 – Cycle 4
Village Bank ID No.		Date	

Late Internal Account Loan Repayments to the Village Bank

Name	ID Number	Amount at Risk	Days Overdue	If Repaid, Date Repaid	Action Taken
Sasha	18	14.00	21		None
Janet		42.00	14		None
Silvia	20	15.00	7		Treasurer informs will pay at next meeting
TOTALS		**69.00**			

Prepared by		Date	
Bank President		Date	

Tool Set: Managing the Cash Reserve

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To provide an objective guide for regulating internal account cash reserves
Frequency	Upon bank formation; as needed thereafter
Description	A table of cash reserve guidelines for the internal account that can be used to stimulate discussion; case studies
Strengths	Systematic methodology; flexible, with options of 30%, 20% and 10%; conservative
Limitations	Potential difficulties in tailoring reserves due to monitoring issues and time required to conduct bank assessment

Overview of Tools

Managing the Internal Account's Cash Reserve (Guidelines)

These guidelines present a systematic method for establishing and managing a village bank's cash reserve.

Establishing the Cash Reserve (Lesson 9)

This lesson provides case studies to illustrate the need for maintaining a cash reserve and includes a discussion on various reserve policy issues. It takes approximately two (2) hours to complete the lesson.

Before you begin the lesson, you will need one copy of each of the following reproduced on an overhead or flipchart paper:

- Cash Reserve Guidelines for the Internal Account chart from the Guidelines for Managing the Internal Account's Cash Reserve Tool
- Village Bank Health Checklist, for Agencies Tool

You will also need a copy of the following handouts for each participant:

- Case Studies for Establishing a Cash Reserve (L9-1)
  "The Penny Jar" Case Study (L9-2)

You will also need flipchart paper and markers, and local currency.

Managing the Internal Account's Cash Reserve (Guidelines)

Cash reserves are highly recommended for internal account lending programs. The purpose of a cash reserve is to act as a cushion or buffer for the group in the event a borrower fails to pay back her loan (a loan default). A cash reserve also provides the village bank with some liquidity when an emergency causes members to withdraw savings.

Agencies generally consider an internal account reserve as partial collateral in the event there is a problem with the external account loan. It is one resource that your agency can draw upon if the village bank fails to repay its loan.

In deciding the amount of a cash reserve, you should consider both internal and external account factors, along with overall capabilities and management capacity of the village bank. The guidelines presented here are one way for your agency to systematically review the reserve policy for a specific village bank.

General Recommendations for Setting Cash Reserves

Recommended reserve policies are as follows:

- Require an initial cash reserve of 30% of available funds for all village banks that have been in operation for less than one year, assuming that the country is not experiencing high inflation and that there are secure deposit-taking institutions available. For banks operating in inflationary economies or environments without sufficient financial infrastructure, a cash reserve is generally not feasible;

- After the management committee and members are familiar with practices for accounting, auditing, loan analysis, disbursement and collection (generally one year), you can begin to adjust the cash reserve as warranted. A village bank's cash reserve requirement will fluctuate up and down over the life of the bank depending on its historical performance and such external factors such as the inflation rate;

- To reassess the village bank, first evaluate it against the indicators under the 30% benchmark. On-time repayments for both internal and external account loans are the most important financial indicators. Both these indicators must remain high in order to justify a lower reserve. Use the Village Bank Health Checklist (an agency audit tool) to quickly assess the operational and management capacity of a bank. You can adjust both the checklist and the guidelines to fit specific country standards. However, your repayment-rate standards should remain high (above 95%);

- Some agencies adopt a standardized reserve policy. While this is easier for the agency, it may be harder for the members and represents a disincentive for them to save with the village bank. On the other hand, if members see that reserves are tailored to the performance of their bank, their sense of ownership and responsibility is reinforced. Rewarding good performance with lower reserve requirements has several advantages, including the fact that more money is available for lending, resulting in more interest income and higher dividends to savers which attract more savers;

- Guidelines on how to adjust a cash reserve according to portfolio performance and management committee capacity are provided in the following chart.

Cash Reserve Guidelines for the Internal Account		
30% of funds available	**20% of funds available**	**10% of funds available**
Portfolio Standards: Less than one year of operation Internal account on time repayment less than 90% External account on time repayment <90%	**Portfolio Standards:** One or more years of operation Internal account on time repayment at least 90% External account on time repayment at least 95%	**Portfolio Standards:** One or more years of operation Internal account on-time repayment rate of 95% or more External account on-time repayment 99% or more
Management Capacity Village Bank Health Checklist score less than 80%	**Management Capacity** Village Bank Health Checklist score of 85% or more	**Management Capacity** Village Bank Health Checklist score of 90% or more

Establishing a Cash Reserve (Lesson 9)

Case Studies

Ask participants to find a partner and distribute the case studies from Handout L9-1.

Read the first case aloud and ask each pair to discuss how it would respond. Then ask a few randomly selected pairs to explain their decisions. List responses.

Proceed through the next three cases in the same manner. (With village banks, do this step in group session by reading each case and asking participants to call out their spontaneous responses.)

Ask: What do all of these stories have in common?

Ask: What is the problem that the village bank faces? How will it cover this potential loss?

Explain that in each of these cases, the village bank internal account needs to have funds on hand.

Ask: What would happen if all the internal account funds were out in loans? What can a village bank do to protect itself?

Discussion

If participants don't raise the topic, explain the concept of a reserve. Ask them to identify other examples of just-in-case reserves that they use in their daily lives (such as an extra blouse in case the one we normally wear gets torn; holding onto old tools even after they are replaced just in case something happens to the new tool).

Brainstorm further on how much a village bank should hold in reserve in the internal account. Should it be a fixed amount? Should it be a percentage of the savings on deposit? List the answers and review the differences.

A cautious bank would set the reserve very high. (Use a stack of real money to illustrate a large portion locked away, unavailable for lending, leaving only a small amount accessible to members.)

Ask: What are the advantages of establishing a high, conservative reserve? What are the disadvantages?

A less cautious bank would keep the reserve as low as possible.

Ask: What are advantages? And the disadvantages? What kind of bank are you? Cautious or risk taking?

Does it make sense to establish a reserve requirement that is "middle of the road" (halfway between cautious and risky) for all village banks to follow ?

If we want to consider a *variable reserve* that is lower for strong banks and higher for less mature banks, what factors should determine a bank's move to a lower reserve?

Explain that the Guidelines to Managing the Internal Account's Cash Reserve is a tool with two components: a set of general guidelines for establishing a variable cash reserve and a chart of more specific criteria. Certain of these criteria are based on the Village Bank Health Checklist Tool.

Show the Cash Reserve Guidelines for the Internal Account chart from the tool. Explain the three categories and the benchmarks for each.

Show a Village Bank Health Checklist and review the questions and method of scoring.

"The Penny Jar" Case Study

Divide the participants into small groups of three or four people and distribute "The Penny Jar" case study (Handout L9-2).

After reading the case study, each group should prepare a Village Bank Health Checklist (see Tool Set: Agency Mini-audits) for this bank, using information provided in the case. (In a village bank training, participants can use the checklist to assess their own bank. If the participant group includes representatives of different banks, they can interview each other about their respective banks.)

Participants should score the checklist and make a recommendation regarding the reserve policy for this bank.

Review each group's decision and discuss the merits of this tool using the following questions as a guide:

- Are there additional questions that should be included in the checklist?
- Are there any questions that aren't very important?
- Are there any questions that are difficult to answer? Why?
- How many of the village banks with which you work would score over 80%? Over 85%? Over 90%?

Handout L9-1: Case Studies for Establishing a Cash Reserve

Case One

Betina is a village bank member in very good standing. Now on her third loan from the internal account, Betina has never missed a meeting and she would never dream of missing a payment. But a tragedy has occurred: Her daughter was in a bus accident and will be in the hospital for a long time. Betina is by her side day and night, except when she returns home to cook for her. Betina is no longer able to make her payments and she doesn't know when she will be able to take up her business again.

Case Two

A serious storm destroyed many bank members' stalls in the market. Ten members want to withdraw their savings from the bank in order to rebuild.

Case Three

Dorina had two payments left on her internal account loan when she suddenly left the village. Most bank members believe that she went across the border in search of her husband who was working on a large plantation. But no one is certain where she is and few believe she is coming back.

Case Four

An epidemic has swept through the village. Most bank members are sick or are busy caring for a family member who is sick. Business activity is at a standstill and, as a result, the village bank has missed two external account payments to the agency. The agency is demanding at least a partial payment by the next meeting (in two weeks time).

Handout L9-2: "The Penny Jar" Case Study

The Penny Jar started almost two years ago with 22 members. Now in its fifth lending cycle, our bank has grown to 26 members. Only two of the original members have left the bank. Our leader is a big part of the reason why we are so enthusiastic about our bank. Our president, Elizabeth, has been active in our village for a long time; she is just the kind of dynamic person that seems to attract other people to her. Elizabeth has made the bank run very efficiently, leaving time during meetings for other interesting activities such as providing speakers, planning social events and fundraisers—and even classes on topics that interest us.

We members are very proud of our repayment rate. So far, we have repaid every external account loan to the agency, and with only one late payment. Our on-time repayment rate is over 97% and we Penny Jar ladies want to keep it that way. Members help each other with payments when necessary and, because of the trust we must share to do so, are very careful about who we admit as members. True enough, we have been lucky in that most of our initial members have founded stable, if small, businesses. We turned away inexperienced women who applied for membership.

Elizabeth's grown son helps our bank manage its books. When he comes home from his job in the city—approximately every two weeks—he spends several hours bringing the records up to date. After he has them in order, the management committee signs them. This is a great service and everyone is relieved that he is willing to help out in this way. After he updates the records, Elizabeth likes to show off at the meeting by picking five members to compare their passbooks with the records her son has written. So far, all have matched every time!

The Penny Jar started lending from its internal account during cycle 3, and is currently in the third lending cycle. We started slowly; at first members were hesitant to borrow more than their external account loan and feared being the one who might lose the savings of fellow members. But the loans are easy to obtain and don't have to be just for business, so once the daredevils started, more of us have followed suit. Elizabeth keeps the record of who borrows how much; it is easy because there are not that many internal account loans each cycle. So far, repayment is very high. I don't know of anyone who has failed to repay her loan. Once, during the last cycle, a nonmember borrower missed several payments during the cycle and everyone was wondering what to do. But then the borrower came running in to the last meeting of the cycle, breathless, with the whole loan payment in her hand. Elizabeth told the treasurer to take the money and record it. She even found a nice way to explain to the borrower that she was close to losing a very special privilege.

Our treasurer is always careful to record everything in ink. She makes sure we sign our names in her book every time we make a payment or receive a loan. When she makes a mistake, she never just scribbles over it. She carefully draws a line through the mistake and writes in the correct amount nearby.

The best thing about our internal account, besides the fact that it is a source of funds a person can get for any number of reasons including emergencies, is that it actually makes money for members. Last cycle, for the first time, we each received a dividend of 2.00.

Elizabeth is involved in a lot of other activities besides the village bank that take her to town frequently. Sometimes, the treasurer is not able to go to the bank right after the meeting, so Elizabeth deposits the village bank money instead. It is more efficient that way. She keeps the receipts she gets so that her son can use them when he is updating the accounts.

Oh! The meeting of the Penny Jar is about to start. As usual, just about everybody is here. No one wants to miss a meeting. I know of two members who are going to ask for a loan from the internal account today. It will be interesting to listen to the discussion about their businesses. That's when Elizabeth and the treasurer try to figure out if the applicant's business idea or plan will be successful. I always learn something during these discussions.

Savings Policies and Practices

Savings Policies and Practices consists of a single tool set:

- Savings Practices

Tool Set: Savings Practices

Audience	Bank members, agency staff in training
Purpose	To train bank members in the importance of savings, and provide guidelines for setting mandatory and voluntary savings requirements
Frequency	As part of initial training; as necessary thereafter
Description	Three-part exercise and lesson to encourage savings; savings guidelines
Strengths	Simple to perform, with a clear message; participatory. Story-telling technique is inclusive of illiterate members and encourages discussion based on common life events.
Limitations	Requires animated facilitator who is effective with group discussion

Overview of Tools

Moving Away from the Cliff and A "Crummy" Lesson (Exercises)

These two tools include a role play and exercise to illustrate the importance of member savings.

Moving Away from the Cliff requires some sort of stage, either literal or imaginary, as a prop.

For A "Crummy" Lesson, you will need seven cookies or biscuits. Break off a very small piece of one of the cookies. Serve the cookies, including the cookie crumbs, on a platter or tray. You will also need eight slips of paper; seven with expenses typical to the trainees and one with the word *savings*. For example:

1. Housing or rent
2. Transport
3. Food
4. Clothing
5. Medicine
6. School fees
7. School books
8. Savings

Four Lessons in Savings (Exercise)

The lesson presents four stories highlighting the importance of saving.

If you use the stories during village bank meetings rather than in the context of a seminar, you can do so over a period of two or four meetings. In advance of the first session, prepare the pictures on a flipchart or within a large spiral notebook that is easy to carry and that allows you to refer to previous stories for review.

To conduct the lesson, you will need a copy of Handout L10-1 with pictures for each story referenced in "Four Lessons in Savings."

You should also be familiar with the pictures and the general stories, so that you do not have to refer to notes to refresh your memory. Try to have fun with the stories and, if appropriate, connect them to events in the members' lives.

Savings Practices (Lesson 10)

This lesson presents the previous two tools (Moving Away from the Cliff and A "Crummy" Lesson, and Four Lessons in Savings) in the context of a single lesson for a training seminar. It requires approximately two (2) hours to complete.

Refer to the overview of each tool for required materials.

Guidelines for Savings Requirements (Analysis)

This tool includes a matrix that outlines the various savings goals of the agency, village bank and bank members, as well as a table that identifies various savings-access options and the advantages and disadvantages of each.

It can be used as a discussion guide to educate both bank members and agency staff.

Moving Away from the Cliff (Exercise)

Role Play

In advance of the session, ask for two volunteers. Assign one the role of "Maria" (or any other local name), a typical mother in the program's area of work. Assign the other the role of "Sickness." Brief them on their characters and ask them to review their parts in this lesson.

Ask Maria to stand on stage at the edge of a "cliff" and then have her move farther away from it. If nothing is available to show differences in height, then simply draw a line. Have Maria stand by the line and explain that the other side of the line is a drop-off of hundreds of feet.

Ask Maria to describe her character to the audience. She is very poor and has no savings to draw on for emergencies. She has three small children and no husband. Her friends and relatives are all just as poor as she is; all have no savings.

Explain to the audience that because Maria has no savings, it is as if she and her children are on the edge of a cliff—very vulnerable to any "push" that may come along. Have her stand right on the edge, then assign someone else the role of Sickness. Have Sickness slowly walk towards her while saying "Maria, I'm here for your daughter. Do you have savings to pay for medicine for her?" Maria has to say that she doesn't, so Sickness merely gives her a gentle push and she falls down the cliff, screaming and crying for her daughter.

Then ask "What would this look like if Maria had savings? Would she still be as vulnerable to calamities and misfortunes?"

Elicit a response to the effect that Maria would now be several steps away from the cliff. Have Sickness come again, with similar threats; but this time when Sickness pushes her, she does not fall over—although she may be forced a step or two closer to the edge of the cliff.

Have Maria express something to the effect that "I have savings now, Sickness, so I've bought medicine for my child."

Debriefing

Discuss this role play with participants; elicit their recognition that having savings makes a person and her family less vulnerable, less at-risk.

Ask what other dangers besides Sickness can push a poor person without savings over the edge of the cliff.

A "Crummy" Lesson (Exercise)

Exercise

Ask for eight volunteers. Have each draw a slip of paper containing the description of a common household expense. Call out each expense in turn and ask whether the person with the slip listing that expense has spent any money on it during the past month. (Be sure to leave the savings expense for last.)

Have fun with it. You want each person to say that she has spent money on the expense, so rephrase the question a bit if she says she has not. For example, if a volunteer says "I haven't spent money on school books in the past month," ask her if she's EVER spent money on such, or even she has ever KNOWN anyone who has done so. As each person is able to say "yes," offer congratulations and a cookie as a reward.

By the time you call the eighth category, "savings," the seven whole cookies will be gone and only crumbs will remain. When the savings holder comes forward to get the cookie, act terribly embarrassed, "Oh, I'm so sorry, I must not have counted correctly. I feel terrible. All that is left is crumbs. Oh, I feel awful."

Eventually, transition from this to the moral of the story. Ask participants what this object lesson was meant to teach.

Elicit the answer that "if you leave saving to what is left over after all other expenses are paid, only crumbs will remain. To save requires discipline and planning—setting aside a budgeted amount for savings first."

As the old expression goes, "You don't plan to fail. You only fail to plan."

Four Lessons in Savings (Exercise)

Lessons

Present each story to the participants. At the end of each story, ask the group as a whole (or in small subgroups) to discuss the set of questions and assign a representative to report the answers. Make certain that each question is clear and that the group has enough time to discuss each one.

The questions may raise other issues about savings, a woman's view of the world, and the constraints women face. These are good discussion issues. Encourage the women to think about these issues and include them in the report, so that you can discuss them with all the participants. The goal is to help these women to help themselves. (Remember, there are no wrong answers to the questions.)

End the lesson with the message provided at the end of each storytelling session. Remind them that saving is always one solution to the problem.

Introduction to the Stories

We will be talking about four women and their lives. Some of the stories are happy and some are sad; we can learn from all of them.

Story One: Nosave

This woman's name is Nosave and she lives near _____________ (fill in the blank with a nearby village or town)
[Nosave Picture 1]

Nosave married a man who had a great deal of money and a nice house. He had a good job and they bought whatever they wanted; but they never gave any thought to the future and they never saved. [Nosave Picture 2]

One day a terrible thing happened: Nosave's husband became very sick and had to go to the hospital. He was there for several weeks, and then he died. [Nosave Picture 3]

Nosave had to pay for all of the hospital and doctor's expenses as well as for all of the funeral expenses. After her husband died, she had no income. She also found that her husband had borrowed from moneylenders and owed a lot of money. To pay off her debts she had to sell her house and move into a smaller one. She also had to sell many of her possessions, so she was left with very little. [Nosave Picture 4]

Nosave was very sad. She got a loan from a moneylender and began selling fruit. [Nosave Picture 5]

What happened to my life she thought?

Question for Group Discussion

Could Nosave have done things differently?

Answer: If she had saved, she would not have had to borrow from the moneylender and she would have money for emergencies.

Message

It does not matter how much money you have. You may have a lot, or you may have a little—either way, you need to save.

Story Two: Sameso

Sameso was not rich but she had a small business selling fruit. [Sameso Picture 1]

She wanted to improve her life and she dreamed that one day she would own her own business. [Sameso Picture 2]

She wanted to have a butcher shop where she could sell meat in the market. She knew that she could make a good profit that would enable her to make improvements to her house. But, day after day, she spent everything that she made. Some days she made a good profit and other days a small one. But whatever she made, she spent. She did not save and her savings box was very sad. [Sameso Picture 3]

Days, weeks and years passed. She continued to spend everything that she made. She never started her butcher shop. She couldn't even expand her fruit business. As a result, she was never able to improve her house. [Sameso Picture 4]

"I guess that I was meant to be poor," thought Sameso, "I will never improve my house or my life."

Questions for Group Discussion

What would you say to Sameso?

- Was she right that she was meant to be poor?

  Answer: No one is destined to be poor.

- Was it bad for her to dream of having a butcher shop or a better home some day?

  Answer: It was not bad for her to dream. We all need to have dreams of what we want to be and have some day. This is the first step to getting what we want.

- What could she have done differently?

  Answer: She could have saved so that she had money for the future. By putting money away she would have it available to increase her business size or improve her house.

Message

Saving allows you to do big things—such as improving your house or expanding your business.

Story Three: Emergency Ela

Emergency Ela was very similar to Sameso and Nosave. She had a business selling fruit. [Emergency Ela Picture 1]

She also spent all that she made. As a result, she had a very sad cash box. [Emergency Ela Picture 2]

One day, one of her children became sick. She took the child to the doctor. But, since she had no savings, she had to sell all of the stock in her business. She had to take care of the sick child for many weeks and could not run her business.

Then the child died. [Emergency Ela Picture 3]

To pay for funeral costs, she had to borrow money from a moneylender.

She borrowed more money to start another small business. She was sad. [Emergency Ela Picture 4]

Question for Group Discussion

What could Emergency Ela have done differently?

She could have put away money for emergencies. This is another important use of savings; they allow you to get an emergency loan from your village bank rather than from a moneylender.

Message

Savings help you to pay for emergencies. Do you have an emergency fund?

Story Four: Saversocan

Saversocan was the poorest of all four women. [Saversocan Picture 1] She had a small business selling flowers.

Some days she sold more and some days she sold less. But there was one important difference between Saversocan and the others. Can you guess what it is?

She saved. [Saversocan Picture 2]

Every day she set aside _______ (insert amount). This was not always easy and her children complained that they wanted things. But Saversocan knew that she needed to set aside money. It took a lot of discipline. After one year she had saved more than ___________(insert amount). With this she rented a good place in the market and changed her business to selling fruit (a higher profit margin product). Her savings also allowed her to buy in bulk, and this brought her more profit. Her business improved. [Saversocan Picture 3]

The change did not happen all at once and she had her struggles. But slowly, because she saved and invested, she was able to improve her situation. She always kept an emergency fund—and by being a part of village bank, she could get an internal account loan for emergencies or for her business. She never went to moneylenders.

Her cash box was very happy. [Saversocan Picture 4]

As time went on she was able to open a butcher shop. [Saversocan Picture 5]

As the years passed, she was even able to buy a better house. [Saversocan Picture 6]

Now, she is in the best situation of all of the women. [Saversocan Picture 7]

Question for Group Discussion

What did Saversocan do differently?

She saved. Savings help dreams become reality. [Saversocan Picture 7]

Additional Questions for Group Discussion

Which woman do you want to be like?

Who has the highest savings in this group?

Remember: You do not have to save with the village bank, but it is important that you save in some way.

Message

Is anyone here too poor to save?

How much money do you have in your pocket?

It adds up, even if you only save a very small amount every day. If you invest some of it, it grows even more quickly. You can invest with the village bank and get a return on your savings or you can invest in other ways.

Savings Practices (Lesson 10)

Guide participants through each of the following exercises:

- Moving Away from the Cliff
- A “Crummy” Lesson
- Four Lessons in Savings

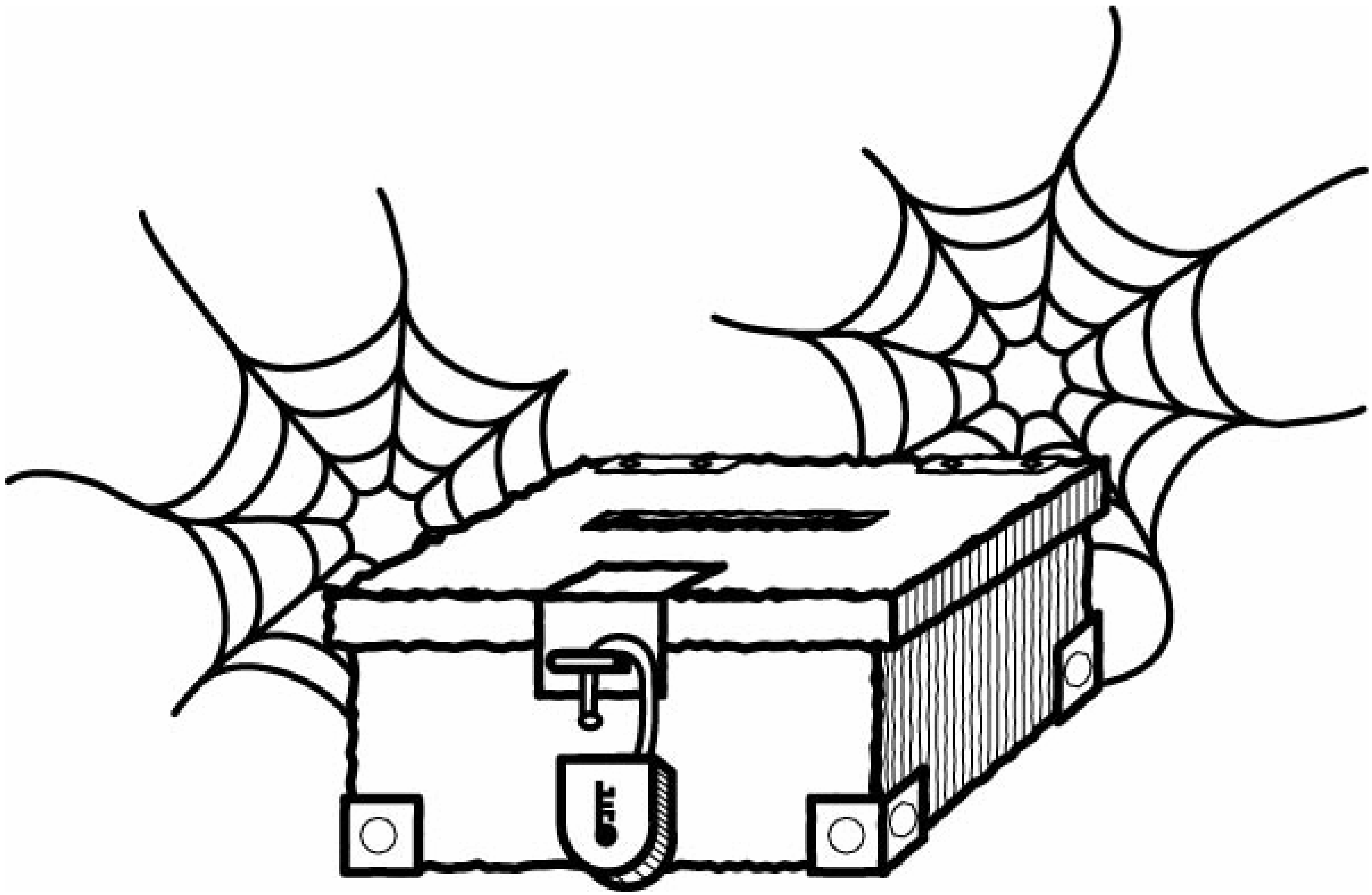
Handout L10-1 provides all of the pictures referenced in “Four Lessons in Savings.”

Handout L10-1: Pictures for Four Lessons in Savings

The following pages provide pictures of Nosave, Sameso, Emergency Ela and Saversocan for the lesson.

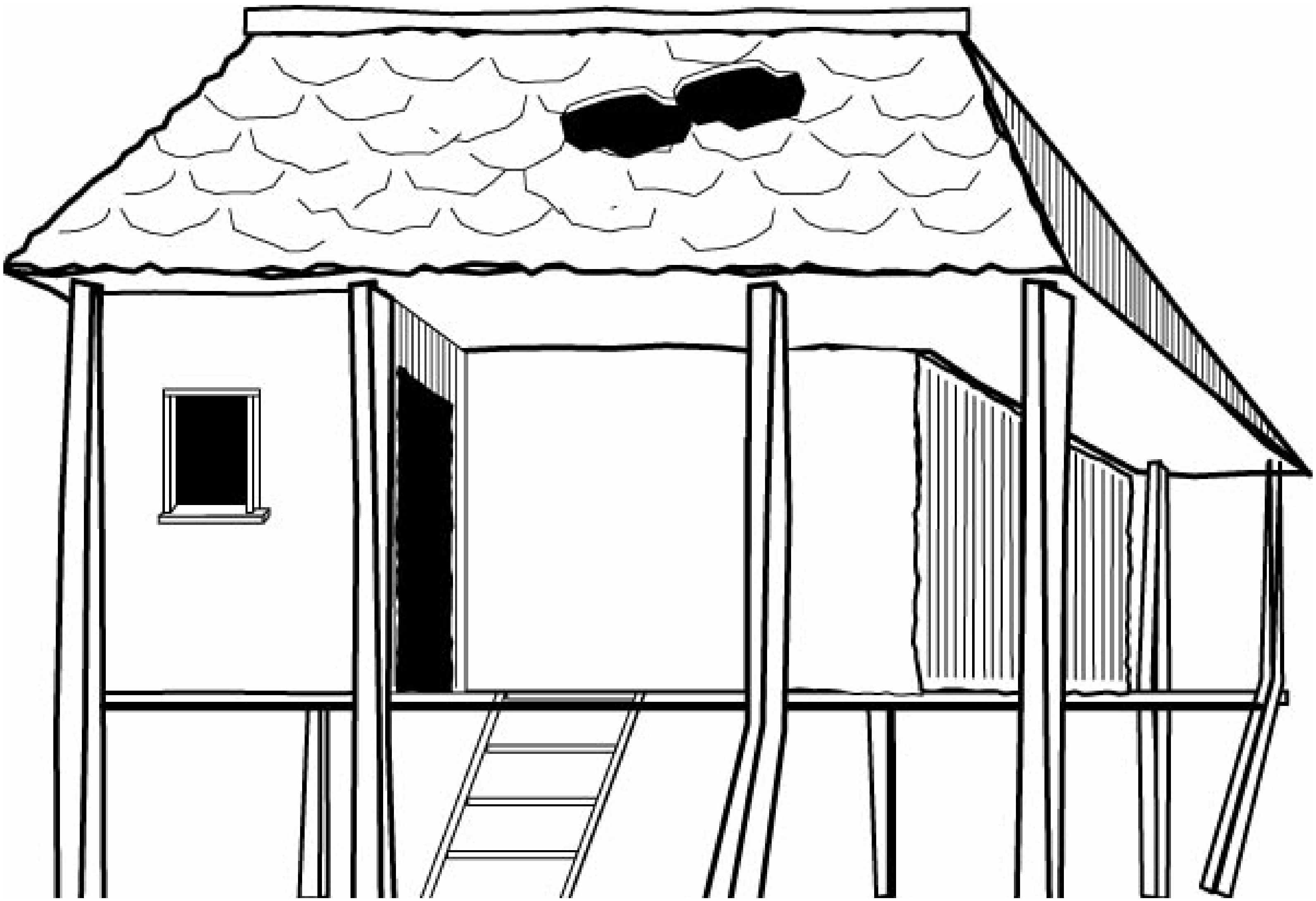
Nosave Picture 1

Nosave Picture 2



Nosave Picture 3

Nosave Picture 4

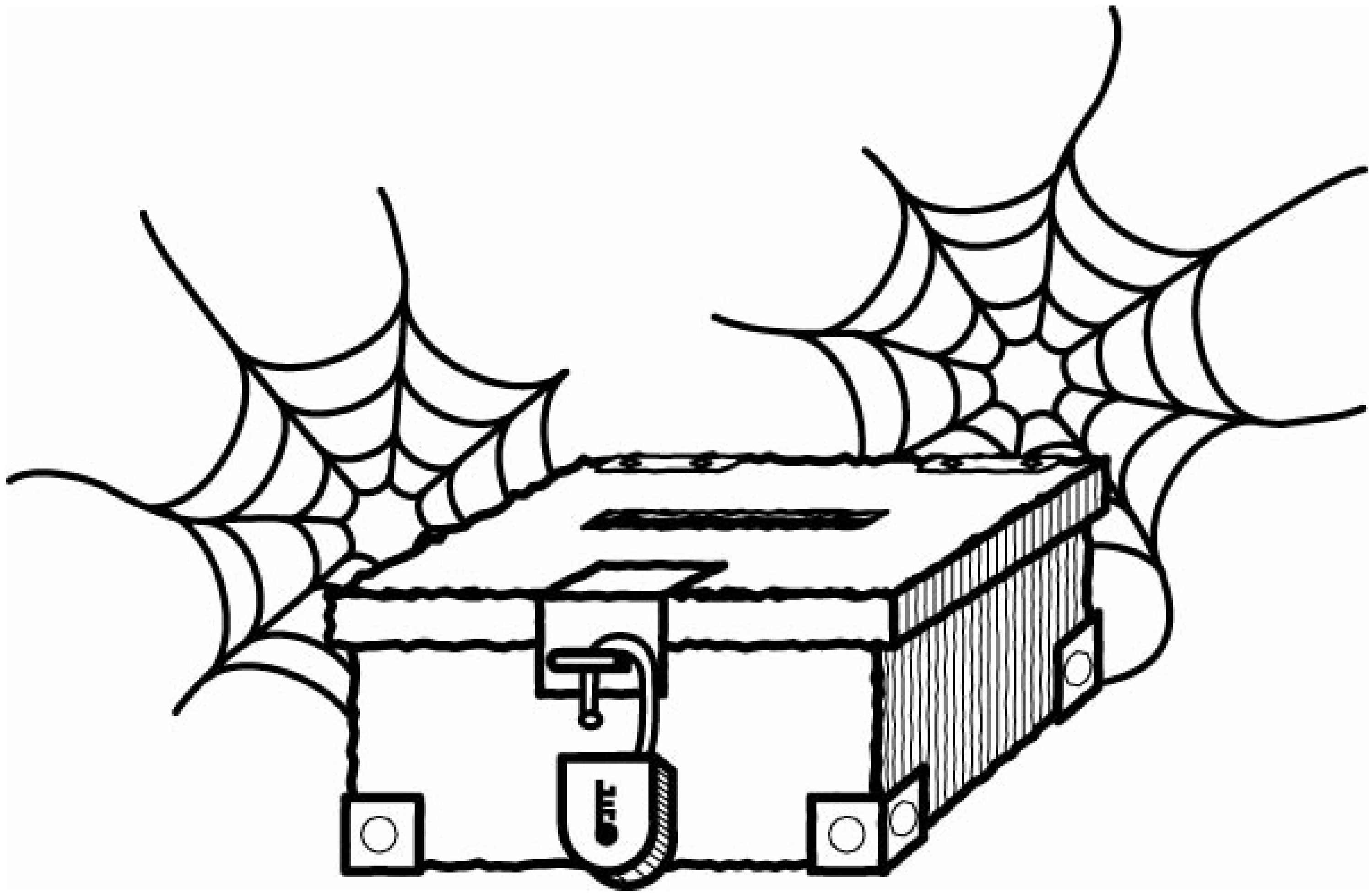


Nosave Picture 5

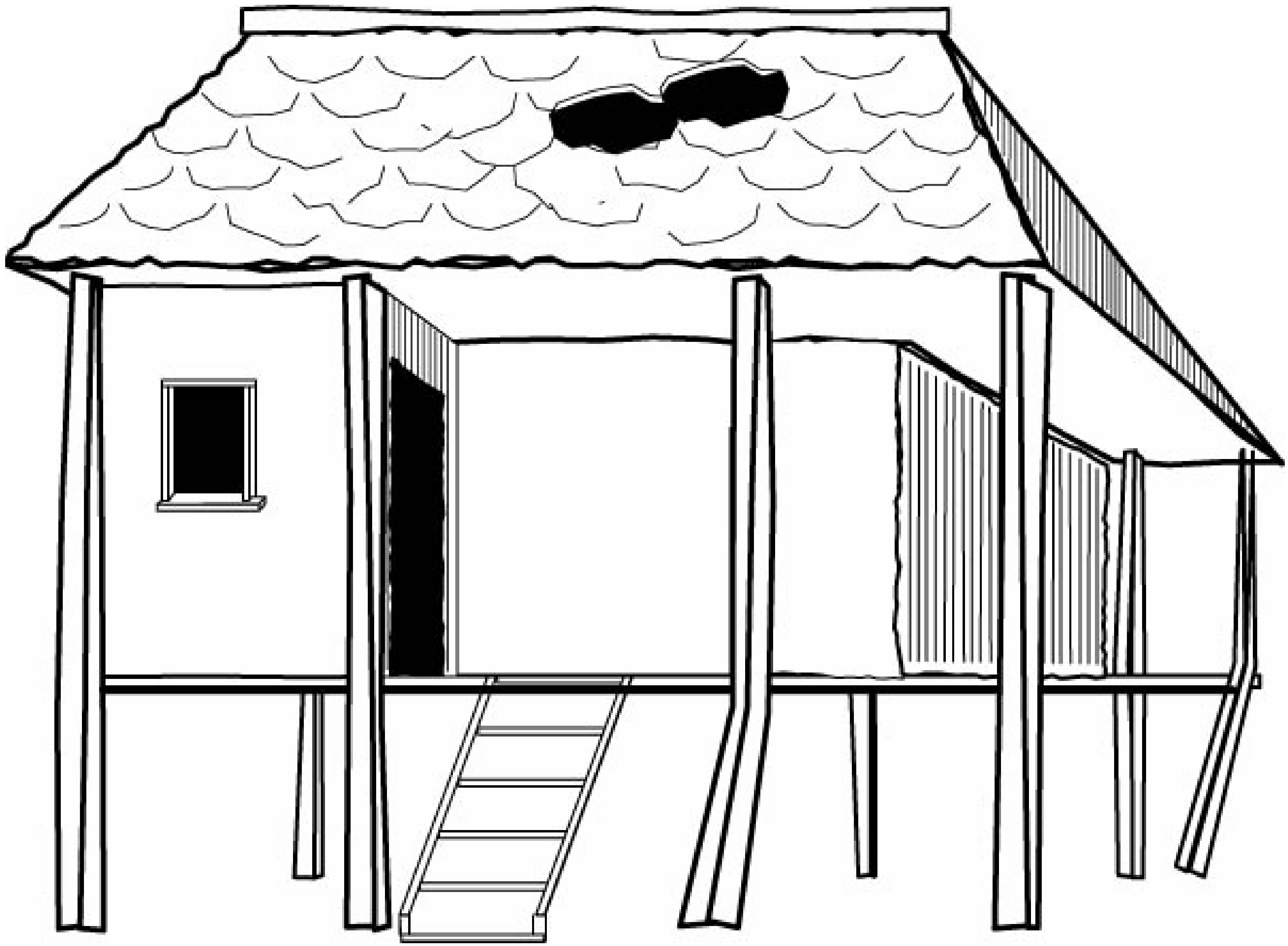
Sameso Picture 1

Sameso Picture 2

Sameso Picture 3

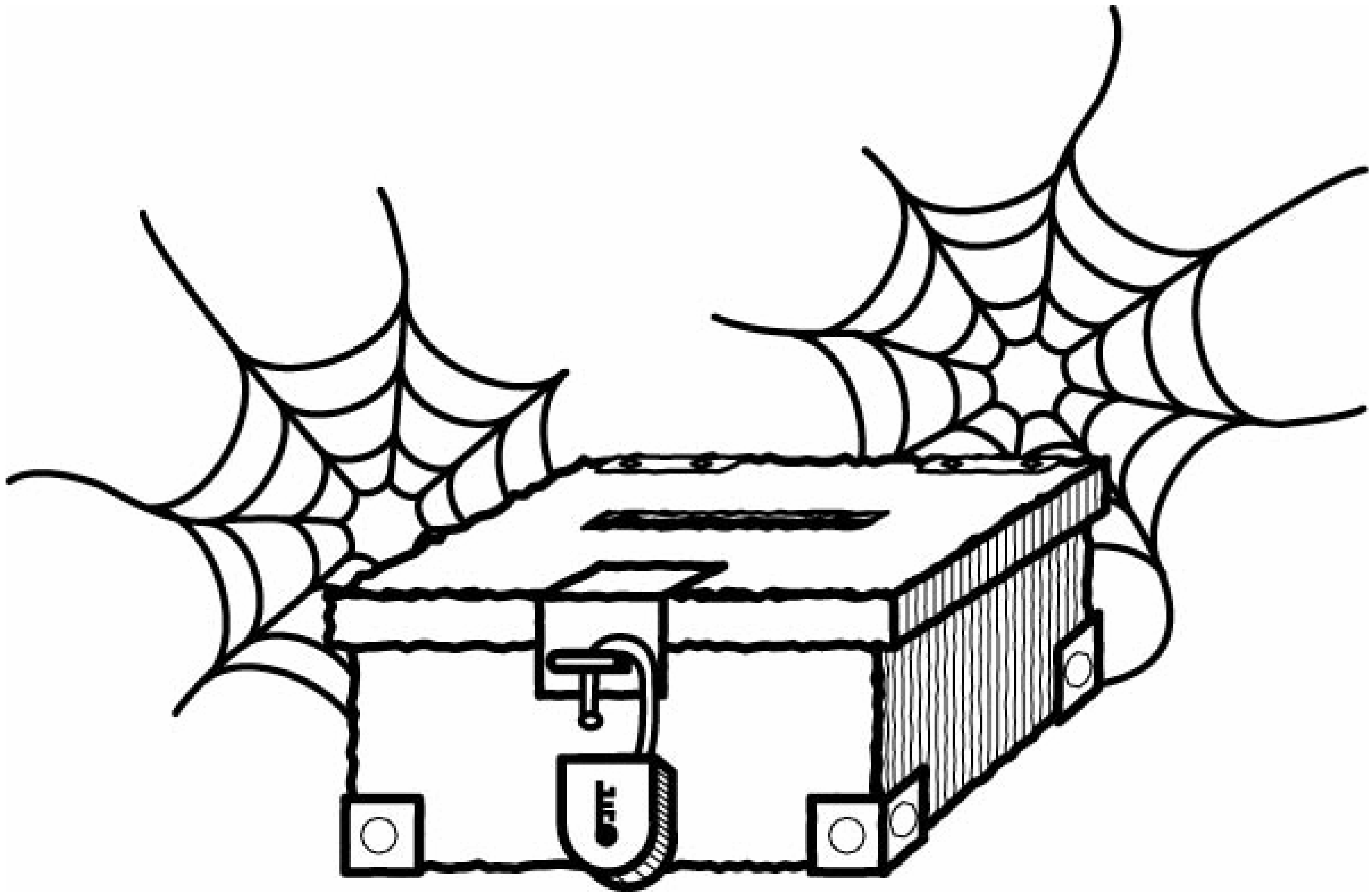


Sameso Picture 4

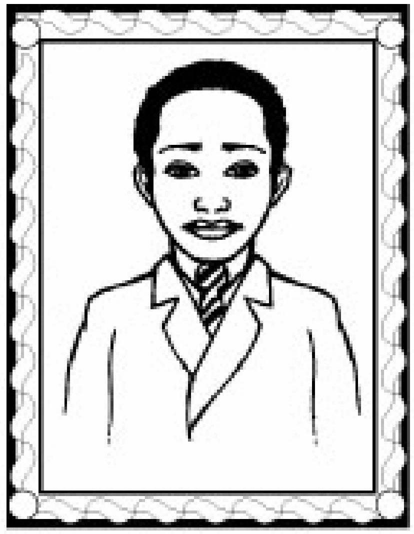


Emergency Ela Picture 1

Emergency Ela Picture 2



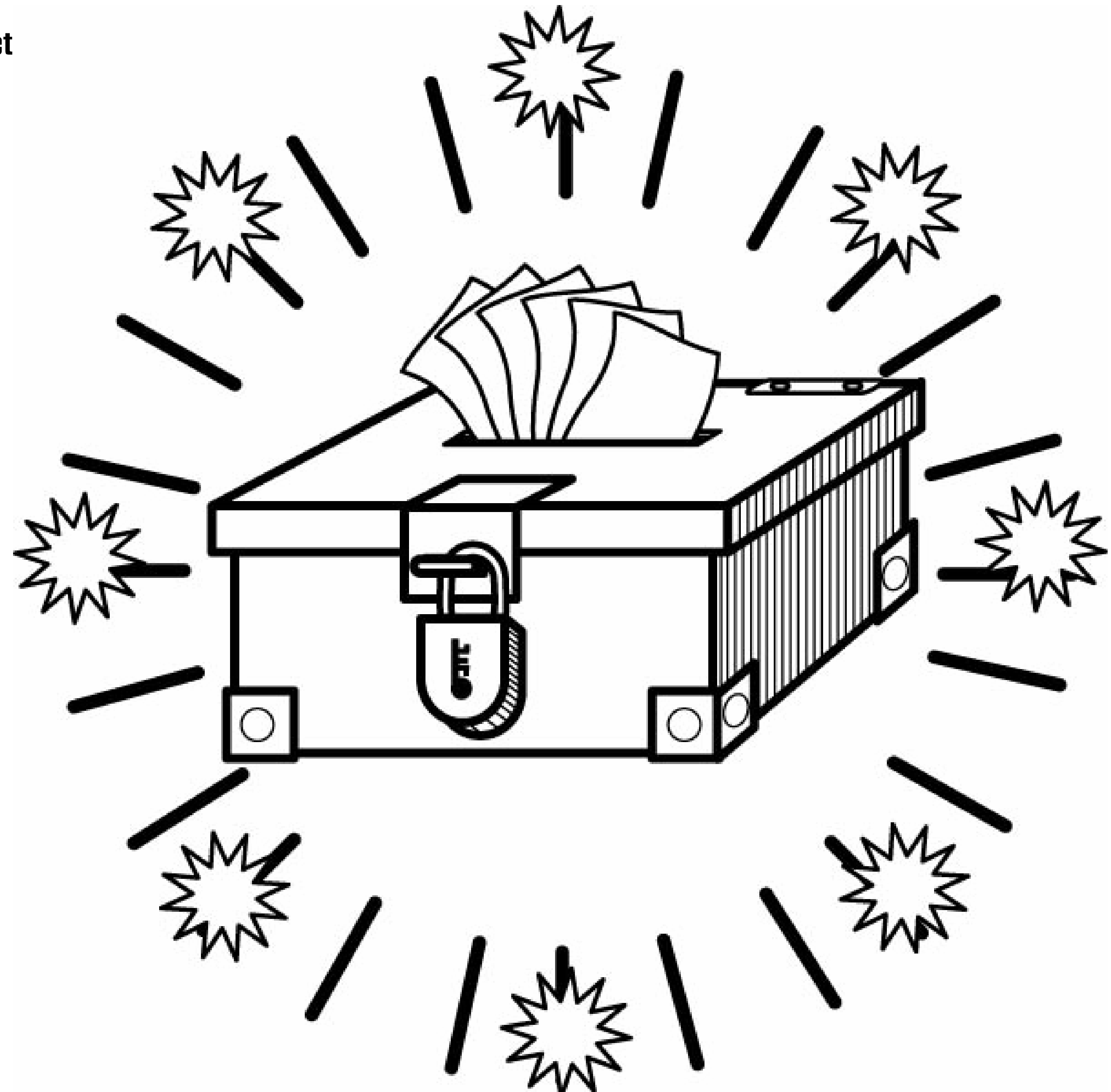
Emergency Ela



Emergency Ela Picture 4

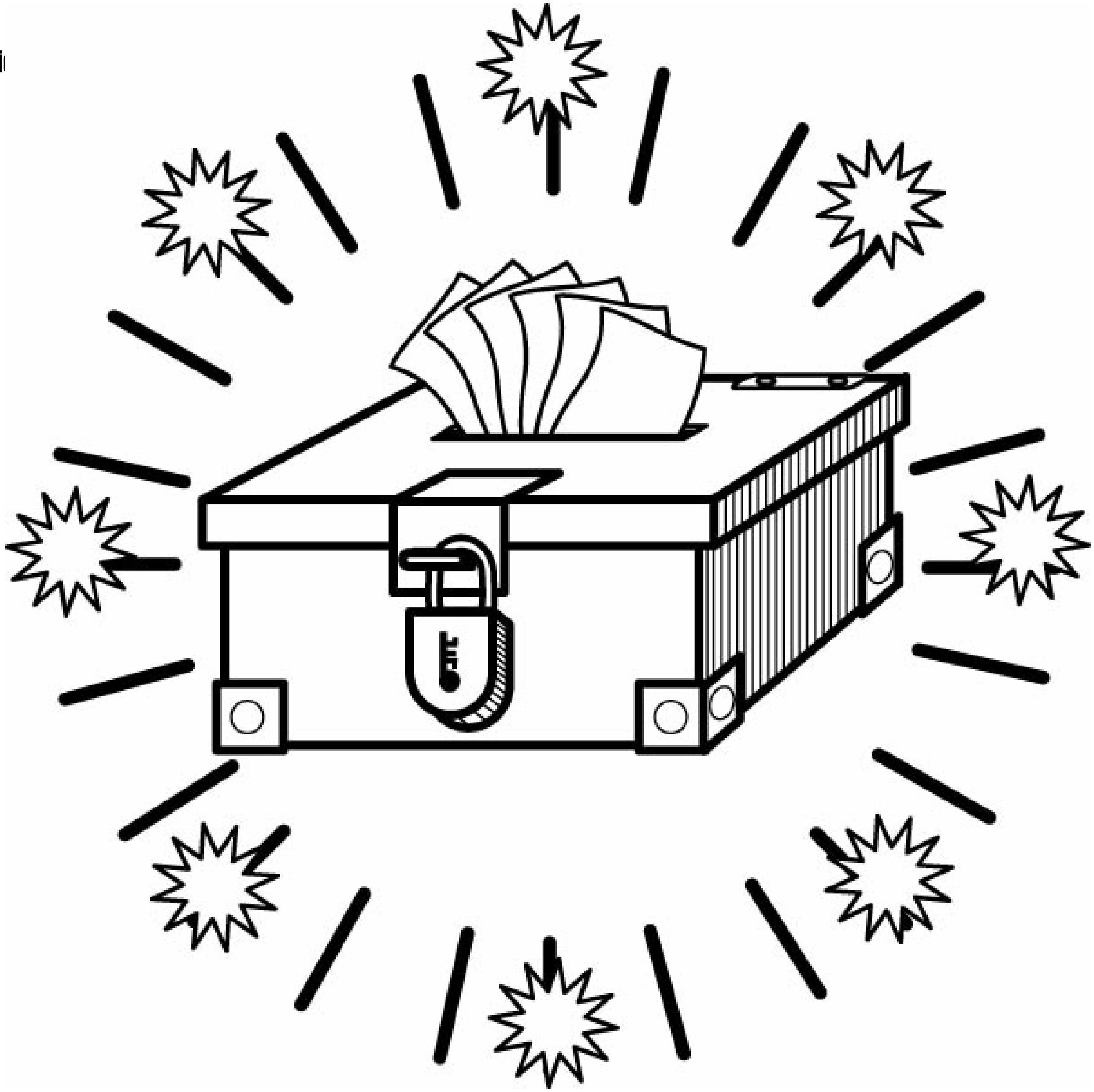
Saversocan Picture 1

Saversocan Pict

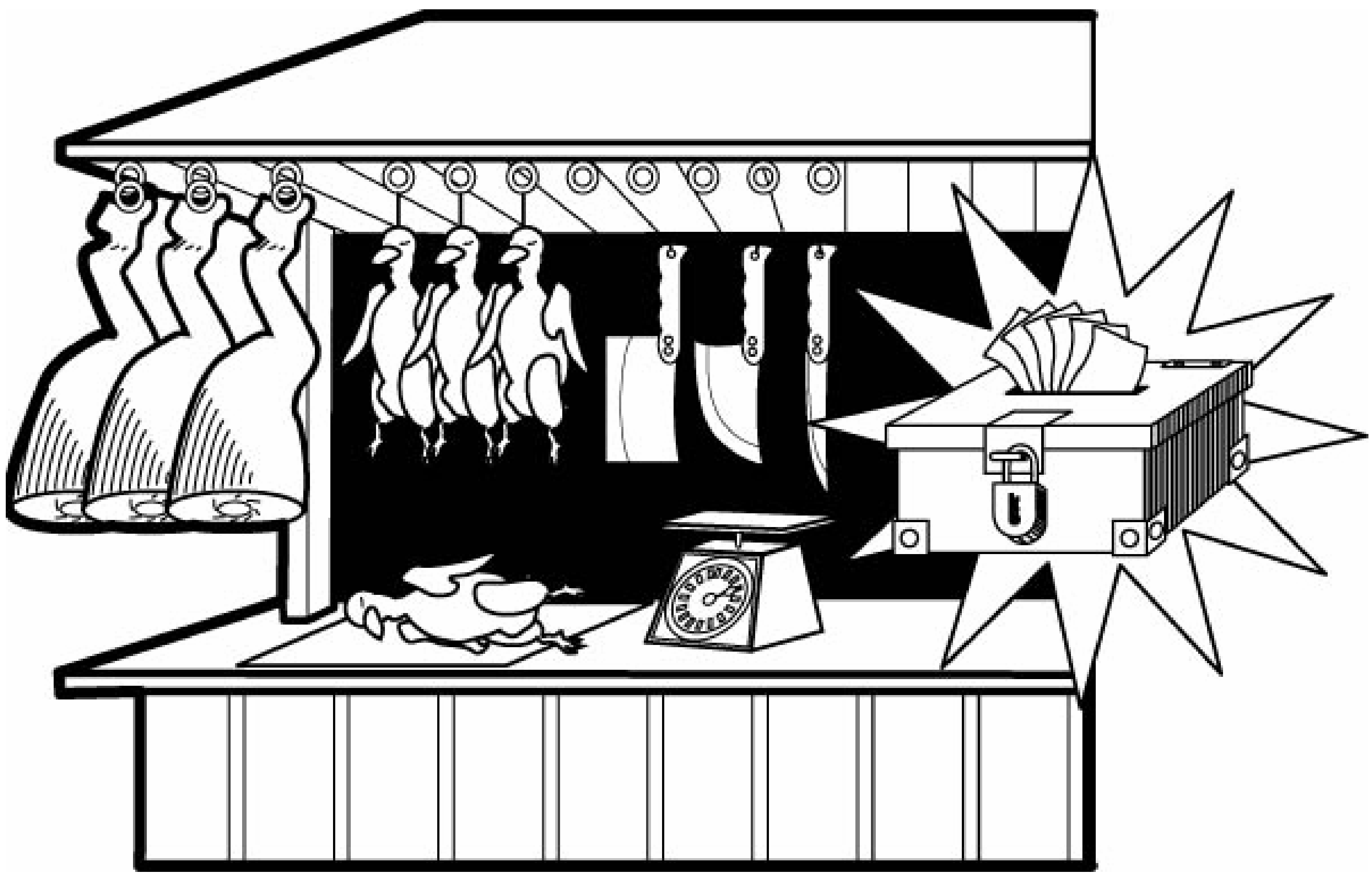


Saversocan Picture 3

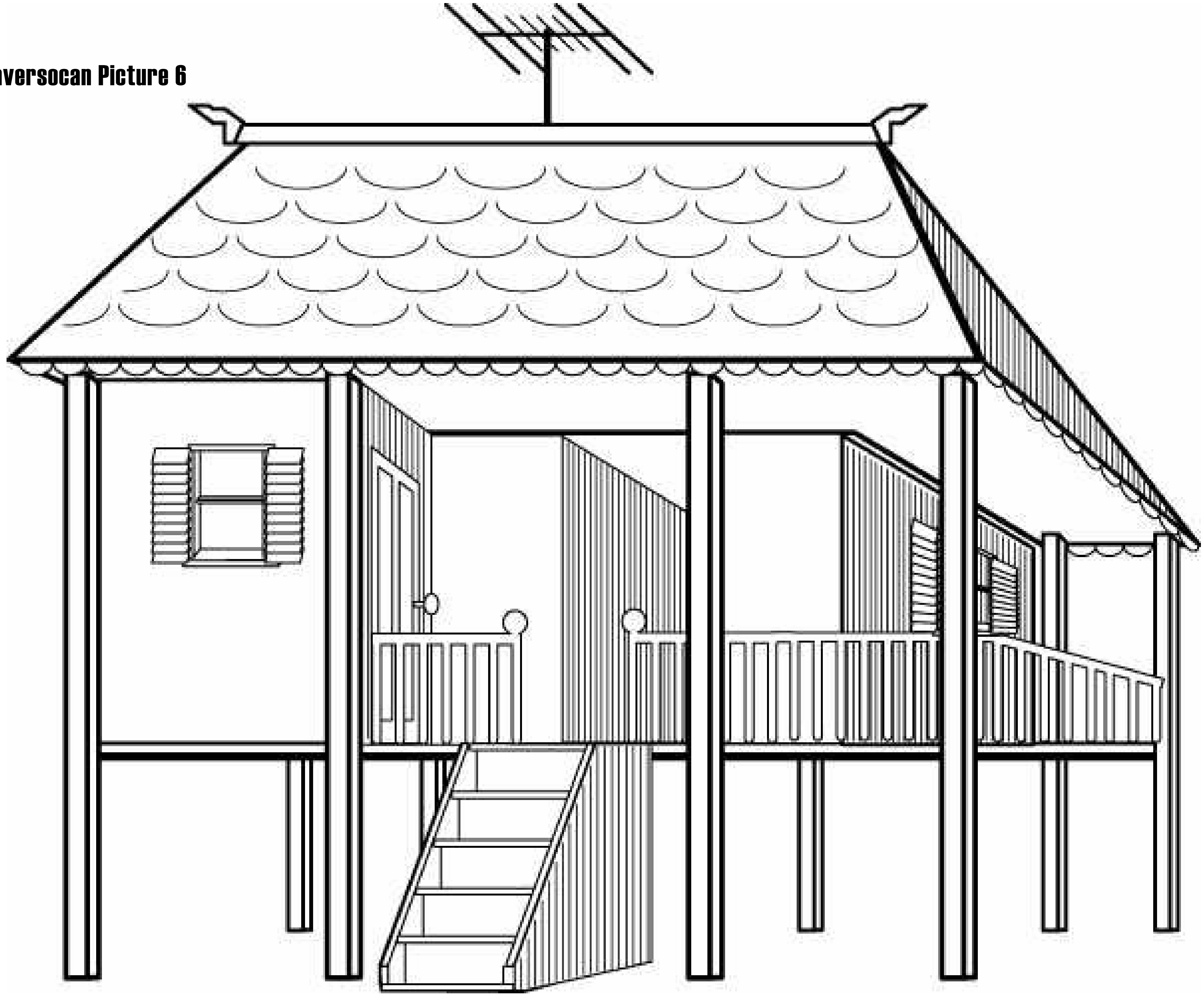
Saversocan Pi



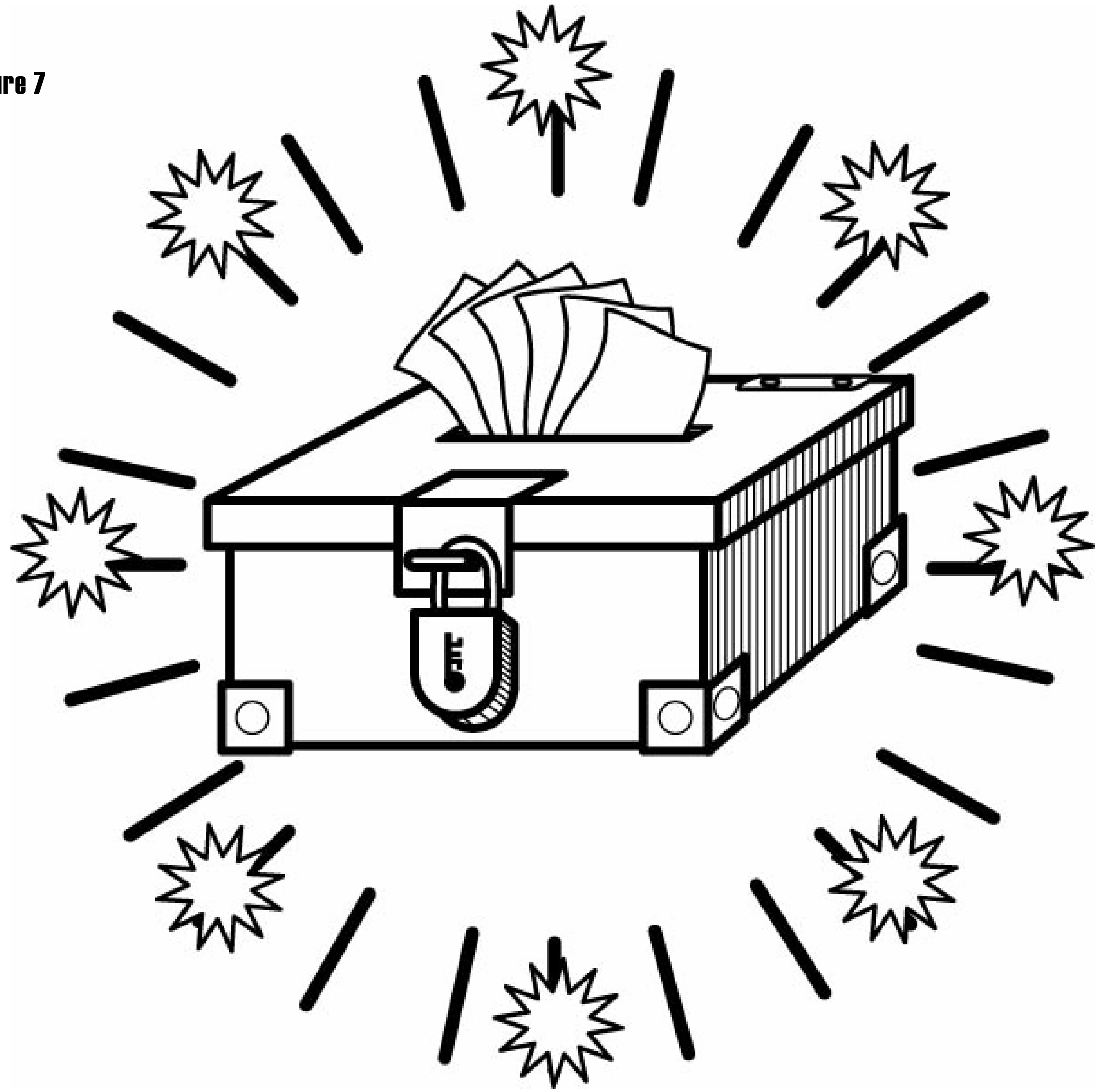
Saversocan Picture 5



Saversocan Picture 6



Saversocan Picture 7



Guidelines for Savings Requirements (Analysis)

Goals for Savings Programs

The matrix below outlines the different incentives or goals of the agency, village bank, and bank members in implementing different types of savings programs. It can be used as a discussion guide to educate both bank members and agency staff.

Savings Type	**Agency Goals**	**Village Bank Goals**	**Member Goals**
Required %, or Forced Savings	Collateral for external account loans Greater program sustainability that comes from higher external account loans	Leverage loan fund Provide capital for internal account loans Collateral for external account loans	Leverage loan Generate a return (dividend) at the cost of a lower effective rate and less access
Voluntary Savings with End of Cycle Access	Convenience and enhanced service to clients	Larger internal account loan fund Additional collateral for internal account and external account loans Convenience and enhanced service to members	Leverage for larger loan Generate a return (dividend) Asset accumulation
Voluntary Savings with 100% Access	Convenience and enhanced service to clients	Larger internal account loan fund available to community Convenience and enhanced service to members Increased member confidence	Leverage for larger loan Generate a return (dividend): highest effective rate Asset accumulation Emergencies

The table below identifies various savings-access options along with the advantages and disadvantages of each option.

Savings Access Options

Savings Access Option	Pros	Cons
Upon resignation Members usually resign at the end or beginning of a cycle if they have a current loan. Upon resignation, member no longer participates in lending or savings activities.	Reduces frequency of withdrawals, leaving a larger loan fund available to the community. Increases security for external account. Fewer transactions, shorter meeting time for members and less work for the committee. If widely lent, higher return to members.	Negative returns in high-inflation economies. Inhibits savings beyond minimum required, as members seek other, more liquid, alternatives for emergency funds. Encourages drop-out if members prefer access to savings rather than new loans.
End of cycle External account loans adjusted to reflect new savings level. For example: Cycle 2 loan 100 Savings 30 Cycle 3 loan 80 Remaining savings 10	Increases flexibility for member, yet maintains security. Fewer transactions, shorter meeting time for members and less work for the committee. The amount of internal account loan fund stable during the cycle.	Amount of the internal account fund can fluctuate significantly between cycles. Can reduce external-account borrowing, affecting program sustainability.
Complete access only if no outstanding internal account loans	Reduces risk to internal and external accounts. Provides incentive to members in good standing. May reduce member debt.	Represents a disincentive for internal account lending. Provides a disincentive to save at full capacity.
Emergency situations with bank approval (Usually an illness, failed business beyond owner's control, or other extreme family need.)	Reduces risk to internal account and external account. Provides some convenience to members.	Provides a disincentive to save at full capacity. If large amounts are withdrawn, can reduce internal account return.

Savings Access Option	Pros	Cons
Complete access with internal account loans outstanding Members can withdraw savings at any meeting.	Internal fund may increase with proper member orientation. Complete convenience to members. Higher returns to savers with an increased loan fund.	Internal account loan fund may become unstable if there is a run on the bank. Higher transaction costs in meeting time and committee oversight. Increased risk to internal and external accounts if delinquencies occur.

Recordkeeping Policies and Practices

Recordkeeping policies and practices consist of seven sets of tools as follows:

- Keeping Records for the Internal Account, an Overview
- Lending Documents
- Loan Disbursement Records
- Payment Records
- Dividend Records
- Cash Flow
- Financial Status Bar Chart

Taken together, the tools in these tool sets provide a comprehensive accounting and recordkeeping solution for a village bank's internal account loan activities.

Tool Set: Keeping Records for the Internal Account, an Overview

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To provide an overview of the practices required to adequately record activity in the internal account
Frequency	As part of initial training; as needed
Description	Short brainstorming lesson on internal account activities to be recorded and monitored

Overview of Tools

Using the Internal Account Management Toolkit (Lesson 11)

This lesson introduces the elements of the Internal Account Management recordkeeping tool set. It takes approximately thirty (30) minutes to complete the lesson.

You will need a copy of the Internal Account Information Flow Diagram (Handout L11-1) for each participant. Before you begin the lesson, you will also need one copy of each of the following:

- Overheads or enlarged copy of each recordkeeping form: Loan Contract and Payment Plan, Loan Disbursement Summary, Passbook, Individual Internal Account Loan Record, Payment Activity Summary, Dividend Calculation and Distribution Forms, Cash Flow, and Financial Status Bar Chart;
- Flipchart paper and markers.

Keeping Records for the Internal Account (Lesson 11)

Discussion

Ask participants: What do your village banks do to keep track of internal account loans?

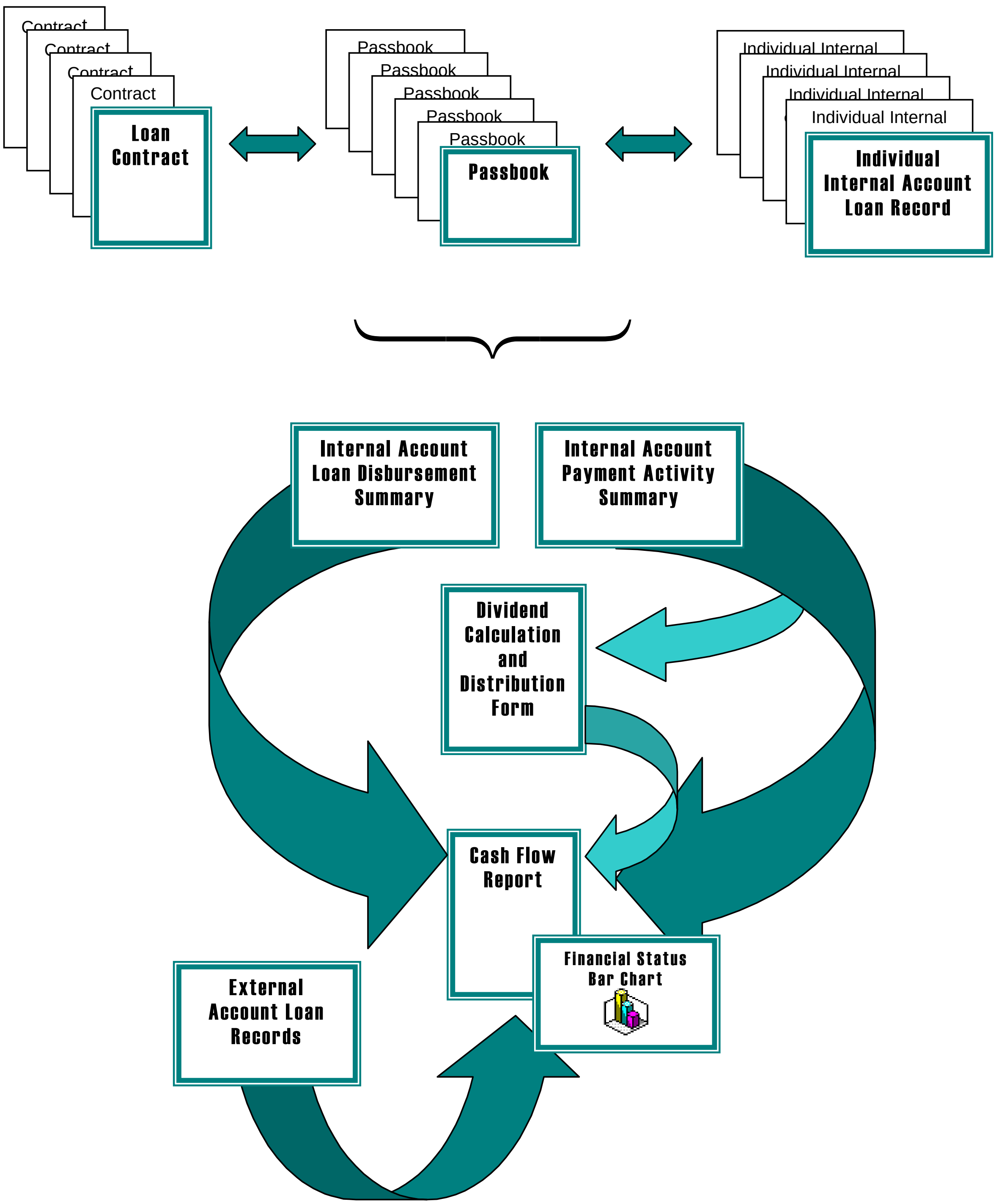
Brainstorm on the issues and problems that they have encountered with recording and monitoring these loans.

Ask participants: From your experience with internal account lending, what is the single most important thing for members to track? Record responses on flipchart.

Display the Internal Account Information Flow Diagram (Handout L11-1), and explain the components of the recordkeeping system. Provide a brief overview of the forms and the recordkeeping tools.

Finally, ask participants to imagine that they are at a village bank meeting where applications for internal account loans are analyzed, accepted, recorded and disbursed. Explain that for the next lessons, they will work their way through the recommended recordkeeping system, using sample data for five borrowers (Handout L12-3).

Handout L11-1: Internal Account Information Flow Diagram



Tool Set: Lending Documents

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To formally document internal account loans
Frequency	For each approved loan
Description	Comprehensive set of documents for approved loans, including loan contract with payment plan
Strengths	Thoroughly documents loans and provides support for potential legal action in case of delinquency
Limitations	Paper- and time-intensive; requires advanced level literacy and serious commitment by bank members

Overview of Tools

Loan Contract and Payment Plan (Form)

This tool consists of a two-sided form that includes a loan contract with a payment plan for the loan, plus a set of instructions. It contains information from the loan approval and analysis process and acts as a contract between the borrower and village bank. You should prepare one for every loan request. It clearly documents the loan terms and may serve as proof in the event legal action for collection is required.

The History section includes member information that helps the management committee and bank members to judge the reliability of the applicant based on past performance. The amount of savings an applicant has is an important factor; these savings are similar to collateral for the loan and show the level of commitment to the village bank. Regular attendance, no default and no or few late payments show that she is good risk for the internal account loan. The amount of her current external account loan is important also. If she already has a very high external account loan, she may have a hard time paying back both internal and external account loans. All of these factors should be considered in the loan analysis.

The Loan Information section shows how much was requested and approved. It also briefly states the purpose of the loan based on the loan feasibility study.

The payment plan documents the loan terms and amortization schedule. This schedule is repeated on the borrower's passbook and the village bank's individual internal account loan record.

Management committee members, loan applicant and a guarantor, if required, all sign and date the loan contract.

Using the Loan Contract and Payment Plan Form (Lesson 12)

This lesson explains the procedure for preparing a loan contract and payment plan form. It takes approximately two (2) hours to complete.

Before you begin the lesson, you will need an overhead, poster or copy of the Loan Contract and Payment Plan form, plus three copies of the blank forms for each participant. You will also need flipchart paper and markers, and enough copies of the following handouts for everyone:

- Sample Data for “Mary” Sample Exercise (L12-1),
- Borrower Profiles Sample Data for Lessons 12 – 16 (L12-3).

The lesson also includes the Solution to “Mary” Sample Exercise (L12-2) for your use.

Loan Contract (Form)

Application Date ______________________________
Village Bank Name ______________________________ Village Bank ID ______________
Cycle Number ______________________________ Week/Month No. ______________
Member Name ______________________________
Member Number ______________________________

History

Amount of savings with village bank ______________
Regular attendance at meetings? Yes ___ No ___
Most recent external account loan amount ______________
Previous internal account loan amount ______________
Balance of outstanding loans ______________
Number of late payments in most recent or current cycle (internal and external) ______________
Any default at past end of cycle? Yes ___ No ___
Number of late payments in previous cycles (internal and external accounts) ______________

Loan Information

Amount Requested ______________________ Amount Approved ______________
Purpose of Loan ____

Loan Terms

Interest Rate ________________ Principal ________________
Number of Payments ________________ Periodic Interest % ________________
Form of Payment ________________ Term ________________
Fine for Late Payment ________________ Interest Amount ________________
Due Date ________________ Total Due ________________

Payment Plan (Form)

Date	Payment	Principal	Interest	Commission	Fees	Balance

Name of Committee Member	Signature	Date
Name of Committee Member	Signature	Date
Name of Member	Signature	Date
Name of Guarantor	Signature	Date
Name of Guarantor	Signature	Date

Collateral ______________________________

____

Comments ______________________________

____

Preparing a Loan Contract and Payment Plan (Instructions)

Contract D

Loan Contract

Application Date	D		
Village Bank Name	D	Village Bank ID	D
Cycle Number	D	Week/Month No.	D
Member Name	D		
Member Number	D		

History

Amount of savings with village bank	D
Regular attendance at meetings?	D. . . . . . Yes ___ No ___
Most recent external account loan amount	D.
Previous internal account loan amount	DD
Balance of outstanding loans	D.
Number of late payments in most recent or current cycle (internal and external)	D.
Any default at past end of cycle?	D. . . . . . Yes ___ No ___
Number of late payments in previous cycles (internal and external accounts)	DD

Loan Information

Amount Requested	D.	Amount Approved	D.
Purpose of Loan	D.		

Loan Terms

Interest Rate	D.	Principal	D.
Number of Payments	DD	Periodic Interest %	D.
Form of Payment	D.	Term	D.
Fine for Late Payment	DD	Interest Amount	D.
Due Date	D.	Total Due	D.

Payment Plan

Date	Payment	Principal	Interest	Commission	Fees	Balance
D.	D.	DD	D.	D.	D.	DD

D.	D.	D.
Name of Committee Member	Signature	Date
D.	D.	DD
Name of Committee Member	Signature	Date
D.	D.	D.
Name of Member	Signature	Date
DD	D.	D.
Name of Guarantor	Signature	Date
D.	D.	D.
Name of Guarantor	Signature	Date

Collateral DD

Comments D.

Instructions for Preparing a Loan Contract and Payment Plan

Enter the information described below on the loan contract and payment plan forms:

Field	Instructions
D	Contract number, if used
D	Date of application (DD/MM/YY or MM/DD/YY)
D	Name of village bank
D	Village bank identification number
D	Village bank cycle number
D	Number of week or month in current cycle
D	Village bank member name
D	Village bank member number
D	Amount of savings borrower has in the village bank
D.	Check *Yes* or *No* to indicate whether or not the borrower regularly attends meetings
D.	Amount of most recent external account loan
DD	Amount of previous internal account loan
D.	Balance of loans outstanding to be repaid
D.	Number of late payments in most recent or current cycle in both the internal and external accounts
D.	Check *Yes* or *No* to indicate whether or not the borrower has defaulted on any loans
DD	Total number of late payments in previous cycles for internal and external accounts loans
D.	Loan amount requested by borrower
D.	Loan amount approved by village bank members
D.	Brief description of loan purpose
D.	Interest rate for the period as a percent (for example, 3% monthly or 36% annual)
D.	Amount of loan principal
DD	Number of payments to be made by borrower
D.	Periodic interest rate as a percent
D.	Form of payment—weekly, bimonthly, monthly
D.	Total number of periods over which the loan is calculated
DD	Amount of fine for late payment (specify percent of outstanding balance or amount)
D.	Amount of interest (D. x D. x D.)
D.	Date loan is due
D.	Total due by borrower (D. + D.)

Field	Instructions
D.	Date of first payment (continue down column with additional payment dates)
D.	First payment amount due (continue down column for each additional payment due)
DD	Amount of principal due (continue down column for each additional amount of principal payment due)
D.	Amount of interest due (continue down column for each additional amount of interest payment due)
D.	Amount of commissions, if any, pertaining to this loan
D.	Amount of fees, if any, pertaining to this loan
DD	Balance of loan after the payment is made (continue down column for each balance)
D.	Name of authorizing management committee member
D.	Signature of authorizing management committee member
D.	Date of authorization by management committee member
D.	Name of authorizing management committee member
D.	Signature of authorizing management committee member
DD	Date of authorization by management committee member
D.	Name of borrower
D.	Signature of borrower
D.	Date of acceptance by borrower
DD	Name of first guarantor
D.	Signature of first guarantor
D.	Date first guarantor signs contract
D.	Name of second guarantor
D.	Signature of second guarantor
D.	Date second guarantor signs contract
DD	Description of collateral or guarantee for the loan, if any
D.	Relevant comments, if any

Using the Loan Contract and Payment Plan Form (Lesson 12)

Ask participants the following questions regarding internal account policies:

- Who is eligible to borrow from the internal account? Members? Nonmembers?
- What conditions must borrowers meet?
- Can a borrower take a loan for any purpose? What types of loans are allowed?
- What interest rates are charged on loans from the internal account?

Overview of the Loan Contract

Display the internal account loan contract and payment forms using an overhead projector, flipchart paper, or a poster-size version of the form available for display and completion. Provide copies of the forms as handouts for every participant.

Review each line of the form. For those items referring to credit history, ask participants to explain why the form requires this information. When reviewing the loan terms and payment plan sections, refer back to the internal account policies the village bank has established in its bylaws.

"Mary" Payment Plan Exercise

Using the data in the sample client profile (Handout L12-1), work with participants to complete the loan contract form. The answer to this sample problem is provided in handout L12-2.

Ask participants to complete the payment plan form. Carefully explain the following points:

- There are many ways to establish a repayment schedule: weekly or monthly payments of uniform amounts; balloon payments where the bulk of the loan is paid at the end of the loan term, or interest paid up front and followed by a balloon payment of principal. Many village banks have adopted a single standardized repayment format. But flexibility is one of the advantages of the internal account and, therefore, a bank may choose to offer different types of repayment schedules adapted for each borrower and loan;

- It is vital that the borrower and the bank's management committee understand the repayment schedule, so that the borrower can make timely payments and the bank can accurately track amounts paid against amounts due;

- In the repayment schedules that you create using the sample data, all interest is paid up-front (rather than allocated to each payment period). The total amount of the payment is the same each period, but only the first includes interest; all others are principal only;

- No matter what the repayment schedule is, interest is calculated on a monthly basis. This is true even if a month passes where no payment is due.

Loan Applicants Role Play

Reproduce the page of borrower profiles (Handout L12-3) and cut it so that each borrower is on a separate strip of paper.

Display the General Information parameters from Handout L12-3 to establish the date of the loan disbursement meeting and the end-of-cycle date for the role play.

Divide the participants into pairs or small groups. Make sure each has at least two different borrowers.

Explain to participants that they will role play an interview between a loan applicant and a village bank loan committee member. The loan committee member asks the questions required to prepare the loan contract form; the loan applicant uses the information in the borrower profile to answer the questions. Then the loan committee member prepares the bottom sections of the form, including the payment schedule. Partners can offer advice. When the first interview and loan contract is complete, members of each pair should switch roles and prepare a second loan contract.

Keep in mind that different groups may be more skilled than others in filling out the forms. Have those who are faster help groups that have questions or problems.

As a group, review the loan contract forms for each of the applicants. Correct any mistakes.

Review the different payment schedules within this portfolio and emphasize that this ability to maintain various payment schedules is a unique feature of the internal account. Discuss any questions that arise.

Handout L12-1: Sample Data for "Mary" Sample Exercise

Field	Value
Name	Mary
Status	Member
Amount in Savings	15.00
Previous Internal Account Loan	None
Amount Requested	20.00
Amount Approved	20.00
Interest Rate	4% per month
Disbursement Date	January 31
Due Date	March 31
Number of Payment Periods	2
Interest Amount	1.60
Total Due	21.60

Handout L12-2: Solution to "Mary" Sample Exercise

Payment Schedule				
Date	**Payment**	**Principal**	**Interest**	**Balance**
February 28	10.80	9.20	1.60	10.80
March 31	10.80	10.80	0	0

Handout L12-3: Borrower Profiles Sample Data for Lessons 12 - 16

General Information

Field	Value
Application Date	December 15
Village Bank Name	Voted on at the beginning of the exercise
Village Bank Number	VB01
Cycle Number	3
Disbursement Date	December 31
Interest Rate	The interest rate for members is 5% per month and for nonmembers 7% per month
Payment Amounts	All payments are of equal amounts (except for rounding and, in the case of Elaine, where interest is paid as a separate payment). All interest is collected before any capital. No borrower has a loan outstanding as of 12/31.
Fines	Late payment fine is 10% of the outstanding balance for members and 15% for nonmembers.

Loan Applicant One: Ann

Ann is village bank member 01. She is in good standing with the village bank and attends every meeting. Her last external account loan was 82.00. She always pays on time and has never defaulted on a loan. This is her first request for a loan from the internal account. She is asking for 24.00 to purchase more pots for her cooked-food kiosk business in the market. Currently, Ann has 12.00 in savings with the village bank. On December 31, the village bank management committee approves Ann's loan request at half of the amount she requested—or 12.00—due in two months time. The loan is due on February 28. She will be charged an interest rate of 5% per month and will make two equal monthly payments.

Loan Applicant Two: Betty

Betty is village bank member 02. She is in good standing and attends meetings regularly. She has never defaulted on a loan and has never been late with her loan payments. Her most recent external account loan was 60.00. This is Betty's second application for a loan from the internal account. Her first internal account was for 10.00. Betty has 10.00 in savings with the village bank. Betty will use her loan to buy additional merchandise to sell at the local market. The management committee has approved Betty's request for an internal account loan of 10.00 for a term of three months. Betty will pay interest of 5% per month and will make a total of three equal monthly payments. The loan is due on March 31.

Loan Applicant Three: Carla

Carla is village bank member 03. She sometimes misses meetings because her child is weak and cannot be left alone. Carla had an external account loan of 82.00, and she had one late payment of 5.00. However, she has never defaulted on a loan and she has been a good saver with 20.00 in savings. Carla has never requested an internal account loan. Carla is asking for 25.00 to pay medical bills. She proposes to use income from her steady school uniform business to repay the loan. The management committee has approved Carla's loan for 25.00 for four months. Her loan is due on April 30. Carla will pay 5% interest per month and she will make a total of four equal monthly payments.

Loan Applicant Four: Denise

Denise is not a member of the village bank. She does not attend meetings. However, she does save with the village bank and has 20.00 in her account. She has already taken out one internal account loan of 10.00 that she repaid without any late payments or default. Denise has asked for a loan of 15.00 to purchase and fatten a pig. The management committee has approved Denise's loan request for 15.00. As a nonmember, she will pay 7% interest per month. Her loan is due in four months, on April 30, but she will repay the whole amount due—principal and interest—in one payment at the end of the four-month loan term.

Applicant Five: Elaine

Elaine is not a member of the village bank, but attends the meetings regularly. She has 15.00 in her savings account. She repaid her first loan from the internal account—worth 10.00—on time with no late payments. Now, Elaine is applying for a loan of 25.00 to expand her vegetable business. The management committee has approved a loan of 20.00 due in four months. Elaine will pay the nonmember interest rate of 7% per month. She has agreed to repay the loan in two bimonthly payments. She will repay the interest due on the loan first and the principal two months later.

Handout L12-4: Loan Contract and Payment Plan Solution for Lessons 12 - 16

Contract ______________

Loan Contract

Application Date	December 15		
Village Bank Name		Village Bank ID	VB01
Cycle Number	3	Week/Month No.	
Member Name	Ann		
Member Number	01		

History

Amount of savings with village bank	12.00
Regular attendance at meetings?	Yes 4 No ___
Most recent external account loan amount	82.00
Previous internal account loan amount	0
Balance of outstanding loans	0
Number of late payments in most recent or current cycle (internal and external)	0
Any default at past end of cycle?	Yes ___ No 4
Number of late payments in previous cycles (internal and external accounts)	0

Loan Information

Amount Requested	24.00	Amount Approved	12.00
Purpose of Loan	Purchase pots for food business.		

Loan Terms

Interest Rate	5% Month	Principal	12.00
Number of Payments	2	Periodic Interest %	5%
Form of Payment	Monthly	Term	2 Months
Fine for Late Payment	10% OB	Interest Amount	1.20
Due Date	February 28	Total Due	13.20

Payment Plan

Date	Payment	Principal	Interest	Commission	Fees	Balance
01/31	6.60	5.40	1.20			6.60
02/28	6.60	6.60	0.00			0.00

Name of Committee Member	Signature	Date
Name of Committee Member	Signature	Date
Name of Member	Signature	Date
Name of Guarantor	Signature	Date
Name of Guarantor	Signature	Date

Collateral ______________________________

____

Comments ______________________________

____

Loan Contract

Application Date	December 15		
Village Bank Name		Village Bank ID	VB01
Cycle Number	3	Week/Month No.	
Member Name	Betty		
Member Number	02		

History

Amount of savings with village bank	10.00
Regular attendance at meetings?	Yes 4 No ___
Most recent external account loan amount	60.00
Previous internal account loan amount	10.00
Balance of outstanding loans	0
Number of late payments in most recent or current cycle (internal and external)	0
Any default at past end of cycle?	Yes ___ No 4
Number of late payments in previous cycles (internal and external accounts)	0

Loan Information

Amount Requested	10.00	Amount Approved	10.00
Purpose of Loan	Purchase additional merchandise for sale in market.		

Loan Terms

Interest Rate	5% Month	Principal	10.00
Number of Payments	3	Periodic Interest %	5%
Form of Payment	Monthly	Term	3 Months
Fine for Late Payment	10% OB	Interest Amount	1.50
Due Date	March 31	Total Due	11.50

Payment Plan

Date	Payment	Principal	Interest	Commission	Fees	Balance
01/31	3.83	2.33	1.50			7.67
02/28	3.83	3.83	0.00			3.84
03/31	3.84	3.84	0.00			0.00

Name of Committee Member Signature Date

Name of Committee Member Signature Date

Name of Member Signature Date

Name of Guarantor Signature Date

Name of Guarantor Signature Date

Collateral

Comments

Loan Contract

Application Date	December 15		
Village Bank Name		Village Bank ID	VB01
Cycle Number	3	Week/Month No.	
Member Name	Carla		
Member Number	03		

History

Amount of savings with village bank	20.00
Regular attendance at meetings?	Yes ____ No 4
Most recent external account loan amount	82.00
Previous internal account loan amount	0
Balance of outstanding loans	0
Number of late payments in most recent or current cycle (internal and external)	1
Any default at past end of cycle?	Yes ___ No 4
Number of late payments in previous cycles (internal and external accounts)	0

Loan Information

Amount Requested	25.00	Amount Approved	25.00
Purpose of Loan	Pay medical bills.		

Loan Terms

Interest Rate	5% Month	Principal	25.00
Number of Payments	4	Periodic Interest %	5%
Form of Payment	Monthly	Term	4 Months
Fine for Late Payment	10% OB	Interest Amount	5.00
Due Date	April 30	Total Due	30.00

Payment Plan

Date	Payment	Principal	Interest	Commission	Fees	Balance
01/31	7.50	2.50	5.00			22.50
02/28	7.50	7.50	0.00			15.00
03/31	7.50	7.50	0.00			7.50
04/30	7.50	7.50	0.00			0.00

Name of Committee Member	Signature	Date
Name of Committee Member	Signature	Date
Name of Member	Signature	Date
Name of Guarantor	Signature	Date
Name of Guarantor	Signature	Date

Collateral ______________________________

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Comments ______________________________

____

Loan Contract

Application Date	December 15		
Village Bank Name		Village Bank ID	VB01
Cycle Number	3	Week/Month No.	
Member Name	Denise		
Member Number	N/A		

History

Amount of savings with village bank	20.00
Regular attendance at meetings?	Yes ____ No 4
Most recent external account loan amount	N/A
Previous internal account loan amount	10.00
Balance of outstanding loans	0
Number of late payments in most recent or current cycle (internal and external)	0
Any default at past end of cycle?	Yes ___ No 4
Number of late payments in previous cycles (internal and external accounts)	0

Loan Information

Amount Requested	15.00	Amount Approved	15.00
Purpose of Loan	Purchase and fatten pig.		

Loan Terms

Interest Rate	7% Month	Principal	15.00
Number of Payments	1	Periodic Interest %	7%
Form of Payment	End of Term	Term	4 Months
Fine for Late Payment	15% OB	Interest Amount	4.20
Due Date	April 30	Total Due	19.20

Payment Plan

Date	Payment	Principal	Interest	Commission	Fees	Balance
01/31	0.00	0.00	0.00			19.20
02/28	0.00	0.00	0.00			19.20
03/31	0.00	0.00	0.00			19.20
04/30	19.20	15.00	4.20			0.00

Name of Committee Member	Signature	Date
Name of Committee Member	Signature	Date
Name of Member	Signature	Date
Name of Guarantor	Signature	Date
Name of Guarantor	Signature	Date

Collateral

Comments

Loan Contract

Application Date	December 15		
Village Bank Name		Village Bank ID	VB01
Cycle Number	3	Week/Month No.	
Member Name	Elaine		
Member Number	N/A		

History

Amount of savings with village bank	15.00
Regular attendance at meetings? N/A	Yes 4 No ____
Most recent external account loan amount	N/A
Previous internal account loan amount	10.00
Balance of outstanding loans	0
Number of late payments in most recent or current cycle (internal and external)	0
Any default at past end of cycle?	Yes ___ No 4
Number of late payments in previous cycles (internal and external accounts)	0

Loan Information

Amount Requested	25.00	Amount Approved	20.00
Purpose of Loan	Expand vegetable selling business.		

Loan Terms

Interest Rate	7% Month	Principal	20.00
Number of Payments	2	Periodic Interest %	7%
Form of Payment	Bi-monthly	Term	4 Months
Fine for Late Payment	15% OB	Interest Amount	5.60
Due Date	April 30	Total Due	25.60

Payment Plan

Date	Payment	Principal	Interest	Commission	Fees	Balance
01/31	0.00	0.00	0.00			25.60
02/28	5.60	0.00	5.60			20.00
03/31	0.00	0.00	0.00			20.00
04/30	20.00	20.00	0.00			0.00

Name of Committee Member	Signature	Date
Name of Committee Member	Signature	Date
Name of Member	Signature	Date
Name of Guarantor	Signature	Date
Name of Guarantor	Signature	Date

Collateral

Comments

Tool Set: Loan Disbursement Records

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To track all internal account loan disbursements
Frequency	Each village bank meeting
Description	Disbursement summary form with instructions and a lesson in its use
Strengths	Effectively documents internal account loan disbursements
Limitations	Very paper- and time-intensive; requires advanced level of numeracy and literacy and a serious commitment by bank members

Overview of Tools

Loan Disbursement Summary (Form)

This tool includes the loan disbursement summary form and instructions for its preparation.

During each meeting, the village bank management committee should prepare a loan disbursement summary form to document the new loan disbursements that were approved during that meeting. The data required to complete the form comes from the loan contracts for each borrower and includes information on the borrower and the loan plus borrower signatures indicating agreement. The village bank president and treasurer also sign the form.

Totals at the bottom of the form indicate the amount of internal account funds disbursed during the meeting and the interest to be earned on those loans. Because most banks require that internal account loans be repaid by the end of the cycle, the data helps the village bank to project earnings for the cycle.

The borrower's passbook (a form in the Payment Records tool set that follows) also includes certain disbursement data.

Using the Loan Disbursement Summary Form (Lesson 13)

This lesson explains the procedure for completing the loan disbursement summary. It takes thirty (30) minutes to complete.

Before you begin the lesson, you will need a copy of a blank loan disbursement form for each participant.

The lesson includes a copy of Solution to Sample Problem, Lesson 13 (Handout L13-1) for your use.

Loan Disbursement Summary (Form)

Village Bank Name ______________________________ Cycle ____________

Meeting Date ______________________________

		Amount Approved						
Date	**Name of Borrower**	**Principal**	**Interest Rate**	**Interest Amount**	**Total Loan**	**Due Date**	**No. of Pmnts**	**Borrower Signature**
Totals								

Village Bank President ______________________________ Date ____________

Village Bank Treasurer ______________________________ Date ____________

Preparing a Loan Disbursement Summary (Instructions)

Village Bank Name D Cycle D

Meeting Date D

		Amount Approved						
Date	**Name of Borrower**	**Principal**	**Interest Rate %**	**Interest Amount**	**Total Loan**	**Due Date**	**No. of Pmnts**	**Borrower Signature**
D	D	D	D	D	D	D.	.	DD
						D		
Totals		D.		D.	D.			

Village Bank President DD Date D.

Village Bank Treasurer D. Date D.

Instructions for Preparing a Loan Disbursement Summary

Enter the information described below on the loan disbursement summary*:*

Field	Instructions
D	Name of village bank
D	Current village bank cycle number
D	Date of meeting
D	Date of disbursement of loan (which should correspond to a meeting date)
D	Name of borrower
D	Amount of principal disbursed
D	Interest rate of loan as a percent (for example, 3% monthly or 36% annually)
D	Amount of interest due
D	Total amount of loan
D.	Date loan is due to be paid in full (MM/DD/YY or DD/MM/YY)
D.	Number of payments to be made by borrower
DD	Signature of borrower—indicating loan information is correct and disbursement has been made
D.	Total principal disbursed at this meeting
D.	Total interest due from loans disbursed at this meeting
D.	Total amount due to village bank from loans disbursed at meeting
DD	Signature of village bank president, authorizing disbursement
D.	Date village bank president authorizes disbursement
D.	Signature of village bank treasurer, authorizing disbursement
D.	Date village bank treasurer authorizes disbursement

Using the Loan Disbursement Summary (Lesson 13)

Activities

Ask the following questions in rapid succession. Do not give participants time to calculate the answers from the loan contracts. Act surprised that they do not know the answers immediately.

- How many loans were made during this meeting?
- How much was loaned out?
- What is the total amount of interest the village bank will collect on these loans?

Are these questions important? Do we need to know the answers? Why? How can we make it easier to have this information readily available?

Keep prompting participants until they arrive at the idea of consolidating basic internal account loan information on one form per meeting (a disbursement summary).

An Alternative Activity

Perform a very short skit to show the connection between the loan application forms everyone has just practiced preparing and the loan disbursement summary form to be prepared for this lesson:

The village bank management committee is meeting to review the status of the internal account and asks the treasurer to report on the basic facts such as number of loans made and the total amount disbursed. The treasurer groans, leaves the room and returns shortly thereafter with a huge stack of application forms. She asks for everyone's patience while she totals the information from each form. Another committee member suggests that she divide up the papers among them so that they can help her. In the process, everyone becomes confused, mistakes are made and papers get disorganized until they are literally flying around the room.

Ask participants to discuss what they saw in the skit. How can this problem be overcome? Keep bringing out suggestions until you arrive at the idea of consolidating basic internal account loan information on one form per meeting.

Display the loan disbursement summary form (on an overhead or flipchart, or via handouts). Review the column headings.

Divide participants into pairs and ask them to prepare a loan disbursement summary form using the five completed loan contracts (for Ann, Betty, Carla, Denise and Elaine) from Lesson 12. Review the completed form as a group. The solution to this sample problem is provided in Handout L13-1.

Ask: What information can you get from this form that you cannot get from the individual application forms?

Answer: Total number of loans made; total amount disbursed; and amount of interest due at each meeting.

Handout L13-1: Solution to Sample Loan Disbursement Summary Problem

Loan Disbursement Summary

Village Bank Name [supplied by participants] Cycle 3

Meeting Date 12/31

		Amount Approved						
Date	**Name of Borrower**	**Principal**	**Interest Rate**	**Interest Amount**	**Total Loan**	**Due Date**	**No. of Pmnts**	**Borrower Signature**
12/31	Ann	12.00	5%	1.20	13.20	02/28	2	
12/31	Betty	10.00	5%	1.50	11.50	03/31	3	
12/31	Carla	25.00	5%	5.00	30.00	04/30	4	
12/31	Denise	15.00	7%	4.20	19.20	04/30	End of Cycle	
12/31	Elaine	20.00	7%	5.60	25.60	04/30	2	
Totals		82.00		17.50	99.50			

Village Bank President ______________________ Date ________

Village Bank Treasurer ______________________ Date ________

Tool Set: Payment Records

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To record payment activity on internal account loans during each meeting
Frequency	Each village bank meeting
Description	Three forms—Passbook (for bank members), Individual Internal Account Loan Record (for village bank), and Payment Activity Summary (for village bank)—with instructions, and a lesson covering the use of all three forms
Strengths	Effectively documents internal account loan payments
Limitations	Very paper- and time-intensive; requires advanced level of numeracy and literacy and serious commitment by bank members

Overview of Tools

A village bank uses three forms to record payments on internal account loans as follows:

- a *passbook* form that records payment information for the borrower,
- an *individual internal account loan record* that records the same information as the passbook, only for the village bank treasurer and management committee,
- a *payment activity summary* that summarizes the payments made by all internal account borrowers during a single village bank meeting.

Passbook (Form)

This tool includes a passbook form and instructions for its preparation.

The passbook, prepared by the village bank, represents a running-balance record and a receipt for the external or internal account borrower. It documents the loan disbursement plus each payment the borrower makes to repay the loan. Information recorded in the passbook must match data on loan contracts, individual account records and disbursement and repayment summaries.

Individual Internal Account Loan Record (Form)

This tool includes an individual internal account loan record and instructions for its preparation.

As a companion to the passbook, the village bank maintains individual records for each borrower, referred to as individual internal account loan records. These records are updated whenever a borrower makes a payment, and they are validated against the passbook and loan contract.

The frequency and number of payments mandated for a loan usually depend on the bank's meeting schedule and the purpose of the loan. Often, payments are weekly, monthly or biweekly. The payment schedule on the lower portion of the individual internal account loan record allows the village bank to readily track arrears.

The borrower is asked to sign the record as a validation that the amounts recorded correspond to the amounts in the borrower's passbook. When the loan is paid off or canceled, both the village bank president and treasurer sign and date the record, which is then archived for future reference.

Payment Activity Summary (Form)

This tool includes a payment activity summary and instructions for its preparation.

The payment form summarizes key information from the individual internal account loan records and the loan disbursement summary forms. Village bank committee members prepare a payment summary before each meeting to carry forward past activity and to indicate amounts due. The form records all active internal account borrowers (existing and new this meeting) and their loan payments (principal and interest) made to the village bank during the course of the meeting. In addition to documenting payments, it highlights the outstanding balance and current arrears (based on the individual internal account loan records) for each loan.

The committee member that prepares the form should verify each borrower's balance against the payment summary completed during the previous meeting and the individual internal account loan record. Once a borrower's balance reaches zero (the loan is paid off), her name drops off the list unless she takes out another loan at the meeting.

Using the Loan Payment Forms (Lesson 14)

This lesson explains the use of the passbook form, individual internal account record and payment activity summary. It takes approximately two (2) hours to complete the lesson. Participants should bring their completed loan contracts from Lesson 12.

Before you begin the lesson, you need copies of the following blank forms as handouts (and overheads, if desired):

- Passbook (five for each participant),
- Individual Internal Account Loan Records (five for each participant),
- Payment Activity Summary (four for each participant).

You will also need a single copy of each of the following handouts for each participant:

- Sample Data for Lesson 14 (L14-1),
- Sample Questions for Lesson 14 (L14-5).

The following solutions to the sample problems are provided for your convenience:

- Solution to Sample Problem: Passbooks (L14-2),
- Solution to Sample Problem: Individual Internal Account Loan Records (L14-3),

- Solution to Sample Problem: Payment Activity Summaries (L14-4),
- Answers to Sample Questions for Loan Payment Forms (L14-6)

(Optional) Wall-size, blank Payment Activity Summary form (for use during training at village bank).

Passbook (Form)

		Loan Information			Payment Information				
Pmt No.	Date	Principal Due	Interest Due	Total Due	Principal	Interest	Balance Due	Arrears	Treasurer Signature
0									
1									
2									
3									
4									
5									
6									
7									
8									
9									
10									
11									
12									
13									
14									
15									
16									

Preparing the Passbook Form (Instructions)

		Loan Information			Payment Information				
Pmt No.	Date	Principal Due	Interest Due	Total Due	Principal	Interest	Balance Due	Arrears	Treasurer Signature
0	D	D	D	D	D	D	D	D	D
1	D.	.	DD	D.	.	.	DD	D.	.
2									
3	D			D	D			D	
4									
5									
6									
7									
8									
9									
10									
11									
12									
13									
14									
15									
16									

Instructions for Preparing the Passbook Form

Enter the information described below on the passbook form.

Note that borrower's name, ID number and other relevant information will appear on the cover of the passbook.

Payment No. Line 0

D Date loan was disbursed

D Total principal disbursed

D Total interest due

D Total amount of principal and interest due (D + D)

D On Line 0, blank since no payments have yet been made

D On Line 0, blank since no payments have yet been made

D On Line 0, equals the Total Due (D)

D On Line 0, blank since no payments are due

D Village bank treasurer signs to indicate correct disbursement has been made

Payment No. Line 1 and Following Lines (Add lines as necessary)

D. Date of first payment

D. On Line 1, the amount of principal due on this date

DD On Line 1, the amount of interest due on this date

D. On Line 1, the total amount due on this date (D. + DD)

D. Amount of principal paid on this date

D. Amount of interest paid on this date

DD Outstanding balance (D – D. – D.)

D. Amount of arrears, if payment is less than amount due (a missed or a partial payment)

D. Signature of village bank treasurer indicating payment has been received

Individual Internal Account Loan Record (Form)

Borrower's Name	ID No.	Principal	Rate %	Term	Interest	Total Loan	Due Date	No of Pmts

Village Bank Name ______________________

Bank Cycle ______________________ Village Bank Number ______________________

Cycle Start Date ______________________ Cycle End Date ______________________

Date Credit Disbursed ______________________ Date Credit Due ______________________

Guarantor 1 ______________________ Guarantor 2 ______________________

Collateral ____

	Payment Date	Loan Principal	Interest	Total Due	Payments	Outstanding Balance	Arrears	Borrower's Signature
0								
1								
2								
3								
4								
5								

Village Bank President ______________________ Date ____________

Village Bank Treasurer ______________________ Date ____________

Preparing the Individual Internal Account Loan Record (Instructions)

Borrower's Name	ID No.	Principal	Rate %	Term	Interest	Total Loan	Due Date	No of Pmts
D	D	D	D	D	D	D	D	D

Village Bank Name	D.		
Bank Cycle	DD	Village Bank Number	D.
Cycle Start Date	D.	Cycle End Date	D.
Date Credit Disbursed	D.	Date Credit Due	DD
Guarantor 1	D.	Guarantor 2	D.
Collateral	D. _		

	Payment Date	Loan Principal	Interest	Total Due	Payments	Outstanding Balance	Arrears	Borrower's Signature
0	D.	.	DD	D.	.	.	DD	D.
1	D.	.	.	.	DD	D.	.	.
2	D							
3	D			D	D			
4		D	D			D	D	
5								

Village Bank President DD Date D.

Village Bank Treasurer D. Date D.

Instructions for Preparing the Individual Internal Account Loan Record

Enter the information described below on the individual internal account loan record:

Field	Instructions
D	Name of borrower
D	Borrower’s identification number
D	Total amount of loan principal
D	Interest rate as a percent (for example, 3% monthly or 36% annually)
D	Term of loan in weeks, months or other time period
D	Total amount of interest on loan
D	Total amount of the loan (D + D)
D	Date loan is due
D	Number of payments borrower must make
D.	Name of the village bank
D.	Village bank identification number
DD	Number of current village bank cycle
D.	Current cycle start date
D.	Current cycle end date
D.	Date on which loan was disbursed
DD	Date on which loan is due to be paid in full
D.	Name of first guarantor, if any
D.	Name of second guarantor, if any
D.	Description of collateral, if any

Payment No. Line 0

D.	Date the loan was disbursed
D.	Amount of loan principal
DD	Amount of loan interest
D.	Total amount due (D. + DD)
D.	On Line 0, blank
D.	On Line 0, the total amount due (D.)
DD	On Line 0, blank since no payments are due
D.	Signature of borrower

Field	Instructions
Payment No. Line 1 and following lines	
D.	Date of first payment (continue down column as additional payments are made)
D.	Amount of principal paid by borrower (continue down column as additional principal is paid)
D.	Amount of interest paid by borrower (continue down column as additional interest is paid)
D.	Amount of loan due on this date (continue down column as additional payments are made)
DD	Total amount paid by borrower on this date (continue down column as additional payments are made)
D.	Outstanding balance of loan (D. – DD)
D.	Amount of arrears, if payment is incomplete
D.	Signature of borrower indicating information is complete and accurate
DD	Upon final payment, signature of village bank president confirming information is complete and accurate
D.	Date of village bank president’s signature
D.	Upon final payment, signature of village bank treasurer confirming information is complete and accurate
D.	Date of village bank treasurer’s signature

Payment Activity Summary (Form)

Village Bank Name ______________________ Cycle No. ________ Date ____________

		Loan Payment Record					Arrears			
Borrower Name	Borrower ID No.	Total Due	Principal	Interest	Total Paid	Outstanding Balance	Arrears Days	Principal	Interest	Penalties and Fines
Balance Forward										
Totals This Meeting										
Balance to Date										

Village Bank President ______________________ Date ____________

Village Bank Treasurer ______________________ Date ____________

Comments ______________________

Preparing the Payment Activity Summary (Instructions)

Village Bank Name D Cycle No. D Date D

		Loan Payment Record					Arrears			
Borrower Name	**Borrower ID No.**	**Total Due**	**Principal**	**Interest**	**Total Paid**	**Outstanding Balance**	**Arrears Days**	**Principal**	**Interest**	**Penalties and Fines**
Balance Forward			D	D	D	D	D	D	D.	D.
DD	D.	.	.	DD	D.	.	.	.	.	DD
					D					
	D	D				D	D	D		
Totals This Meeting		D.	D.	D.	DD	D.	D.	D.	D.	D.
Balance to Date			DD	D.	D.		D.	DD	D.	D.

Village Bank President D. Date D.

Village Bank Treasurer D. Date DD

Comments D.

Instructions for Preparing the Payment Activity Summary

Enter the information described below on the payment activity summary form:

Field	Instructions
D	Name of village bank
D	Current village bank cycle number
D	Date of payment meeting
D	Balance forward of principal paid from last meeting (DD of previous meeting form, or leave blank if this is first payment meeting)
D	Balance forward of interest paid from last meeting (D. of previous meeting form, or leave blank if this is first payment meeting)
D	Balance forward of total paid from last meeting (D. of previous meeting form, or leave blank if this is first payment meeting or D + D)
D	Balance forward of outstanding balance from last meeting (D. of previous meeting from, or total outstanding balance if this is first meeting)
D	Balance forward of arrears days from last meeting (D. of previous meeting form, or leave blank if this is first payment meeting)
D	Balance forward of principal in arrears from last meeting (D. of previous meeting form, or leave blank if this is first payment meeting)
D.	Balance forward of interest in arrears from last meeting (D. of previous meeting form, or leave blank if this is first payment meeting)
D.	Balance forward of fines from last meeting (D. of previous meeting form, or leave blank if this is first payment meeting)
DD	Name of borrower with outstanding internal account loan
D.	Borrower identification number
D.	Total amount due as of this payment meeting
D.	Amount of principal paid by borrower during the meeting
DD	Amount of Interest paid by borrower during the meeting
D.	Total paid by borrower (D. + DD) during the meeting
D.	Outstanding balance owed by borrower (D. . – D.)

Field	Instructions
D.	Number of days in arrears, if any. This refers to the number of days between the date of the last actual payment and the date of the *next* scheduled payment meeting after the date this form is prepared. For example, assume a village bank has a four-month cycle with weekly payment meetings. The bank prepares this form during the fourth meeting of the cycle. It includes information on a borrower with a two-month loan taken out at the beginning of the cycle, and who failed to make payments after the first weekly meeting. The Days Overdue for this borrower should be listed as 21 (seven days each for the two payments missed during the second and third meetings, plus the seven days that will pass until the next meeting, since payments can only be made during meetings).
D.	Amount of principal in arrears (if borrower has paid past principal arrears, enter as negative amount). The committee will know if a client is in arrears as this information is taken from the individual internal account loan record, which has the schedule or due date for each payment. The amount of principal or interest in arrears is the total of outstanding loan payments according to the payment schedule. The recorder will have to refer back to the last meeting's payment summary form to update the status of arrears.
D.	Amount of interest in arrears (if borrower has paid past interest arrears, enter as negative amount)
DD	Amount of fines levied on borrower for late payment. (The fine depends on the contract. The borrower should pay it immediately. If she is not there, it should be pledged by the guarantor.)
D.	Total due as of this payment meeting (should equal outstanding balance forward column from last meeting (D)
D.	Total principal received at this payment meeting
D.	Total interest received at this payment meeting
DD	Total loan payments received at this payment meeting (D. . + . D.)
D.	Total outstanding balance at this payment meeting (D. – DD)
D.	Total number of days members are in arrears at this payment meeting
D.	Total amount of principal in arrears at this payment meeting
D.	Total amount of interest due but not paid at this payment meeting
D.	Total amount of fines collected at this payment meeting
DD	Total Principal collected to date (D. + . D.)
D.	Total Interest collected to date (D. + . D.)
D.	Total loan payments collected to date (D. + . DD) (should equal D. , Outstanding Balance)
D.	Total number of days in arrears to date (D + D.). Note: when borrower repays the amount in arrears, days in arrears is entered as a negative amount, in parentheses.

Field	Instructions
DD	Total amount of principal in arrears to date (should equal D. + D.). Note: when borrower repays the principal in arrears, principal in arrears is entered as a negative amount, in parentheses.
D.	Total amount of interest due but not paid to date (should equal D. + D.). Note: when borrower repays the interest in arrears, interest in arrears is entered as a negative amount, in parentheses.
D.	Total amount of fines collected to date (D. . + . D.)
D.	Signature of village bank president confirming payment information
D.	Date of village bank president confirmation
D.	Signature of village bank treasurer confirming payment information
DD	Date of village bank treasurer confirmation
D.	Comments regarding this payment meeting

Using the Loan Payment Forms (Lesson 14)

Opening Skit

Act out a scene to illustrate the rationale for maintaining a payment activity summary. The scene may require a few additional players recruited from among the participants:

> *It is the last bank meeting of the cycle and borrowers have repaid their internal account loans.*
>
> *The management committee is counting the money collected, separating principal from interest. Committee members check the amount of money they have on hand (or recorded in the account) against the projected amount of interest to be collected as noted on the loan disbursement summary.*
>
> *When the two numbers do not match, the treasurer tries to remember who did not pay; then another committee member suggests that maybe everyone did pay and it is in fact the treasurer who is responsible for the difference. Maybe some of the money got lost? Then a bank member reminds the treasurer of Lola, the member who had missed two payments earlier in the cycle. Lola sent in her final payment with another member before she left the village to work with her husband in the city.*

Complete the skit with the following questions:

- What is wrong with the way the treasurer and the committee have tracked the internal account loans?
- What might have happened had someone not remembered Lola's case?
- What could they have done differently?

Overview of Payment Forms

Explain that a village bank uses the following three forms to record payments on internal account loans. (See the overview for the Payment Forms set of tools for more information on the reasons for, and uses of, each of these forms):

- a passbook form contains a record of payments and belongs to the borrower,
- an individual internal account loan record provides the same information to the village bank treasurer and management committee,
- the payment activity summary records all borrowers' payments at each meeting.

Display each of these forms. Point out that the same information is recorded on each form.

Select one of the five borrowers from the sample data to use as an example. Using the information on her loan contract, prepare the three forms for the first meeting at which an internal account loan payment is due.

Exercise

Divide the participants into pairs. Post the sample data for five borrowers (Handout L14-1) on the wall, or project it from an overhead. Explain the chart and what the various boxes mean.

Using the payment schedule from the borrower's loan contracts prepared for Lesson 6 plus the actual repayment history on the handout, participants should prepare the passbooks, individual internal account loan records and payment activity summaries for the borrowers' first and second meetings. Solutions for these sample problems are provided in Handouts L14-2 through L14-4.

As a group, review each pair's work for the first and second meetings by displaying a completed payment activity summary form for each meeting. If participants' completed forms do not match yours, review them to identify the errors and ask participants to make corrections.

Return to working in pairs. Ask participants to complete the three forms for the remaining two meetings. Correct in group sessions.

Review the entire record set presented to date: loan contract, loan disbursement summary, passbook, individual internal account loan record, payment activity summary. Ask for a participant volunteer to explain the order of completion. Give another participant volunteer the set of five blank forms and ask her to put them in the order in which they are prepared.

Answer any questions the participants may have.

Follow-up Questions

Now, have some fun.

Use the questions in Handout L14-5 to encourage participants to study the forms and understand the information they provide. Make this fun by awarding points to the first group to get the right answer; award fewer points for a valiant effort, and take away points for too many good answers!

Alternatively, give these questions to the participants to work on in small groups.

Handout L14-1: Sample Data for Loan Payment Problem

Village Bank Monthly Meetings, Cycle 3				
	January 31	**February 28**	**March 31**	**April 30**
Ann	Complete Payment	Complete Payment	Paid in Full	Paid in Full
Betty	Complete Payment	Complete Payment	Complete Payment	Paid in Full
Carla	Complete Payment	Complete Payment	Missed Payment	Double Payment
Denise	No Payment Required	No Payment Required	No Payment Required	Paid 15.00 only
Elaine	No Payment Required	Complete Payment	No Payment Required	Complete Payment

Handout L14-2: Solution to Sample Problem: Passbooks

Passbook for Ann

		Loan Information			Payment Information				
Pmt No.	Date	Principal Due	Interest Due	Total Due	Principal	Interest	Balance Due	Arrears	Treasurer Signature
0	12/31	12.00	1.20	13.20	0.00	0.00	13.20		
1	01/31	5.40	1.20	6.60	5.40	1.20	6.60		
2	02/28	6.60	0.00	6.60	6.60	0.00	0.00		
3									

Passbook for Betty

		Loan Information			Payment Information				
Pmt No.	Date	Principal Due	Interest Due	Total Due	Principal	Interest	Balance Due	Arrears	Treasurer Signature
0	12/31	10.00	1.50	11.50	0.00	0.00	11.50		
1	01/31	2.33	1.50	3.83	2.33	1.50	7.67		
2	02/28	3.83	0.00	3.83	3.83	0.00	3.84		
3	03/31	3.84	0.00	3.84	3.84	0.00	0.00		

4									

Passbook for Carla

		Loan Information			Payment Information				
Pmt No.	Date	Principal Due	Interest Due	Total Due	Principal	Interest	Balance Due	Arrears	Treasurer Signature
0	12/31	25.00	5.00	30.00	0.00	0.00	30.00		
1	01/31	2.50	5.00	7.50	2.50	5.00	22.50		
2	02/28	7.50	0.00	7.50	7.50	0.00	15.00		
3	03/31	7.50	0.00	7.50	0.00	0.00	15.00	15.00	
4	04/30	7.50	0.00	7.50	15.00	0.00	0.00		
5									

Passbook for Denise

		Loan Information			Payment Information				
Pmt No.	Date	Principal Due	Interest Due	Total Due	Principal	Interest	Balance Due	Arrears	Treasurer Signature
0	12/31	15.00	4.20	19.20	0.00	0.00	19.20		
1	01/31	0.00	0.00	0.00	0.00	0.00	19.20		
2	02/28	0.00	0.00	0.00	0.00	0.00	19.20		
3	03/31	0.00	0.00	0.00	0.00	0.00	19.20		

4	04/30	15.00	4.20	19.20	15.00	0.00	4.20	4.20	
5									

Passbook for Elaine

		Loan Information			Payment Information				
Pmt No.	Date	Principal Due	Interest Due	Total Due	Principal	Interest	Balance Due	Arrears	Treasurer Signature
0	12/31	20.00	5.60	25.60	0.00	0.00	25.60		
1	01/31	0.00	0.00	0.00	0.00	0.00	25.60		
2	02/28	0.00	5.60	5.60	0.00	5.60	20.00		
3	03/31	0.00	0.00	0.00	0.00	0.00	20.00		
4	04/30	20.00	0.00	20.00	20.00	0.00	0.00		
5									

Handout L14-3: Solution to Sample Problem: Individual Internal Account Loan Records

Individual Internal Account Loan Record for Ann

Borrower's Name	ID No.	Principal	Rate %	Term	Interest	Total Loan	Due Date	No. of Pmts
Ann	01	12.00	5	2 M	1.20	13.20	02/28	2

Village Bank Name [supplied by participants]

Bank Cycle 3 Village Bank Number VB001

Cycle Start Date 12/31 Cycle End Date 04/30

Date Credit Disbursed 12/31 Date Credit Due 02/28

Guarantor 1 ______ Guarantor 2 ______

Collateral ______

	Payment Date	Loan Principal	Interest	Total Payment Due	Payments	Outstanding Balance	Arrears	Borrower's Signature
0	12/31	12.00	1.20	13.20		13.20		
1	01/31	5.40	1.20	6.60	6.60	6.60		
2	02/28	6.60	0.00	6.60	6.60	0.00		
3								

Village Bank President ______ Date ______

Village Bank Treasurer ______ Date ______

Individual Internal Account Loan Record for Betty

Borrower's Name	ID No.	Principal	Rate %	Term	Interest	Total Loan	Due Date	No. of Pmts
Betty	02	10.00	5	3 M	1.50	11.50	03/31	3

Village Bank Name	[supplied by participants]		
Bank Cycle	3	Village Bank Number	VB001
Cycle Start Date	12/31	Cycle End Date	04/30
Date Credit Disbursed	12/31	Date Credit Due	03/31
Guarantor 1		Guarantor 2	
Collateral			

	Payment Date	Loan Principal	Interest	Total Payment Due	Payments	Outstanding Balance	Arrears	Borrower's Signature
0	12/31	10.00	1.50	11.50		11.50		
1	01/31	2.33	1.50	3.83	3.83	7.67		
2	02/28	3.83	0.00	3.83	3.83	3.84		
3	03/31	3.84	0.00	3.84	3.84	0.00		

Village Bank President ______________________ Date ____________

Village Bank Treasurer ______________________ Date ____________

Individual Internal Account Loan Record for Carla

Borrower's Name	ID No.	Principal	Rate %	Term	Interest	Total Loan	Due Date	No. of Pmts
Carla	03	25.00	5	4 M	5.00	30.00	04/30	4

Village Bank Name	[supplied by participants]		
Bank Cycle	3	Village Bank Number	VB001
Cycle Start Date	12/31	Cycle End Date	04/30
Date Credit Disbursed	12/31	Date Credit Due	04/30
Guarantor 1		Guarantor 2	
Collateral			

	Payment Date	Loan Principal	Interest	Total Payment Due	Payments	Outstanding Balance	Arrears	Borrower's Signature
0	12/31	25.00	5.00	30.00		30.00		
1	01/31	2.50	5.00	7.50	7.50	22.50		
2	02/28	7.50	0.00	7.50	7.50	15.00		
3	03/31	7.50	0.00	7.50	0.00	15.00	15.00	
4	04/30	7.50	0.00	7.50	15.00	0.00		

Village Bank President ____________________ Date __________

Village Bank Treasurer ____________________ Date __________

Individual Internal Account Loan Record for Denise

Borrower's Name	ID No.	Principal	Rate %	Term	Interest	Total Loan	Due Date	No. of Pmts
Denise		15.00	7	4 M	4.20	19.20	04/30	1

Village Bank Name	[supplied by participants]		
Bank Cycle	3	Village Bank Number	VB001
Cycle Start Date	12/31	Cycle End Date	04/30
Date Credit Disbursed	12/31	Date Credit Due	04/30
Guarantor 1		Guarantor 2	
Collateral			

	Payment Date	Loan Principal	Interest	Total Payment Due	Payments	Outstanding Balance	Arrears	Borrower's Signature
0	12/31	15.00	4.20	19.20		19.20		
1	01/31	0.00	0.00	0.00	0.00	19.20		
2	02/28	0.00	0.00	0.00	0.00	19.20		
3	03/31	0.00	0.00	0.00	0.00	19.20		
4	04/30	15.00	4.20	19.20	15.00	4.20	4.20	

Village Bank President ______________________ Date ____________

Village Bank Treasurer ______________________ Date ____________

Individual Internal Account Loan Record for Elaine

Borrower's Name	ID No.	Principal	Rate %	Term	Interest	Total Loan	Due Date	No. of Pmts
Elaine		20.00	7	4 M	5.60	25.60	04/30	2

Village Bank Name [supplied by participants]

Bank Cycle 3 — Village Bank Number VB001

Cycle Start Date 12/31 — Cycle End Date 04/30

Date Credit Disbursed 12/31 — Date Credit Due 04/30

Guarantor 1 ____ Guarantor 2 ____

Collateral ____

	Payment Date	Loan Principal	Interest	Total Payment Due	Payments	Outstanding Balance	Arrears	Borrower's Signature
0	12/31	20.00	5.60	25.60		25.60		
1	01/31	0.00	0.00	0.00	0.00	25.60		
2	02/28	0.00	5.60	5.60	5.60	20.00		
3	03/31	0.00	0.00	0.00	0.00	20.00		
4	04/30	20.00	0.00	20.00	20.00	0.00		

Village Bank President ____ Date ____

Village Bank Treasurer ____ Date ____

Handout L14-4: Solution to Sample Problem: Payment Activity Summaries

Payment Activity Summary for 01/31

Village Bank Name [supplied by participants] Cycle No. 3 Date 01/31

		Loan Payment Record					Arrears			
Borrower Name	**Borrower ID No.**	**Total Due**	**Principal**	**Interest**	**Total Paid**	**Outstanding Balance**	**Arrears Days**	**Principal**	**Interest**	**Fines**
Balance Forward			0.00	0.00	0.00	99.50				
Ann	01	13.20	5.40	1.20	6.60	6.60				
Betty	02	11.50	2.33	1.50	3.83	7.67				
Carla	03	30.00	2.50	5.00	7.50	22.50				
Denise		19.20	0.00	0.00	0.00	19.20				
Elaine		25.60	0.00	0.00	0.00	25.60				
Totals This Meeting		99.50	10.23	7.70	17.93	81.57				
Balance to Date			10.23	7.70	17.93					

Village Bank President ______________________ Date ____________

Village Bank Treasurer ______________________ Date ____________

Payment Activity Summary for 02/28

Village Bank Name [supplied by participants] Cycle No. 3 Date 02/28

		Loan Payment Record					Arrears			
Borrower Name	**Borrower ID No.**	**Total Due**	**Principal**	**Interest**	**Total Paid**	**Outstanding Balance**	**Arrears Days**	**Principal**	**Interest**	**Fines**
Balance Forward			10.23	7.70	17.93	81.57				
Ann	01	6.60	6.60	0.00	6.60	0.00				
Betty	02	7.67	3.83	0.00	3.83	3.84				
Carla	03	22.50	7.50	0.00	7.50	15.00				
Denise		19.20	0.00	0.00	0.00	19.20				
Elaine		25.60	0.00	5.60	5.60	20.00				
Totals This Meeting		81.57	17.93	5.60	23.53	58.04				
Balance to Date			28.16	13.30	41.46					

Village Bank President ______________________ Date ________

Village Bank Treasurer ______________________ Date ________

Payment Activity Summary for 03/31

Village Bank Name [supplied by participants] Cycle No. 3 Date 03/31

		Loan Payment Record					Arrears			
Borrower Name	**Borrower ID No.**	**Total Due**	**Principal**	**Interest**	**Total Paid**	**Outstanding Balance**	**Arrears Days**	**Principal**	**Interest**	**Fines**
Balance Forward			28.16	13.30	41.46	58.04				
Betty	02	3.84	3.84	0.00	3.84	0.00				
Carla	03	15.00	0.00	0.00	0.00	15.00	30	15.00		1.50
Denise		19.20	0.00	0.00	0.00	19.20				
Elaine		20.00	0.00	0.00	0.00	20.00				
Totals This Meeting		58.04	3.84	0.00	3.84	54.20	30	15.00		1.50
Balance to Date			32.00	13.30	45.30		30	15.00		1.50

Village Bank President __________ Date __________

Village Bank Treasurer __________ Date __________

Payment Activity Summary for 04/30

Village Bank Name [supplied by participants] Cycle No. 3 Date 04/30

		Loan Payment Record					Arrears			
Borrower Name	**Borrower ID No.**	**Total Due**	**Principal**	**Interest**	**Total Paid**	**Outstanding Balance**	**Arrears Days**	**Principal**	**Interest**	**Fines**
Balance Forward			32.00	13.30	45.30	54.20	30	15.00		1.50
Carla	03	15.00	15.00	0.00	15.00	0.00	(30)	(15.00)		
Denise		19.20	10.80	4.20	15.00	4.20	30	4.20		0.63
Elaine		20.00	20.00	0.00	20.00	0.00				
Totals This Meeting		54.20	45.80	4.20	50.00	4.20	0	(10.80)		0.63
Balance to Date			77.80	17.50	95.30		30	4.20		2.13

Village Bank President ______________________ Date __________

Village Bank Treasurer ______________________ Date __________

Handout L14-5: Sample Questions for Loan Payment Forms

	Question	Answer
1	Why don't Denise and Elaine have member ID numbers?	
2	Based on these five borrowers, how much interest should the village bank collect by the end of the cycle?	
3	On the payment activity summary form for the January meeting, the first meeting after the internal account loans were disbursed, what does the amount listed as outstanding balance on the first line represent?	
4	What does the amount 81.57 at the bottom of that column represent? Where will we see this number again?	
5	Look at the zeros in Denise and Elaine's repayment records for this first payment activity summary form. If they haven't made their payments, why aren't the arrears columns completed?	
6	Look at Ann's record for the meeting dated February 28. Why hasn't she paid any interest this time?	
7	Look at Elaine's record for the meeting dated February 28. Why has she paid only interest and no principal?	
8	Are there any late payments in this internal account portfolio?	
9	When does the first appear?	
10	According to Carla's loan contract, how much should she pay on March 31?	
11	If Carla missed a payment of 7.50, why is the amount listed in arrears 15.00, more than the amount of the payment she missed?	
12	What happens to Carla's arrears at the next meeting?	
13	Now that Carla has paid up, is the village bank portfolio healthy again?	
14	Why, at the end of the cycle when all loans are fully due, is there still an outstanding balance of 4.20?	

	Question	Answer
15	What can the village bank management committee do to ensure payment of this balance?	
16	Look at Denise’s loan contract. What is her repayment schedule?	
17	How is it different from Ann’s, Betty’s and Carla’s?	
18	Why would a borrower need a loan structured like this?	
19	What is the risk of such a payment schedule for the village bank?	
20	Would it be okay for all internal account loans to have a balloon payment like this?	

Handout L14-6: Answers to Sample Questions for Loan Payment Forms

	Question	Answer
1	Why don't Denise and Elaine have member ID numbers?	They are not village bank members.
2	Based on these five borrowers, how much interest should the village bank collect by the end of the cycle?	17.50
3	On the payment activity summary form for the January meeting, the first meeting after the internal account loans were disbursed, what does the amount listed as outstanding balance on the first line represent?	The total amount owed by borrowers on this date
4	What does the amount 81.57 at the bottom of that column represent?	The amount owed after payments at this meeting are deducted
	Where will we see this number again?	In the outstanding balance column on the balance forward line of the next meeting form
5	Look at the zeros in Denise and Elaine's repayment records for this first payment activity summary form. If they haven't made their payments, why aren't the arrears columns completed?	Because they do not owe a payment at this time
6	Look at Ann's record for the meeting dated February 28. Why hasn't she paid any interest this time?	She paid all of her interest on her first payment in January
7	Look at Elaine's record for the meeting dated February 28. Why has she paid only interest and no principal?	Her payment plan allows her to do this
8	Are there any late payments in this internal account portfolio?	Yes
9	When does the first appear?	March 31
10	According to Carla's loan contract, how much should she pay on March 31?	7.50
11	If Carla missed a payment of 7.50, why is amount listed in arrears 15.00, more than the amount of the payment she missed?	Because the arrears amount is the amount of her loan at risk on this date which is equal to her unpaid balance
12	What happens to Carla's arrears at the next meeting?	Carla's arrears are paid
13	Now that Carla has paid up, is the village bank portfolio healthy again?	No
14	Why, at the end of the cycle when all loans are fully due, is there still an outstanding balance of 4.20?	Denise only paid 15.00 of her 19.20 payment

	Question	Answer
15	What can the village bank management committee do to ensure payment of this balance?	The management committee can contact Denise's guarantor or use her collateral to collect the amount owed
16	Look at Denise's loan contract. What is her repayment schedule?	One payment of principal and interest at the end of the loan term
17	How is it different from Ann's, Betty's and Carla's?	Denise makes no payments during the term of the loan
18	Why would a borrower need a loan structured like this?	She may need to invest in inventory or materials to make a product or plant a crop that takes several months to complete or harvest
19	What is the risk of such a payment schedule for the village bank?	The bank doesn't know until the end of the loan term whether there will be a payment problem
20	Would it be okay for all internal account loans to have a balloon payment like this?	No. It would put the internal account funds at great risk

Tool Set: Dividend Records

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To calculate total dividends for distribution, and each member's share of the distribution
Frequency	At the end of each cycle
Description	Two forms—Dividend Calculation and Dividend Distribution—with instructions and a lesson covering the use of both forms
Strengths	Equitable and systematic method for calculating and distributing village bank profits among the members
Limitations	Requires numeracy skills and commitment on the part of bank members

Overview of Tools

Dividend Calculation and Dividend Distribution (Form)

This tool includes dividend calculation and dividend distribution forms and instructions for their preparation.

The two dividend forms assist the village bank management committee to equitably calculate and distribute dividends to bank members. Dividend eligibility criteria, such as membership periods, are established in the bylaws.

The internal account profits to be distributed as dividends include interest on internal account loans, fees or fines levied by the bank, and profits from other bank investments.

The first form (Dividend Calculation) computes the total village bank profits to be distributed as dividends and the dividend factor used to allocate the total dividend among the eligible bank members. The second form (Dividend Distribution) determines the amount of the total dividend to be distributed to each eligible member based on the dividend factor. Dividends can be distributed to members in cash or, alternatively, added to the savings balances in their passbooks.

Using the Dividend Forms (Lesson 15)

This lesson explains the use of the passbook form, individual internal account record and payment activity summary. It takes approximately forty-five (45) minutes to complete the lesson.

Participants should bring their completed loan contracts for the five borrowers from Lesson 12.

Before you begin the lesson, you will need copies of blank dividend forms for each participant, and flipchart paper and markers.

Handout L15-1 provides the solution to the sample problem.

Dividend Calculation (Form)

Village Bank Name ________________ Village Bank No. __________

Village Bank Cycle ________________

Cycle Start Date ________________ Cycle End Date

Total Beginning Cycle Savings

Loan Cycle Income Information

Fees or Fines Collected

Interest on Internal Account Loans

Income from other Internal Account Activity

Expenses

Earnings Available for Dividend Distribution

Calculate Dividend Factor

Total Beginning Cycle Savings

Earnings to be Distributed

Dividend Factor (Earnings / Beginning Savings)

Bank President Date

Bank Treasurer Date

Dividend Distribution (Form)

Borrower Name	Borrower ID No.	Beginning Savings	Dividend Factor	Individual Dividends	Borrower Signature
Totals					

Bank President ______________________________ Date ____________

Bank Treasurer ______________________________ Date ____________

Preparing the Dividend Calculation and Distribution Forms (Instructions)

Village Bank Name	D	Village Bank No.	D
Village Bank Cycle	D		
Cycle Start Date	D	Cycle End Date	D

Total Beginning Cycle Savings	D
Loan Cycle Income Information	
Fees or Fines Collected	D
Interest on Internal Account Loans	D
Income from other Internal Account Activity	D
Expenses	D.
Earnings Available for Dividend Distribution	D.
Calculate Dividend Factor	
Total Beginning Cycle Savings	DD
Earnings to be Distributed	D.
Dividend Factor (Earnings / Beginning Savings)	D.

Bank President	D.	Date	DD
Bank Treasurer	D.	Date	D.

Instructions for Preparing the Dividend Calculation and Dividend Distribution Forms

Borrower Name	Borrower ID No.	Beginning Savings	Dividend Factor	Individual Dividends	Borrower Signature
D.	D.	D.	DD	D.	D.
Totals		D.		DD	

Bank President D.______________________ Date D.__________

Bank Treasurer D.______________________ Date D.__________

Instructions for Preparing the Dividend Calculation and Dividend Distribution Forms

Enter the information described below on the Dividend Calculation and Dividend Distribution forms:

Field	Instructions
D	Name of village bank
D	Village bank number
D	Current village bank cycle
D	Village bank cycle start date
D	Village bank cycle end date
D	Total amount of savings at the start of the current cycle. *Source:* Savings Journal
D	Total amount of fees and fines collected during the cycle. *Source:* payment activity summary, D.
D	Total interest collected on loans from the internal account. *Source:* payment activity summary, D. .
D	Total income from other internal account activity. *Source*: Cash Journal
D.	Total expenses during the current cycle for supplies, transportation, bank fees, committee fees, other. *Source*: Cash Journal
D.	Amount of earnings available for distribution (D + D + D – D. = D.)
DD	Amount of savings at the beginning of the current cycle (D)
D.	Amount of earnings available for distribution (D.)
D.	Dividend factor (D. divided by DD)
D.	Signature of village bank president authorizing disbursement
DD	Date village bank president authorizes disbursement
D.	Signature of village bank treasurer authorizing disbursement
D.	Date village bank treasurer authorizes disbursement
D.	Name of borrower
D.	Borrower identification number
D.	Amount of borrower savings at beginning of cycle
DD	Dividend factor (D.)
D.	Individual dividends (D. x DD)
D.	Signature of borrower confirming receipt of dividends
D.	Total amount of savings at the beginning of this cycle (must equal D)
DD	Total amount of individual earnings (must equal D.)
D.	Signature of village bank president confirming disbursement amounts
D.	Date village bank president confirms disbursement amounts

Field	Instructions
D.	Signature of village bank treasurer confirming disbursement amounts
D.	Date village bank treasurer confirms disbursement amounts

Using the Dividend Forms (Lesson 15)

Discussion

Ask participants to explain the concept of a dividend and brainstorm the sources of income for the internal account that can be paid out as dividends.

Review the village bank's policies regarding dividends, as follows:

- Who is eligible to receive dividends?
- How often are dividends paid?
- Are dividends paid in cash or credited to members' savings?

Ask: How do the village banks you work with calculate their dividends? List the various formulas or procedures mentioned.

What are the problems that can arise around the calculation and distribution of dividends? Examples include misunderstandings, competition, and mistrust among members.

Calculating the Dividend Factor

Explain that the dividend calculation form presents a simple method for calculating each member's dividend. Display the form on a flipchart or on an overhead projector. Review the calculation to arrive at the dividend factor. Explain that the dividend factor is the rate at which the internal account savings are earning money. Once figured, each member's individual savings is multiplied by the dividend factor to determine her portion of the dividend. The more savings a member has, the higher her dividend will be.

Ask participants to find a partner and work in pairs to calculate the dividend factor for the sample village bank. Provide everyone with the following information:

Total Beginning Savings = 160.00
Expenses = 5.00

Review the calculation as a group.

Calculating Member Dividends

Using the dividend distribution form, calculate Ann's dividend. Ask participants to work with their partners to calculate the dividends owed to the remaining two bank members in the portfolio. [Note: Denise and Elaine do not receive dividends because they are not members of the village bank.] The solution to this sample problem is provided in handout L15-1. Review answers as a group.

If participants require more practice in calculating dividends for individual members, add borrowers with varying amounts of beginning savings.

Review the system. Identify how it differs from what participants are doing now. Does it make sense? Is it easier or harder than what they do now?

Handout L15-1: Solution to Sample Dividends Problem

Dividend Calculation Form for Cycle 3

Village Bank Name	[supplied by participants]	Village Bank No.	VB001
Village Bank Cycle	3		
Cycle Start Date	12/31	Cycle End Date	04/30

Total Beginning Cycle Savings	160.00
Loan Cycle Income Information	
Fees or Fines Collected	2.13
Interest on Internal Account Loans	17.50
Income from other Internal Account Activity	0.00
Income from Commercial Bank Account	0.00
Expenses	5.00
Earnings Available for Dividend Distribution	14.63
Calculate Dividend Factor	
Total Beginning Cycle Savings	160.00
Earnings to be Distributed	14.63
Dividend Factor (Earnings / Beginning Savings)	0.09

Bank President	______________	Date	________
Bank Treasurer	______________	Date	________

Dividend Distribution Form for Cycle 3

Borrower Name	Borrower ID No.	Beginning Savings	Dividend Factor	Individual Earnings	Borrower Signature
Ann	01	12.00	0.09	1.08	
Betty	02	10.00	0.09	0.90	
Carla	03	20.00	0.09	1.80	
[etc.]					
Totals		160.00		14.63	

Bank President ______________________________ Date ____________

Bank Treasurer ______________________________ Date ____________

Tool Set: Cash Flow

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To reconcile cash inflows and outflows; serves as a financial report and an audit document
Frequency	Each village bank meeting
Description	Form, with instructions, and a lesson covering the use of the form
Strengths	Systematic methodology
Limitations	Time consuming; requires numeracy skills and a serious commitment on the part of bank members

Overview of Tools

Cash Flow (Form)

This tool includes a cash flow and instructions for its preparation.

The cash flow form is prepared by the management committee at each village bank meeting. This form (also referred to as a cash reconciliation) confirms that the appropriate funds have been collected and disbursed during the meeting. The amounts can later be audited against documentation including bank statements, deposit receipts, loan contracts, member passbooks, village bank ledgers and agency ledgers.

The cash flow is an important element of the village bank's records and its audit trail.

Using the Cash Flow Form (Lesson 14)

This lesson explains the use of the cash flow form. It takes approximately two (2) hours to complete the lesson.

You will also need a single copy of each of the following handouts for each participant:

- Sample Data, Mujeres Unidas Exercise (L16-1)
- Partially Completed Cash Flow Report (L16-3)

The following solutions to the sample problems are provided for your convenience:

- Solution to Mujeres Unidas Exercise (L16-2)
- Solution to Sample Cash Flow Problem (L16-4)

Cash Flow (Form)

Village Bank Name ______________________ Village Bank No. __________

	Date ______	Date ______	Date ______	Date ______	Date ______	Date ______
Balance Forward						
Cash Received						
Implementing Agency Capital						
External Account Principal						
External Account Interest						
Internal Account Principal						
Internal Account Interest						
Savings Deposits						
Other Income						
Total Cash Received						
Cash Out						
Payments to Implementing Agency						
External Account Loans Disbursed						
Internal Account Loans Disbursed						
Dividends Paid Out						
Savings Withdrawals						
Other Expenses						
Total Cash Out						
Ending Balance this Period						
Amount to be Deposited						
Amount Kept as Cash on Hand						

Bank President ______________________ Date __________

Bank Treasurer ______________________ Date __________

Preparing a Cash Flow (Instructions)

Village Bank Name D ______________________ Village Bank No. D ______

	Date	Date	Date	Date	Date	Date
	D	______	______	______	______	______
Balance Forward	D	D.				
Cash Received						
Implementing Agency Capital D						
External Account Principal D						
External Account Interest D						
Internal Account Principal D						
Internal Account Interest D						
Savings Deposits D.						
Other Income D.						
Total Cash Received DD						
Cash Out						
Payments to Implementing Agency D.						
External Account Loans Disbursed D.						
Internal Account Loans Disbursed D.						
Dividends Paid Out DD						
Savings Withdrawals D.						
Other Expenses D.						
Total Cash Out D.						
Ending Balance this Period D.						
Amount to be Deposited D.						
Amount Kept as Cash on Hand DD						

Bank President D. ______________________ Date D. ______

Bank Treasurer DD ______________________ Date D. ______

Instructions for Preparing a Cash Flow

Enter the information described below on the cash flow form:

Field	Instructions
D	Village bank name
D	Village bank number
D	Date of current payment meeting (additional meetings are recorded in subsequent columns)
D	Balance of cash on hand from previous meeting
D	Amount of implementing agency capital received, if any
D	Amount of external account principal received
D	Amount of external account interest received
D	Amount of internal account principal received
D	Amount of internal account interest received
D.	Member savings deposited at this meeting
D.	Other income received
DD	Total amount of cash received (D + D + . D + D + D + D. + D.)
D.	Payments made to implementing agency, if any
D.	Amount disbursed for external account loans
D.	Amount disbursed for internal account loans
DD	Amount of dividends paid to members
D.	Amount of savings withdrawn by members
D.	Other expenses paid at this meeting
D.	Total amount of cash paid out (D. + . D. + D. + . DD + D. + D.)
D.	Ending balance of cash on hand this meeting (D + . DD – D.)
D.	Amount of cash to be deposited in commercial bank or other agency
DD	Amount of cash kept at the village bank (D. + . DD must equal D.)
D.	Balance of cash on hand this meeting (D.) is carried forward for following meeting. This process is repeated in the next columns for subsequent meetings.
D.	Signature of village bank president certifying accuracy of report
D.	Date of certification by village bank president
DD	Signature of village bank treasurer certifying accuracy of report
D.	Date of certification by village bank treasurer

Using the Cash Flow Form (Lesson 16)

Read the descriptions of the two village banks below. After reading each, discuss the questions that follow the case studies.

Moving Forward Case Study

The village bank Moving Forward got off to a great start. The 32 members all have invested their loans in new or existing businesses. Several women are particularly happy with the savings they have made. Everyone is paying on time, too, creating even greater enthusiasm and trust. With the weekly payments of principal, interest and savings, the women are pleased that the money in their bank is piling up. But last week, when the treasurer reported the amount of cash on hand, everyone was shocked by how little was actually available for dividend payments. The treasurer tried to explain the many payments she has had to make, but several bank members didn't believe her and have accused her of not being careful with their money. The treasurer, who works very hard for the bank, was offended by these accusations and resigned from her post. Now, someone new has to be trained and the promoter won't be back for two weeks.

- Why did the members get so upset?
- What did they think was happening with the money being collected every meeting?
- How could this problem be avoided?

La Estrella Case Study

The members of the bank La Estrella struggle every meeting to understand all the numbers that their treasurer presents to them. But they know that she is explaining how much money came into the bank and how much has gone out. They know exactly who has resigned and how much they withdrew in savings. They see the amount their bank is earning in interest from the internal account lending, but they also understand that this cash does not simply sit in the bank growing every day. Some of it gets lent out again in new internal account loans; some of it goes to cover the treasurer's expenses when she has to travel to the bank. So, they are not surprised when the cash balance seems small. They like hearing the report about how the bank is working; they feel less nervous knowing that they have paid their debt to the agency on time; they are proud and grateful to their treasurer for working so hard to make it all clear.

- What is this bank doing differently?
- How does the reporting of cash in and cash out help the members?
- If several of the members don't understand all the transactions that the treasurer reports, is it worth her time to make the report?

Discussion

Ask participants how cash flows into a village bank. What are the payments that members and others make to the bank?

Ask participants to think of the ways in which cash leaves the village bank. To whom does the bank pay out money? List these responses.

What is the relationship between these inflows and outflows of cash? What do we do with the totals for each?

Mujeres Unidas Exercise

Divide the participants into pairs or small groups of three. Distribute a blank cash flow form for them to complete based on the sample data of Handout L16-1. To do so, they must complete the following steps:

- First, enter balance forward on the cash flow form;
- Then enter those items representing cash inflows to the bank onto the form, and calculate the Total Cash Received amount;
- Enter the items representing cash outflows from the bank and calculate the Total Cash Out amount;
- Finally, calculate the Ending Balance this Period and carry it forward to the beginning of the next period.

The solution to this exercise is provided in Handout L16-2. Review the groups' answers in plenary session.

Sample Problem

Explain that each participant will complete a cash flow report for each meeting of the sample village bank, based on the internal account activity of its five borrowers.

Distribute the partially completed copies of a cash flow report (Handout L16-3) to each participant.

Ask them to fill in the blanks on the form, meeting by meeting. Base the entries on the bank's payment activity summary form for each of these meetings as prepared in previous lessons. The solution is provided in Handout L16-4.

Handout L16-1: Sample Data, Mujeres Unidas Exercise

Information for village bank “Mujeres Unidas” for the period ending December 31.

Description	Amount
Internal account loans disbursed	450
External account principal	1,000
Internal account loan principal	475
Savings withdrawn	50
External account interest	120
Savings deposits	140
Payment of external account loan to agency	1,120
Other expenses	18
Dividends paid out	86
Other income	35
Balance forward from previous meeting	150
Interest payments on internal account loans	60

Handout L16-2: Solution to Mujeres Unidas Exercise

	Dec 31	Jan 31	Date	Date
Balance Forward	150	106		
Cash Received				
Implementing Agency Capital				
External Account Principal	1,000			
External Account Interest	120			
Internal Account Principal	475			
Internal Account Interest	60			
Savings Deposits	140			
Other Income	35			
Total Cash Received	1,830			
Cash Out				
Payments to Implementing Agency	1,120			
External Account Loans Disbursed				
Internal Account Loans Disbursed	450			
Dividends Paid Out	86			
Savings Withdrawals	50			
Other Expenses	18			
Total Cash Out	1,724			
Ending Balance this Period	106			
Amount to be Deposited				
Amount Kept as Cash on Hand				

Handout L16-3: Partially Completed Cash Flow Report

	Dec 31	Jan 31	Feb 28	Mar 31	Apr 30	May 31
Balance Forward	160.00					
Cash Received						
Implementing Agency Capital						
External Account Principal		61.50	61.50	61.50	61.50	
External Account Interest						
Internal Account Principal						
Internal Account Interest						
Savings Deposits	15.00	15.00	23.00	30.00	35.00	
Other Income				1.50		
Total Cash Received	15.00	101.43	115.03	103.84	153.50	
Cash Out						
Payments to Implementing Agency		68.50	68.50	68.50	68.50	
Internal Account Loans Disbursed	82.00					
Dividends Paid Out						
Savings Withdrawals						
Other Expenses						
Total Cash Out	82.00	68.50	68.50	68.50	88.13	
Ending Balance this Period						
Amount to be Deposited	68.00	100.93	147.46	182.80	248.17	
Amount Kept as Cash on Hand	25.00	25.00	25.00	25.00	25.00	

Handout L16-4: Solution to Sample Cash Flow Problem

Cash Flow Statement for 12/31 Meeting through 5/31 Meeting

	Date	Date	Date	Date	Date	Date
	12/31	01/31	02/28	03/31	04/30	05/31
Balance Forward	160.00	93.00	125.93	172.46	207.80	273.17
Cash Received						
Implementing Agency Capital						
External Account Principal		61.50	61.50	61.50	61.50	
External Account Interest		7.00	7.00	7.00	7.00	
Internal Account Principal		10.23	17.93	3.84	45.80	
Internal Account Interest		7.70	5.60	0.00	4.20	
Savings Deposits	15.00	15.00	23.00	30.00	35.00	
Other Income				1.50		
Total Cash Received	**15.00**	**101.43**	**115.03**	**103.84**	**153.50**	
Cash Out						
Payments to Implementing Agency		68.50	68.50	68.50	68.50	
Internal Account Loans Disbursed	82.00					
Dividends Paid Out					14.63	
Savings Withdrawals						
Other Expenses					5.00	
Total Cash Out	**82.00**	**68.50**	**68.50**	**68.50**	**88.13**	
Ending Balance this Period	93.00	125.93	172.46	207.80	273.17	
Amount to be Deposited	68.00	100.93	147.46	182.80	248.17	
Amount Kept as Cash on Hand	25.00	25.00	25.00	25.00	25.00	

Bank President ______________________________ Date ____________

Bank Treasurer ______________________________ Date ____________

Tool Set: Financial Status Bar Chart

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To reconcile financial status of village bank at end of meeting, including the external account, savings, internal account loan fund and earnings; serves as a financial report and an audit document
Frequency	Each village bank meeting, as needed
Description	Sample chart, with instructions, and a lesson for preparing the chart
Strengths	Presents a visual picture of bank's financial status. Members associate colors or patterns with accounts. Also provides an audit measure and financial analysis for identifying trends.
Limitations	Time-consuming. Logistically, it may be hard to implement at the bank due to setup requirements; storing the bar chart between meetings may be difficult. Some members may have difficulty with conceptualization.

Overview of Tools

Financial Status Bar Chart (Lesson 17)

This lesson explains the preparation and use of the financial status bar chart. It takes approximately two (2) hours to complete the lesson.

To create a financial status bar chart, the village bank must have up-to date bank records and the active participation of its management committee and members. By participating, members develop a sense of ownership and, hopefully, develop an increased interest in the recordkeeping and cash management practices of their bank.

The process of preparing this chart also serves as a mini-audit of the bank because the cash amounts presented on the chart for both the external and internal account loan activities must be in balance.

Before you begin the lesson, you will need a single copy of each of the following handouts for each participant:

- Sample Financial Status Bar Chart (L17-1),
- Sample Data, Lesson 17 (L17-2).

You will also need flipchart paper and colored markers (at least five different colors), plus tape or tacks to hold up the chart for the group.

Financial Status Bar Chart (Lesson 17)

Review an Existing Chart

Show a completed financial status bar chart (Handout L17-1) and briefly explain what each bar represents. For example, the first bar represents the amount of external account loan capital the bank received from the agency and the second bar displays the amount that the village bank has repaid to the agency for its external account loan.

Below each bar, demonstrate where the exact amount is entered next to the meeting date.

Ask the group to answer the following questions regarding the village bank in the sample bar chart:

- Is the village bank saving well?
- Does the village bank have any arrears? If so, are there sufficient earnings or profits to cover the arrears, if necessary?
- What is the internal account outstanding balance compared to the external account outstanding balance? Are the amounts similar or are they very different?
- Is the village bank close to repaying the agency for its external account loan?

Create a New Chart

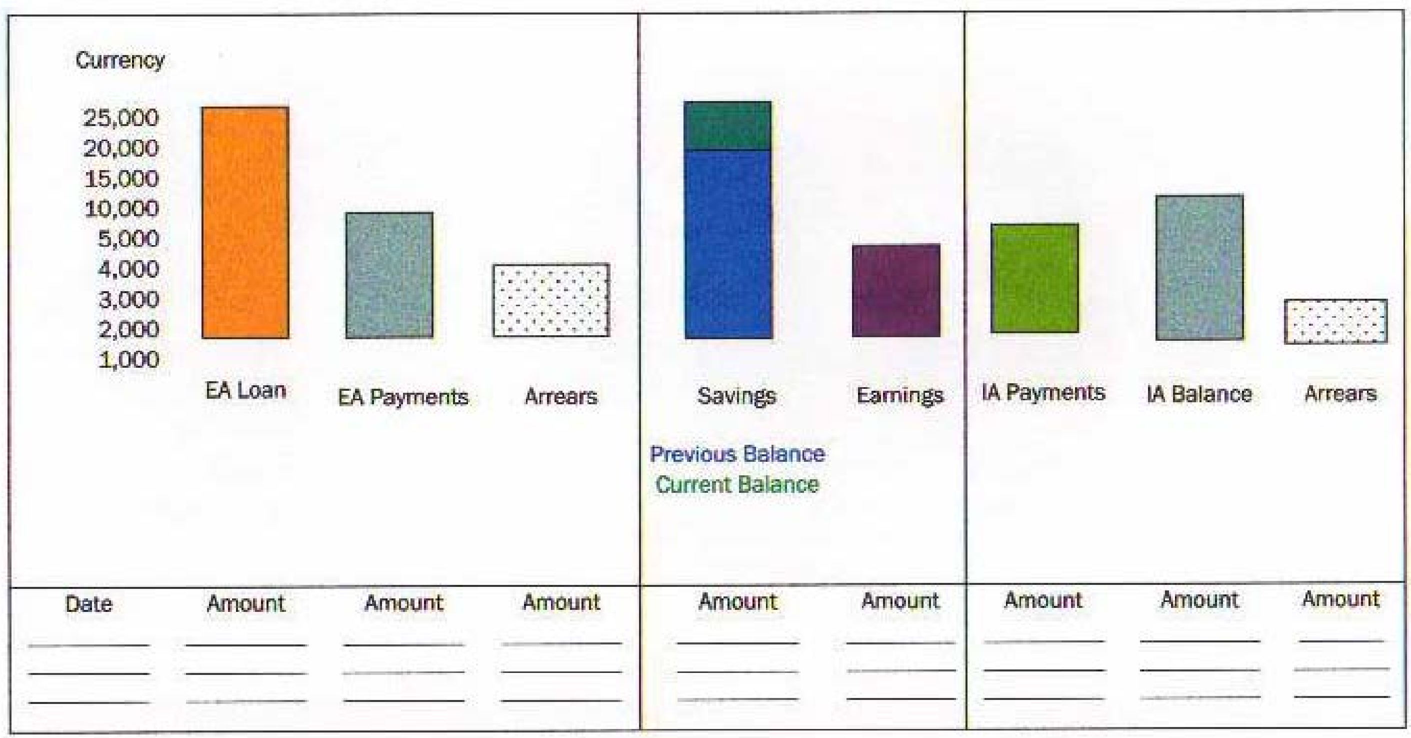
Split the group into four smaller groups and have them create their own bar charts using the sample data in Handout L17-2. Give them one hour to complete the graphs and prepare a statement about the village bank’s financial status.

Post the groups’ charts around the room. Have a representative for each group explain its chart. After each explanation, ask all participants if they have any questions or if they wish to add anything.

Time permitting, have each group modify its sample data by pretending another month has passed. Then have them make changes to their charts using their revised data sets.

Finally, point out that a graph or a picture is often a fast and easy way to communicate to a group. Get feedback from the group on how this might be used at their village bank.

Handout L17-1: Sample Financial Status Bar Chart



Handout L17-2: Sample Data, Financial Status Bar Chart

Bank A					
External Account Loan	10,000	Savings	4,500	Internal Account Payments	2,000
External Account Payments	0	Earnings	800	Internal Account Balance	2,500
External Account Arrears	2,000			Internal Account Arrears	1,000
Bank B					
External Account Loan	15,000	Savings	10,000	Internal Account Payments	2,000
External Account Payments	15,000	Earnings	2,000	Internal Account Balance	3,000
External Account Arrears	0			Internal Account Arrears	1,000
Bank C					
External Account Loan	10,000	Savings	6,000	Internal Account Payments	3,000
External Account Payments	3,000	Earnings	1,000	Internal Account Balance	3,000
External Account Arrears	2,000			Internal Account Arrears	3,000
Bank D					
External Account Loan	10,000	Savings	4,500	Internal Account Payments	2,000
External Account Payments	1,000	Earnings	1,000	Internal Account Balance	2,500
External Account Arrears	3,000			Internal Account Arrears	1,000

Preparing a Financial Status Bar Chart (Instructions)

Enter the information described below on the financial status bar chart:

Field	Instructions
Date	The meeting date for which the bar chart is prepared. (Subsequent meeting dates are listed below. The bar chart can be extended beyond the number of dates shown in the example.)
Amount	Values corresponding to the various columns on the chart
EA Loan	The amount of the external account loan received from the agency. This should match the bank/agency loan contract amount and the sum of all bank members' external account loans (from passbooks, and disbursement summary and individual internal account loan records).
EA Payments	The amount of external account payments made to the agency. This amount can be found on the agency's bank deposit slips, in the bank's savings account passbook and in the bank's cashbook.
Arrears	The amount of programmed payments that are due but unpaid as of the meeting date for which this chart is prepared. This amount can be found in the bank's external account repayment records and individual member loan registers, and passbooks.
Savings	The savings bar is divided in two parts. The lower part of the bar represents the balance of savings from the previous meeting. The upper part of the bar represents savings collected at this meeting. The total of the two sections should match the amount in the bank's savings deposit passbook plus any amounts loaned out from the internal account or on reserve.
Earnings	The amount that the bank has earned from investments, internal account lending activities and fines. The bank's cashbook and internal account lending records should contain the information for this column on the bar chart. Also, at end of cycle, the dividend distribution form includes the total earnings on the internal account during the cycle.
IA Payments	The amount of internal account payments received to date. This amount can be found in the cashbook, in members' passbooks, on the individual internal account loan record and payment activity summary.
IA Balance	The amount listed in the IA payments column amount less the amount on-lent from the internal account.
Arrears	The amount of programmed payments that should have been collected in the internal account, yet are past due as of the date of this meeting. This amount can be found in the bank's payment activity summary, troubled loan report and individual internal account loan records and passbooks.

Audit and Internal Control Policies and Practices

Internal controls and audit policies and practices consist of four sets of tools, as follows:

- Internal Controls
- Agency Audits
- Agency Mini-audits
- Bank Member Audits

The first set of tools, Internal Controls, presents a lesson for implementing internal control practices within the village bank.

The next two sets of tools provide an agency-level audit package designed to provide agency staff with sufficient tools to conduct scheduled and spot audits of a village banking program.

The final tool set in the series, Bank Member Audits, provides bank members with a procedure to audit their own bank, also reducing the opportunity for undiscovered error or fraud on the part of the management committee or promoter.

Tool Set: Internal Controls

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To provide guidelines and practice in establishing internal controls at the village bank
Frequency	During initial training, as needed thereafter
Description	A set of guidelines for establishing internal controls within the bank
Strengths	Comprehensive, relatively simple to implement
Limitations	Requires diligence and commitment on part of bank members

Overview of Tools

Internal Controls (Lesson 18)

This lesson explains the various internal and operational controls that a village bank should implement in its business practices. It takes approximately forty-five (45) minutes to complete the lesson.

Before you begin the lesson, you will need a single copy of the following handout for each participant: Summary of Operational Controls (L18-1).

You will also need the following:

- Copies of commercial bank savings book,
- Sample bank receipts,
- Sample bank records with many figures amended with correction fluid or numbers superimposed one on top of another,
- Flip chart paper and markers, or memo pads for smaller groups.

Internal Controls (Lesson 18)

This lesson demonstrates the importance of establishing and practicing internal control procedures that safeguard bank funds. If the group is large, you may want to split the participants in smaller groups.

Ask participants to define *internal control,* then discuss the ways in which they use internal controls currently. Record the definition and other commentary on flipchart paper (if one group) or on memo pads (if multiple groups). After 15 minutes, have a member of each group present the group's definition and main discussion points.

Show the group a sample signatory page from a commercial bank savings book. Ask them what observations they can make about the signatory requirements. Then ask the group for suggestions on improving the signatory procedure.

Distribute copies of sample village bank receipts that have not been serially prenumbered. See if any participants pick up on the importance of serially numbering receipts. Ask the group to discuss the advantages and disadvantages of serially numbering bank documents.

Divide the participants into small working groups. Provide each group with a copy of a passbook page, disbursement form or repayment form with amounts that have been erased, written over or whited out. Ask each group to total the values on its form.

After the groups have attempted to total their forms, ask a member from each group to describe any difficulties they may have encountered in completing the task. Ask for suggestions on how best to make changes on accounting records.

Review the specific controls mentioned on the summary in Handout L18-1.

Handout L18-1 Summary of Operational Controls

Operational Control	Pros	Cons
Multiple signatures	Widely used Easy to implement Reduces corruption	Can inhibit access to funds if a signatory is not available May encourage forgery
Multiple accounts for savings, interest, and reserves	Allows closer monitoring of accounts Improves transparency and overall management Involves more members and therefore reduces the risk of misuse of funds	Costly in terms of fees and transaction charges
Joint accounts with agency	Provides insurance against fraud	May limit access to funds due to logistics Reduces sense of ownership among members May compromise the agency in cases of fraud
Bank statements and receipts	Improved audit trail Assists in familiarizing clients with bank documents	May intimidate some members Can increase costs
Serially numbered forms	Improved audit trail to highlight missing or duplicate entries Inhibits fraud and increases transparency	Can increase costs
Only ink, no correction fluid	Decreases chance of fraud Increases transparency Conforms to standard recordkeeping practice	None
Separation of duties among recordkeepers and account signatories	Reduces risk of fraud or other misuse of funds because recordkeepers have restricted access to cash Increases transparency	In small groups or groups where illiteracy is a problem, may create difficulties because the number of available recordkeepers is limited
All transactions must take place at meetings	Increases transparency Allows for full participatory involvement and ownership	May create difficulties for members who are unable to attend meetings and are therefore unable to repay on a timely basis

Tool Set: Agency Audits

Audience	Agency staff
Purpose	To provide guideline and forms for agency staff to use in conducting scheduled and spot audits
Frequency	At scheduled and random intervals, based on the agency's audit plan; at least annually
Description	Guidelines and procedures for conducting audits. They include audit and operational procedures, financial status audit, documentation and follow-up.

Overview of Tools

Auditing a Bank, an Agency Overview (Lesson 19)

This lesson introduces the various elements of the audit tool sets, and encourages participants to focus on the purposes of an audit and the procedures for an effective audit. It takes approximately forty-five (45) minutes to complete the lesson.

Before you begin the lesson, you will need the following: flipchart paper, markers and tape.

Operations Audit for Agencies (Form)

This tool includes an operations audit for agencies form and instructions for its preparation.

Using the Operations Audit for Agencies Form (Lesson 20)

This lesson explains the use of the operations audit for agencies form. It takes approximately one (1) hour to complete the lesson.

Before you begin the lesson, you will need the following: flipchart paper, markers and tape.

Operations Audit for Agencies, Findings and Recommendations Report (Form)

This tool includes an operations audit for agencies, findings and recommendations report and instructions for its preparation.

Financial Status Audit for Agencies (Form)

This tool includes a financial status audit for agencies form and instructions for its preparation.

Using the Financial Status Audit for Agencies Form (Lesson 21)

This lesson explains the use of the financial status audit for agencies form. It takes approximately thirty (30) minutes to complete the lesson.

Before you begin the lesson you will need a blank copy of the financial status audit for agencies form and the completed information from the recordkeeping lessons.

The following solution to the sample problem is provided for your convenience: Solution to Financial Status Audit for Agencies (L21-1)

Auditing a Bank, an Agency Overview (Lesson 19)

This lesson introduces the parts of the audit tool sets, and encourages participants to focus on the purposes of an audit and the procedures for an effective audit.

What is the purpose of the audit?

Ask: What is the purpose of conducting an audit of a village bank? *(Write participant responses on a flipchart)*

Possible answers include the following:

- to ensure that there is no misuse of funds by the management committee or members,
- to ensure that there is no misuse of funds by promoters,
- to determine if village bank members or the management committee require additional technical support and, if so, the type of support,
- to determine if a promoter needs additional technical support and what type of support,
- to gauge the effectiveness of the agency's bank-level systems and to determine if they are working appropriately.

Emphasize that audits are not just watchdog tools but instructional tools to help the village bank and the agency staff to do a better job.

Divide participants into small groups and assign each group one of the questions listed below. Give the group 15 minutes to come up with answers and write them on a flipchart to hang on the wall near them. Walk to each flipchart page and have the small group explain their answers to the rest of the participants.

Following are the questions and possible answers, along with the message to be emphasized. Participants may come up with other ideas that are valid. These should be noted and explained to the group as long as they are not in conflict with the recommendations.

When should an audit be conducted?

Possible answers include: each cycle, every year, monthly and as needed. Both scheduled and unscheduled (or spot audits) are necessary. Village banks and promoters should understand that an audit could be conducted at any time; this uncertainty is an incentive to keep the records current and accurate. Village banks should be audited at least once a year—and more, if needed.

Who should do the audit?

The promoter of the village bank should not perform the audit. This would be a conflict of interest. If it is an internal audit, the audit can be conducted by supervisors, accountants or internal auditors, if available. If conducted externally, the audit can be performed by a contract auditor.

What should be audited?

Village bank records, procedures and internal controls, as specified in the financial audit and operational guidelines, should be audited. These include external account and internal account journals, passbooks, receipts, bank statements and records, cash and miscellaneous registers, as appropriate. If there is insufficient time to audit everything, a sample of transactions or records should be randomly selected. Random selection is important to keep the audit unbiased. Explain ways to do random sampling. Give each person a number and roll a die to choose which number is reviewed

Make an alphabetical list and choose every other or every third record. Keep in mind that the objective is to identify any misuse of funds, as well to as identify training or technical assistance needs.

What preparation, if any, is necessary for the village bank or the auditor?

If it is a scheduled audit—the village bank management committee should bring journals, receipts and other records that are kept. Members should bring passbooks. If it is an unscheduled visit—a spot audit—there is no warning and auditors arrive unannounced. This gives them the opportunity to see how the village bank operates on an everyday basis.

Operations Audit for Agencies (Checklist)

Village Bank No.	Date
Village Bank Name	Cycle
Address	Auditor

Use this checklist to verify that the village bank is carrying out recommended procedures. The answer to each question should be yes.

	Yes	No
General Operational Procedures		
Answer questions in the following section based on observations during the meeting and member interviews.		
The members are informed as to the financial status of the village bank:		
Loan principal repayment collected that meeting	o	o
Interest repayment collected that meeting	o	o
Savings amount collected that meeting	o	o
Total savings to date	o	o
Internal account loans disbursed that meeting	o	o
Internal account loans collected (principal and interest) that meeting	o	o
Status of late payment for external account	o	o
Status of late payments for internal account	o	o
Total cash on hand at end of meeting	o	o
Fees/fines collected that day	o	o

	Yes	No
Do village bank committee members sign passbooks each time funds are received?	o	o
Do borrowers sign passbook and/or register when funds are withdrawn or a payment made?	o	o
Is a financial statement produced at the end of each cycle and reconciled to cash (and from bank account records if applicable)? Statements may be produced on a large chart on the wall.	o	o
Select five borrower passbooks at random and answer the following questions.		
List the names of all five members with passbooks to be audited:		
1.		
2.		
3.		
4.		
5.		
Are all five borrowers' passbooks filled out and up to date?	o	o
Do all five passbooks reconcile with:		
Attendance registers	o	o
Internal account books:	o	o
Principal balance	o	o
Interest balance	o	o
Savings balance	o	o
External account books:	o	o
Principal balance	o	o
Interest balance	o	o
Answer questions in the following section based on a review of village bank records, bank receipts and interviews with management committee members.		

	Yes	No
Is there a receipt to verify collections for loan repayment and remaining cash were deposited with the implementing agency or the appropriate commercial bank in a timely manner? (All moneys should be deposited within 48 hours of collection.)	o	o
Is there is a clear separation of duties among village bank management committee members? (For example, treasurer counts and safeguards cash, secretary/accountant prepares passbook and journal entries, president reconciles cash and account journal balances.)	o	o
Are there two signatures of the management committee on the following:	o	o
Reconciliations	o	o
Accounting journal	o	o
Financial statements	o	o
Commercial bank account (if applicable)	o	o
Does the management committee receive, sign and date prenumbered receipts each time funds are received from and repaid to an institution?	o	o
Does the committee maintain a copy on file?	o	o
From a sample of transactions in the bank book and registers, is there proper documentation to support the transaction (receipts, bank statements, passbooks)?	o	o
Is ink used?	o	o
Are errors struck once through and corrections noted above?	o	o
Answer questions in the following section based on a review of village bank bylaws and a sample of internal account loan activity (including loan contracts, passbooks, internal account disbursement forms, individual internal account loan records, and payment activity summary forms).		

	Yes	No
Are all loans due before the end of cycle?	o	o
Is the policy of restricting borrowers to a single internal account loan outstanding followed?	o	o
Is the policy of no loans to agency staff followed?	o	o
Do internal account loans rotate among the members and community (are they not monopolized by a few individuals)?	o	o
Does a signed contract exist for each internal account loan where applicable?	o	o
Do all loans follow bylaw loan policy (terms, amount, eligibility)?	o	o
Are arrears of the internal account less than 5%? (This percentage can vary according to program standards.)	o	o
Are dividend calculations prepared by one committee member and reviewed by another, where applicable?	o	o
Are dividends calculated regularly and disbursed to the members according to policy?	o	o

Preparing the Operations Audit for Agencies (Instructions)

Village Bank No.	______________________	Date	______________________
Village Bank Name	______________________	Cycle	______________________
Address	______________________	Auditor	______________________

Use this checklist to verify that the bank is carrying out recommended procedures. The answer to each question should be Yes.

		Yes	No
	General Operational Procedures		
	Answer questions in the following section based on observations during the meeting and member interviews.		
	The members are informed as to the financial status of the village bank:		
D	Loan principal repayment collected that meeting	o	o
D	Interest repayment collected that meeting	o	o
D	Savings amount collected that meeting	o	o
D	Total savings to date	o	o
D	Internal account loans disbursed that meeting	o	o
D	Internal account loans collected (principal and interest) that meeting	o	o
D	Status of late payment for external account	o	o
D	Status of late payments for internal account	o	o
D	Total cash on hand at end of meeting	o	o
D.	Fees/fines collected that day	o	o
D.	Do village bank committee members sign passbooks each time funds are received?	o	o
DD	Do borrowers sign passbooks and/or registers when funds are withdrawn or payments made?	o	o
D.	Is a financial statement produced at the end of each cycle and reconciled to cash (and from bank account records, if applicable)?	o	o
	Select five borrower passbooks at random and answer the following questions:		
D.	List the names of the five members with passbooks to be audited:		
	1.		
	2.		
	3.		
	4.		
	5.		

		Yes	No
D.	Are all five borrowers' passbooks filled out and up to date?	o	o
DD	Do all five passbooks reconcile with:		
	Attendance registers	o	o
	Internal account books:		
D.	Principal balance	o	o
D.	Interest balance	o	o
D.	Savings balance	o	o
	External account books:		
D.	Principal balance	o	o
D.	Interest balance	o	o
	Answer the questions in the following section based on a review of village bank records, bank receipts and interviews with management committee members.		
DD	Is there a receipt to verify that collections for loan repayments and remaining cash were deposited with the implementing agency or the appropriate commercial bank in a timely manner? (All cash receipts should be deposited within 48 hours of collection.)	o	o
D.	Is there is a clear separation of duties among village bank management committee members? For example: treasurer counts and safeguards cash; secretary/accountant completes passbook and account journal entries; president reconciles cash and account journal balances.)	o	o
D.	Are there two signatures of the management committee on the:		
D.	Reconciliations	o	o
DD	Cash journal	o	o
D.	Financial statements	o	o
D.	Commercial bank account (if applicable)	o	o
D.	Does the management committee receive, sign and date prenumbered receipts whenever funds are received and/or repaid?	o	o
D.	Does the committee maintain a copy on file?	o	o
D.	From a sample of transactions in the bank book and registers, is there proper documentation to support the transaction (receipts, bank statements, passbooks)?	o	o
DD	Is ink used?	o	o
D.	Are errors struck once through and corrections noted above?	o	o

		Yes	No
	Answer the questions in the following section based on a review of village bank bylaws and a sample of internal account loan activity (including loan contracts, passbooks, internal account disbursement forms, individual internal account loan records, and payment activity summary forms).		
D.	Are all loans due before end of cycle?	o	o
D.	Is the policy of restricting borrowers to a single internal account loan followed?	o	o
DD	Is the policy of no loans to agency staff followed?	o	o
D.	Do internal account loans rotate among the members and community (are they not monopolized by a few individuals)?	o	o
D.	Does a signed contract exist for each internal account loan, if applicable?	o	o
D.	Do all loans follow bylaw loan policy (terms, amount, eligibility)?	o	o
D.	Are arrears of the internal account less than 5%? (This percentage can vary according to program standards.)	o	o
D.	Are dividend calculations prepared by one committee member and reviewed by another, if applicable?	o	o
DD	Are dividends calculated regularly and disbursed to the members according to policy?	o	o

Instructions for Preparing the Operations Audit for Agencies

Field	Instructions
.	Bank members should understand, and know how to find answers to, numbers D through D. below:
D.	The amount of loan principal repayment collected that meeting can be found in bank records such as the cash journal and individual account registers.
D	The amount of interest repayment collected that meeting can be found in bank records such as the cash journal and individual account registers.
D	The amount of savings collected that meeting can be found in bank records such as the cash journal and individual account registers.
D	The amount of total savings to date can be found in bank records such as the cash journal and individual account registers.
D	The amount of internal account loans disbursed that meeting can be found in member passbooks, cash journal and the internal account disbursement summary form.
D	The amount of internal account loans collected (principal and interest) that meeting can be found in the cash journal and the internal account payment summary forms.
D	The status of late payment in the external account can be found in bank records such as the individual payment summary and member passbooks.
D	The status of late payments in the internal account can be found in bank records such as the individual payment summary and member passbooks.
D	Total cash on hand at end of meeting can be determined by counting cash on hand and reviewing the cashbook.
D.	The amount of fees and fines collected that day can be found in the cashbook and on the individual payment summary forms.
D.	Management committee members should sign each passbook when payments are received as confirmation of receipt. A random sample of passbooks can be checked to confirm that this is current practice.
DD	When borrowers receive a loan or make a payment, they should sign village bank records as a confirmation along with the signatures of the management committee in the member passbooks. This can be crosschecked in the bank records and member passbooks.
D.	A financial statement can be produced at the bank level from the income statement portion of the Dividend Calculation form. The net profit is recorded on the cash flow statement as dividends disbursed. The savings balance and other income from activities carried out during the cycle (fees, fines, other) should be reconciled on the cash flow statement.
D. . - . D.	Five passbooks, randomly selected should be checked against the payment activity summaries, cash journal and village bank management committee records for each of the indicated issues. This will give the auditor an indication of how accurate the passbooks are overall.

Field	Instructions
DD	There should be a receipt from the bank or other deposit-taking institution confirming that the village bank representative(s) deposited the receipts from the last meeting within 48 hours of the close of that meeting.
D.	It is important to verify that the person who keeps the books does not safeguard cash or make deposits. This can be verified through observation and reviewing bank receipts and the village bank records.
D. .- .D.	It is important that there be more than one signature on bank reconciliations to show that more than one person checked the figures to ensure accuracy.
D. .- .D.	It is important that prenumbered receipts be signed and dated when used. This reduces fraud and creates an audit trail. Copies of the receipts should be maintained by the management committee.
D.	The auditor should select a random sample of transactions or village bank records and ensure they are supported with receipts and that they are consistent with other records (passbooks, cash journal, internal account payment summaries, external account records).
DD.- .D.	Ink should always be used. Correction fluid or Liquid Paper should never be used. If errors are made, a line should be drawn through the incorrect entry and the correction should be noted above or below the line.
D.	Whether all loans are scheduled due before end of cycle can be checked using the individual internal account loan records.
D.	Whether multiple loans are issued to members can be checked through the internal account disbursement registers and the internal account section on member passbooks.
DD	This can be verified by reviewing the list of all current loans outstanding, which are reflected on member passbooks, loan contracts and disbursement records.
D.	Whether loans are disbursed equitably in the community can be checked by reviewing the internal account disbursement records and member passbooks.
D.	The village bank should issue contracts for internal account loans to members, if the loans are sufficiently large, and to all nonmembers.
D.	Whether loan disbursement and repayment follow procedures in the bylaws can be confirmed by reviewing a sample of loans against the terms stated in the bylaws. The most convenient review procedure would be to use the individual internal account loan records that have a summary of loan terms at the top of the form.
D.	The arrears amount can be verified using the payment summary forms and checking them against individual internal account loan records and member passbooks.
D.	The dividend calculation forms and process allows auditors to check for accuracy and conformance with procedures established in the bylaws.
DD	Dividend distribution can be verified against the cash journal. Signatures of both the management committee and borrowers should appear on the dividend form.

Using the Operations Audit for Agencies Form (Lesson 20)

Discussion

Divide the group into three working groups. Give each person a copy of the Operations Audit for Agencies form, along with the instructions.

- Give group number one questions 1 through 21,
- Give group number two questions 22 through 33,
- Give group number three questions 34 through 42.

Ask participants to review each question on the checklist and respond to the questions below.

- Are these questions relevant to your agency?
- Why is it important for the agency to know the answers to these questions?
  [Answer: To find out where the weak spots are in the village bank. To identify where additional training is needed. To assess whether agency controls and systems for the village bank are working?]
- How can the agency use this information?
  [Answer: For training promoters, staff, bank members, amending bylaws and establishing internal control procedures.]

Give participants 15 minutes to review these questions, then write their answers on flipchart paper. Post the answers and highlight the common elements in the responses.

Explain that this questionnaire can be tested in the field. Some of the questions are to be answered through observation, some through questioning of members or management committee members and some by auditing records.

Questions for after the Field Visit (if applicable)

Ask the participants to answer the following questions:

- What questions were difficult to answer and why?
- What was your overall impression of the usefulness of the tool in the field?
- What issues require additional follow-up action with the bank based on the findings of this audit? (Ask for general impressions only.)

Have the respondents prepare answers on flipchart paper and present them to group. Solicit feedback from the group as to whether they agree or not with answers based on their field experience.

Operations Audit for Agencies, Findings and Recommendations Report (Form)

(The following copyrighted Operations Audit Findings and Recommendations Report is reproduced with the permission of Freedom from Hunger.)

In the case of sampling, a yes answer requires that 80% of the sample transactions be correct.

Audit Checklist:		**Completed**		
Item	**Number**	**Date**	**Yes**	**No**
D. - . D.	Informed Membership			
D. . - . DD	Counter-signing			
D.	Financial Statements			
D. . - . D.	Borrower Passbook Sample			
DD	Timely Deposits			
D.	Separation of Duties			
D. . - . D.	Bookkeeping Practices			
DD. - . D.	Use of Ink			
D. . - . DD	Internal Account Practices			
	Arrears			
	Loan Terms			
	Rotation of Funds			
	Multiple Loans			
	Dividends			

Flow of Funds Chart:

D. . [Attached to this report]

Supporting Documentation:

D. [Attached to this report]

Preparing the Operations Audit, Findings and Recommendations Report (Instructions)

Field	Instructions
D. - .D.	*Informed Membership* An informed membership can prevent mismanagement of funds through fraud or bad investment decisions. Internal account vitality depends on involved and interested members, and a capable management committee. Informed members also result in a higher quality external account. It is important for a continuing sense of solidarity and responsibility that members know and understand the status of the external and internal accounts of the village bank. If it is clear the members are uninformed, then the members and your promoter should be trained in the use of tools such as the financial status bar chart. The bank should create and display this chart at the end of each meeting.
D. . - .DD	*Countersigning* Countersignatures of members and the management committee are important controls and they also provide an audit trail. The practice allows members to compare the management committee books with the passbooks, and it allows the management committee to compare the passbook with the bank records. Both should agree and be signed. If this practice is not being carried out, a short training on the importance of countersigning is recommended and your promoter should attempt to instill this practice.
D.	*Financial Statements* Some agencies and older, more experienced banks produce financial statements at end of cycle or during cycles as a tool to inform members of the financial situation of the bank. The financial statement uses information from the dividend calculation form, the cash flow statement, and the cash journal and savings book(s). Displaying these statements keeps the members informed.
D. . - .D.	*Borrower Passbook Sample* If account records do not reconcile to the cash journal, passbooks and/or cash on hand, the management committee should not close the books for the meeting until they find errors and correct them. If more than one of five passbooks does not reconcile with account records, the management committee may require retraining in recordkeeping procedures.
DD	*Timely Deposits* The agency and group should agree on what is a timely deposit and enforce deposit procedures. Receipts should be regularly and randomly monitored by promoters. This is an area where fraud most easily occurs so any discrepancies should be addressed immediately.
D.	*Separation of Duties* Spreading risk by separating duties is important to the overall strength of the village bank, as well as an internal control measure. This may require continual refresher courses if there is turnover in the management committee or reviews to strengthen certain management committee positions. It is important that all committee members check each other’s work in order to maintain transparency.

Field	Instructions
D. .- .D.	*Bookkeeping Practices* Require that books be kept current and reconciliations be prepared consistently. All transactions should have supporting documentation (serially numbered receipts, passbooks, bank statements—depending on the type of transaction).
DD.- D.	*Use of Ink* Require use of ink and one-line cross-outs instead of correction fluid.
D. .- .DD	*Internal Account Practices* If it is clear that the group is not adhering to sound practices, a refresher session should take place with the village bank focusing on the members at large or the management committee, whichever is more appropriate. The learning session should identify the deficiencies and work with the group to identify and adopt solutions to eliminate the problems. Your promoter should closely monitor to ensure that appropriate practices are adopted. If problems persist, the supervisor should intervene. Main issues to watch for are the following: *Arrears:* Less than 5%. This is an indicator of external account health. A high arrears rate in the internal account will begin to affect the external account. *Adhering to bylaws regarding terms of loans:* If terms are not adhered to, review policy and conduct training on why exceptions are being made; make changes as appropriate. *Rotation of funds in community*: A few individuals monopolizing the internal account fund is a common occurrence. If this is due to inefficient credit analysis, the agency should reinforce good practices in allocating internal account funds. *Multiple loans:* This is unacceptable except under emergency situations and only with full membership approval. *Dividends*: Check a sample of dividends and, if necessary, schedule additional training or a policy review of dividend practices.
D.	*Flow of Funds Chart* Develop and attach a flow chart that shows the flow of funds in and out of the village bank. The chart can be used to identify potential bottlenecks or inefficiencies as well as to pinpoint high-risk operations for mismanagement or fraud.
D.	*Supporting Documentation* Attach to the report.

Financial Status Audit for Agencies (Form)

Village Bank No. ______________________ Date ______________________

Village Bank Name ______________________ Cycle ______________________

Address ____

Auditor ____

No. of Payments in Cycle (weeks/months) __________

This form is designed to facilitate a review of the internal and external financial accounts of the village bank in order to complete a reconciliation of ledgers, passbooks and other documentation.

Financial Status of External Account Loan

External account loan principal received __________

Interest payable for entire cycle __________

Total loan __________

Periodic payment amount __________

Weekly or monthly payment due to date __________

Weekly or monthly payments received __________

Delinquency in external account, if any __________

Financial Status of Internal Account Loan

Internal account loans disbursed this audit period

Internal account principal due to date in this audit period

Interest due to date in this audit period

Total due to date in this audit period

Total internal account loan payment collected

Delinquency on internal account loans

Cash Reconciliation for the Period from ____________ to ____________

Balance forward (cash on hand and cash in bank)

Revenues

External account principal collected

External account interest collected

Internal account principal collected

Internal account interest collected

Savings deposits

Other income (identify) ___________________________

Total

Outflows

Payments to agency

Disbursal of external account loan:

Internal account loans

Dividends paid out

Savings withdrawn

Other expenses (identify) _________________________

Total

Balance this period

Certification of audit:

Auditor ______________________________ Date ___________________________

Bank Officer ______________________________ Date ___________________________

Preparing the Financial Status Audit for Agencies (Instructions)

Village Bank No. D ______________ Date D ______________

Village Bank Name D ______________ Cycle D ______________

Address D ______________

Auditor D ______________

No. of Payments in Cycle (weeks/months) D ______________

This form is designed to facilitate a review of the internal and external financial accounts of the village bank in order to complete a reconciliation of ledgers, passbooks and other documentation.

Financial Status of External Account Loan

D External account loan principal received ______________

D Interest payable for entire cycle ______________

D. Total loan ______________

D. Periodic payment amount ______________

DD Weekly or monthly payment due to date ______________

D. Weekly or monthly payments received ______________

D. Delinquency in external account, if any ______________

Financial Status of Internal Account Loan

D. Internal account loans disbursed this audit period ______________

DD Internal account principal due to date in this audit period ______________

D. Interest due to date in this audit period ______________

D. Total due to date in this audit period ______________

D. Total internal account loan payment collected ______________

D. Delinquency on internal account loans

D. **Cash Reconciliation for the Period**
from ____________ to ____________

DD Balance forward (cash on hand and cash in bank) ____________

D. **Revenues**

D. External account principal collected ____________

D. External account interest collected ____________

DD Internal account principal collected ____________

D. Internal account interest collected ____________

D. Savings deposits ____________

D. Other income (identify) ________________________ ____________

D. Total ____________

D. **Outflows**

DD Payments to agency

D. Disbursal of external account loan:

D. Internal account loans ____________

D. Dividends paid out ____________

DD Savings withdrawn ____________

D. Other expenses (identify) ________________________ ____________

D. Total ____________

D. Balance this period ____________

D. Certification of audit:

Auditor ________________________ Date ________________________

Bank Officer ________________________ Date ________________________

Instructions for Preparing the Financial Status Audit for Agencies

Field	Instructions
D	The number of the village bank, if any
D	The name of the village bank
D	The village bank meeting place—the village or town name and address as it is best described.
D	Full name of the person who prepares this form
D	The date of the audit
D	Current cycle of the village bank
D	The number of times during the cycle that the external account payment is collected by the agency
	Financial Status of External Account Loan
	This section verifies that the village bank's loan information and balance are equal to the balance in the records managed by the agency, and that the external account loan is current.
	Verification source for items. D through D. should be detailed in the loan contract with the implementing agency
D	External account loan principal received. The amount of external account principal received by the village bank from the agency during the cycle. *Source*: current cycle loan registers
D	Interest payable for entire cycle. Amount of interest due over the life of the loan. *Source*: current cycle loan agreement
D.	Total loan. The sum of D. + D. *Source*: current cycle loan agreement
D.	Periodic payment amount. The amount on D. . divided by the number of payment periods per cycle. *Source*: current cycle loan agreement
DD	Weekly or monthly payment due to date. The amount the agency should have collected from the village bank to date. *Source*: D. amount multiplied by the number of periods to date
D.	Weekly or monthly payments received. The amount the agency actually collected from the village bank. *Source*: total of agency's receipts compared against the village bank books (cash flow and external account records). This can also be supported by adding up the external account payment amounts in all the passbooks.

Field	Instructions
D.	Delinquency in external account, if any, DD. – . D. . . Members who are in arrears or late with one or more payments as of the audit date. *Source*: review each member's passbook to see if it corresponds to the cashbook and external account ledger records of the village bank. It is important to verify the agency's receipt of funds by referencing serially numbered receipts, bank statements or other signed and dated documents. *Note: For external account payments and outstanding balance: Balance from village bank records = agency records = sum of individual passbooks.*
	Financial Status of Internal Account Loan *Similar to the external account, village bank internal account loan information must balance between member passbooks, village bank committee books, supporting bank records or other receipts along with agency records.*
D.	Internal account loans disbursed this audit period. *Source*: Loan disbursement summary forms, compared against individual internal account loan records and passbooks
DD	Internal account principal due to date in this audit period. The amount of internal account principal that should have been collected to date during the audit period. *Source*: individual internal account records, loan contracts
D.	Interest due to date in this audit period. The amount of internal account interest that should have been collected to date during the audit period. *Source*: individual internal account loan records, loan contracts
D.	Total due to date in this audit period. The sum of DD + D. .
D.	Total internal account loan payment collected. The amount of internal account principal and that interest has been collected during the audit period. *Source*: payment activity summary compared against individual internal account loan records and passbooks
D.	Delinquency on internal account loans, D. – D.
D.	Cash reconciliation for the period from ________ to ________. The time period for which cash is to be reconciled. *Source*: cashbook, bank statement and receipts (if applicable), cash on hand, village bank records
DD	Balance forward (cash on hand and cash in bank). The village bank's cash balance, including amounts on hand and amounts deposited in a commercial bank or other financial institution, at the beginning of the reconciliation period in D. above. *Source*: cash flow statement for the relevant time period, count of cash, bank statement
D.	Revenue. Heading for cash inflows to the village bank
D.	External account principal collected. *Source*: village bank records, passbooks
D.	External account interest collected. *Source*: village bank records, passbooks
DD	Internal account principal collected. *Source*: payment activity summary forms
D.	Internal account interest collected. *Source*: payment activity summary forms
D.	Savings deposits. *Source*: passbooks, cash flow, village bank records

Field	Instructions
D.	Other income (identify). *Source*: village bank records
D.	Total. Sum of D. through D.
D.	Outflows. Heading for cash outflows from the village bank
DD	Payments to agency. *Source*: receipts from agency, village bank records, cash flow
D.	Disbursal of external account loan. *Source*: village bank records, passbooks
D.	Internal account loans. *Source*: loan disbursement summary
D.	Dividends paid out. *Source*: dividend disbursement form, cash flow
DD	Savings withdrawn. *Source*: passbooks, village bank records
D.	Other expenses (identify). *Source*: cash flow, receipts
D.	Total. Sum of DD + D. – D.
D.	Balance this period: D. . – D. . Village bank cash balance at end of the audit period
D.	Certification of Audit. The signature of the auditor and committee member who declare the audit was accurately preformed. These signatures should have the same date.

Note: The amounts on this reconciliation should agree with village bank records and passbooks, agency records and bank statements. Also use cash flows prepared during the cycle as source documentation to verify accuracy.

Using the Financial Status Audit for Agencies Form (Lesson 21)

Exercise

Distribute a financial status audit form to each participant. Participants should have sample data and completed exercises from the recordkeeping lessons available for reference.

The following information should be displayed on a flipchart at the front of the room.

- The audit takes place on: April 30
- External account loan principal the bank received at the beginning of the cycle: 246.00
- Interest payable for the entire cycle: 28.00
- External account delinquencies: 0

In pairs or individually, ask participants to complete the audit form. You should walk around the room and help out those who need it.

As a group, after participants have completed their forms, ask them to assist you in completing an enlarged sample of the audit form. (The solution is provided in handout L21-1) As you enter each field, ask participants if anyone has a different answer.

Correct mistakes, if any, on the audit form and review the source for each item of information. Emphasize the importance of the payment summaries, disbursement summaries, and dividend and cash flow forms as a way to validate this information.

Ask for feedback from the group: While this audit tool works well with the recordkeeping system provided in this toolkit, would it work well with other accounting systems?

Handout L21-1: Solution to Financial Status Audit for Agencies

Village Bank No. ______________________ Date ______________________

Village Bank Name ______________________ Cycle ______________________

Address ____

Auditor ____

No. of Payments in Cycle (weeks/months) ____________

This form is designed to facilitate a review of the internal and external financial accounts of the village bank in order to complete a reconciliation of ledgers, passbooks and other documentation.

Financial Status of External Account Loan

External account loan principal received	246.00
Interest payable for entire cycle	28.00
Total loan	274.00
Periodic payment amount	68.50
Weekly or monthly payment due to date	274.00
Weekly or monthly payments received	274.00
Delinquency in external account, if any:	0.00

Financial Status of Internal Account Loan

Internal account loans disbursed this audit period	82.00
Internal account principal due to date in this audit period	82.00
Interest due to date in this audit period	17.50
Total due to date in this audit period	99.50
Total internal account loan payment collected	95.30
Delinquency on internal account loans	4.20

Cash reconciliation for the period from ____________ to ____________

Balance forward of cash on hand and cash in bank		160.00
Revenues		
External account principal collected	246.00	
External account interest collected	28.00	
Internal account principal collected	77.80	
Internal account interest collected	17.50	
Savings deposits	118.00	
Other income (identify) ____________________________	1.50	
Total		488.80
Outflows		
Payments to agency	274.00	
Disbursal of external account loan:	0.00	
Internal account loans	82.00	
Dividends paid out	14.63	
Savings withdrawn	0.00	
Other expenses (identify) ____________________________	5.00	
Total		375.63
Balance this period		273.17

Certification of audit:

Auditor ______________________________ Date ____________________________

Bank Officer ______________________________ Date ____________________________

Tool Set: Agency Mini-audits

Audience	Agency staff
Purpose	To identify problem areas when a full-scale audit of the village bank is not possible or practical
Frequency	As necessary
Description	Form (checklist) and instructions
Strengths	Simple and practical alternative to full-scale audit
Limitations	Less comprehensive and time-consuming than a full-scale audit

Overview of Tools

Village Bank Health Checklist, for Agencies (Checklist)

This tool includes a village bank health checklist form and instructions for its preparation.

The health checklist helps you to identify those areas for which a specific village bank may need additional assistance when you do not have time to conduct a full agency audit.

It takes approximately two (2) hours to perform the check.

Village Bank Health Checklist, for Agencies

If you do not have time to conduct a full agency audit of a specific village bank, the health checklist helps to identify those areas in which the bank may need additional assistance.

Questions	Yes	No
Participation		
Does the village bank keep attendance for all bank meetings?	o	o
Did more than 90% of members attend the last meeting?	o	o
Did the management committee run the meeting with minimal promoter assistance?	o	o
Is a loan analysis conducted before approving internal account loans?	o	o
Bookkeeping / Audit		
Is the internal account journal up to date and correct?	o	o
Is the external account journal up to date and correct?	o	o
Do five member passbooks match those of external account journals?	o	o
Do five member passbooks match those of internal account journals?	o	o
Operational Controls		
Do different members of the management committee control cash, and who keep the journals?	o	o
Does the management committee sign the passbook when funds are disbursed or received from members?	o	o
Does every member sign the management committee journal when repaying or receiving funds?	o	o
Is there a receipt showing collected funds are deposited within 48 hours?	o	o
Is ink always used and liquid paper never used?	o	o
Profitability		
Is the village bank earning a profit from its internal account loan activity?	o	o
Are members receiving a return on their savings?	o	o
Score the health checklist by adding up the total number of yes *answers and dividing the total by 15 (the total number of questions).*	________%	

Tool Set: Bank Member Audits

Audience	Village bank management committee, bank members, agency staff in training
Purpose	To assist village bank members in auditing their bank's records
Frequency	As part of initial training; each village bank meeting or as needed
Description	Procedures form and lesson to guide bank members in conducting audits
Strengths	Administered by bank members, fostering member control and responsibility; teaches practical skills; systematic approach; consistent use helps to discover errors and misuse of funds
Limitations	May be too complex and time-consuming for some banks; requires training

Overview of Tools

Regular and systematic bank audits encourage village bank members to become familiar with the bank's recordkeeping system, and guard against errors and possible fraud. Bank members should regularly audit their own passbooks to ensure that they are correct.

Audit Procedures for Bank Members (Form)

This tool presents three simple audit procedures for bank members and instructions for their completion.

Audit a Bank: Bank Member Audit Guidelines (Lesson 22)

This lesson explains the importance of bank audits conducted by bank members. It takes approximately twenty (20) minutes to complete the lesson.

Before you begin the lesson, you will need the following:

- Management committee's books and bank statements and member passbooks,
- Audit Procedures for Bank Members form, with sample data,
- Audit tables prepared in a large format so that the participants can see them.

Other Tools

The cash flow and financial status bar chart (prepared by members at each bank meeting) can also be used as bank member audit tools.

Audit Procedures for Bank Members (Form)

Audit One: Comparison of Passbooks and Bank Records

Select five bank members at random and validate their passbooks against the bank's accounting records.

Village Bank Passbook Numbers	Committee Register Numbers
	1.
	2.
	3.
	4.
	5.

Audit Two: Bank Statement Reconciliation

Choose a bank member at random to verify that the commercial bank statements reconcile with the cash in bank amount shown in the village bank's records and on its cash flow statement.

Verify that savings and payment amounts per the village bank's records have been deposited with the commercial bank in full and on a timely basis (within 48 hours, if possible).

Compare bank deposit receipts with the commercial bank statement and the village bank records.

Bank Statement Balance Date	Bank Register Balance Date

Audit Three: Cash Reconciliation for a Meeting

Choose a bank member at random to verify that the sum of the amounts in the first five lines on the form (representing cash outflows) equals the value on line six (cash inflows).

Village Bank Member Cash Reconciliation Sheet		
1	How much cash was used to repay external account debt (by depositing it with the agency or transferring it to a commercial bank)?	
2	How much cash was lent out as internal account loans?	
3	How much cash was used for village bank expenses for the meeting (if any)?	
4	How much cash was disbursed by the village bank as dividends (if the meeting is at the end of cycle)?	
5	How much cash is currently on hand?	
6	How much money was collected by the village bank during the meeting?	
The sum of the amounts on lines 1 through 5 should equal the amount on line 6.		

Preparing the Audit Procedures for Bank Members (Instructions)

Audit One: Comparison of Passbooks and Bank Records

This audit can be performed by members at any time; in fact, members should be encouraged to conduct this audit if they have questions regarding their balances. Such surprise audits—without advance warning—are particularly helpful to deter misuse of funds.

Select five bank members at random and validate their passbooks against the bank's accounting records. The members can validate all amounts in the passbook or just selected amounts: total savings, outstanding external account loan balance, external account payments and dates, internal account loans received, internal account payments and dates and internal account loan balances.

Members can be randomly selected by picking their names from a bowl, assigning members numbers 1 through 10 and throwing a die, or selecting every nth person from an alphabetical list.

Audit Two: Bank Statement Reconciliation

This reconciliation can be performed at any time after the village bank receives its first bank statement. Members should routinely ask to see these statements and other bank receipts in order to reconcile them with what they understand to be the cash in bank amount based on village bank records and the cash flow statement.

Choose a member at random to perform the reconciliation. The member should verify that deposits of village bank savings and loan payments actually appear on the commercial bank records, and that they were made on a timely basis (within 48 hours, if possible). The member should also review bank receipts against the commercial bank statement and the village bank records.

Audit Three: Cash Reconciliation

This audit should be performed any time there is a question regarding a deposit that was to have been made. Bank members have a right to demand timely deposits of their funds.

This reconciliation is based on cash collected at the current or previous meeting and can also serve as a validation of cash if the village bank does not have access to a commercial bank.

Auditing a Bank: Member Audit Guidelines (Lesson 22)

Or "How Members Can Audit Their Own Bank"

This role play can be performed by participant volunteers, training facilitators or a combination of both. If the situation is exaggerated, it will be more lively and fun for those watching.

Role Play

The volunteers should act out a meeting where a number of borrowers repay their internal account loans but do not have their passbook signed, do not get receipts and do not check the management committee's books to see if they reflected the same amounts as their passbooks. At the next meeting, the management committee claims that one of the members did not pay. The members all claim that they paid. They ask the management committee if they can see the internal account records. However, the records were prepared in pencil and there are many erasures, so it is hard to read.

Ask the participants: How can the village bank members check to see where the mistake is? How could the members have avoided this problem?

This kind of misunderstanding would not happen if members had proof of payment represented by signed passbooks and receipts, or if they had checked the management committee's books during the meeting. Members should also make sure that the committee's books are neatly kept—in ink and without the use of correction fluid.

One way to avoid these problems as well as other recordkeeping mistakes is to regularly audit the village bank books. The agency conducts audits, but members should conduct their own audits in case the agency itself makes a mistake. Member audits also tend to be more frequent than agency audits.

Bank Member Audits

There are a number of ways that members can audit their village bank's records. They include preparing a cash flow and a financial status bar chart, and using the small audit procedures from the Audits Procedures for Bank Members tool.

Appendix

Training Seminar Materials

Introduction

This appendix includes a sample agenda incorporating all “lessons” in the *Internal Account Management Toolkit*. It also includes workshop and tool evaluation forms.

In the event your agency conducts a training workshop, CRS would appreciate receiving comments on your experience with the tools in this manual. Please send completed tool evaluation forms (below) to:

Tool Development Manager
Program Quality and Support Department, Microfinance Unit
Catholic Relief Services
209 West Fayette Street
Baltimore, MD 21201
U.S.A.

The majority of the tools on which the lessons are based have been field tested in village banks, management committees, and with program management staff and field agents. While some of the tools are directed at village bank members, most of the lessons are intended for your agency’s program managers and other staff. The rationale for this approach is that to effectively train village bank members, agency staff must first have an understanding and appreciation of internal account developmental and technical objectives, and operations and management.

Adjust the curriculum, training design and even the tools to suit your agency’s requirements and lending environment.

Sample Seminar Agenda

<table>
<tr><td>Day 1</td><td colspan="2">Overview of Internal Account Management</td></tr>
<tr><td>08:30-12:00</td><td colspan="2">L 1: Managing the Internal Account, an Overview</td></tr>
<tr><td>12:00-13:30</td><td colspan="2">Lunch</td></tr>
<tr><td>13:30-15:30
15:30-17:30</td><td colspan="2">L 2: Using the Internal Account Management Toolkit
L 3: Using the Diagnostic to Analyze the Internal Account</td></tr>
<tr><td>Day 2</td><td colspan="2">Accounting and Record Keeping</td></tr>
<tr><td>08:30-12:30</td><td colspan="2">L 11: Keeping Records for the Internal Account, an Overview
L 12: Using the Loan Contract and Payment Plan Form
L 13: Using the Loan Disbursement Summary Form
L 14: Using the Loan Payment Forms</td></tr>
<tr><td>12:30-13:30</td><td colspan="2">Lunch</td></tr>
<tr><td>13:30-17:30</td><td colspan="2">L 15: Using the Dividend Forms
L 16: Using the Cash Flow Form</td></tr>
<tr><td>Day 3</td><td>Lending and Savings Policies</td><td>Auditing</td></tr>
<tr><td>08:30-12:30</td><td>Group I
L 9: Establishing a Cash Reserve
L 10: Savings Practices</td><td>Group II
L 18: Internal Controls
L 19: Auditing a Bank, an Agency Overview
L 20: Using the Operations Audit for Agencies Form</td></tr>
<tr><td>12:30-13:30</td><td>Lunch</td><td>Lunch</td></tr>
<tr><td>13:30-17:30</td><td>L 4: Bylaws Discussion Guide
L 5: Analyzing Loan Feasibility
L 6: Tough Love
L 7: Collecting Delinquent Loans
L 8: Reporting on Troubled Loans</td><td>L 21: Using the Financial Status Audit for Agencies Form
L 22: Auditing a Bank: Member Audit Guidelines
L 17: Financial Status Bar Chart</td></tr>
<tr><td>Day 4</td><td colspan="2">Hands-on Training</td></tr>
<tr><td>08:30-12:00</td><td colspan="2">Lesson 23: Planning for Experiential Training</td></tr>
<tr><td>12:00-13:00</td><td colspan="2">Lunch</td></tr>
<tr><td>13:00-18:00</td><td colspan="2">Lesson 24: Experiential Training at Village Banks</td></tr>
<tr><td>Day 5</td><td colspan="2">Feedback and Evaluation</td></tr>
<tr><td>08:30-12:30</td><td colspan="2">Feedback from Experiential Training</td></tr>
<tr><td>12:30-13:30</td><td colspan="2">Lunch</td></tr>
<tr><td>13:30-17:30</td><td colspan="2">Review of Diagnostic, and Evaluation of Seminar</td></tr>
</table>

Planning for Experiential Training (Lesson 23)

Selection of Village Banks

You should select a sufficient number of village banks so that each team of participants has the opportunity to practice at least one, and preferably two or three, tools. Choose banks at various levels of development. Some tools, such as the savings lessons, are best suited for new banks. On the other hand, some of the audit tools are best suited for more mature banks. The location of the village banks is also important. In your training plan and schedule, consider the logistics and the time required to reach and return from the village banks.

Preparation for Village Bank Visits

Depending on the number of participants, divide the group in teams of two or three. Teams may be divided according to the tool set laid out in the manual—Bylaws, Accounting and Recordkeeping, Audit, Reserves, and Savings, for example. Alternatively, teams may self-select based on interest and expertise. Team members should spend at least two to three hours preparing the materials and their presentations for the village bank members. They can then proceed to the village banks.

It is suggested that team members take turns acting as recorder during the presentations at the village banks. In this way, the team can observe the reactions and learning levels of village bank members during the practice sessions. Notes taken during the presentations can then be used in preparing for the feedback sessions on the last day of the training seminar.

List of Tools Appropriate for Village Bank Practice Sessions

- Bylaws Discussion Guide
- Analyzing Loan Feasibility
- Tough Love Lesson
- Troubled Loan Report
- The Penny Jar
- Four Lessons in Savings
- Recordkeeping Forms and Lessons
- Financial Status Bar Chart
- Internal Controls
- Bank Member Audits

Experiential Training at Village Banks (Lesson 24)

Feedback from Experiential Training Sessions

Each team should be allowed approximately two hours to prepare a summary of their experience with the tools at the village bank. They should address the questions listed below, and prepare a presentation for the entire group of participants.

- What worked about the tool and the training at the village bank?
- What did not work about the tool and the training at the village bank?
- What recommendations do you have for the tool and the training at the village bank?
- In what other ways could you have taught the same lesson?
- How did village bank members react to the practice session?
- Would you use this tool with village banks in your program?

Each team, in turn, presents their experiences and recommendations to the group.

Seminar Evaluation Forms

Evaluation Form

Internal Account Management Toolkit Seminar

Seminar Evaluation

(Please respond to the following questions)

What did you like the most?

What would you like to change?

Which materials were most helpful?

Tool Evaluation

(Please answer for each tool that you worked on during the seminar. Use additional sheets, as necessary.)

Tool Name: ____

Usefulness of tool to your own program.

Limitations of the tool and/or recommendations you have to make it better.

Quality of the presentation of the training design and facilitation surrounding the tool presentation time, materials, preparation of training session.

Glossary

Portions adapted from the Glossary developed by The SEEP Network

Term	Definition
Audit	An examination of the accounting records (and related source documents), the purpose of which is to attest to their fairness and dependability.
Amortization	The gradual reduction of a debt by means of periodic payments sufficient to liquidate the debt at maturity. An *amortized loan* is a loan in which the principal, interest and other amounts are repaid in installments over the life of the loan. An *amortization schedule* shows how a loan will be repaid by listing specific payment dates along with a breakdown of principal, interest, and other amounts for each payment.
Arrears	Payments in arrears, also called delinquent payments, are loan payments that are past due. Loans in arrears, also called delinquent loans, are loans on which any payments are past due. Past due must be defined by the financial institution. Importantly, it should be an indication of when the RISK increases that a loan will not be repaid. Principal and interest arrears should be considered separately. Principal in arrears is assets at risk, while interest in arrears disrupts a program's cash flow.
Assets	Tangible and intangible property with commercial or exchange value. *Current assets* include cash and marketable securities, accounts receivable and inventories which in the normal course of business will be turned into cash within a year. *Fixed assets*, referred to as property, plant and equipment, represent those assets not readily redeemable to cash. They include land, buildings, machinery, equipment, furniture, automobiles and long-term (more than one year) investments or receivables. *Productive assets* are those assets that generate income, either through investments or interest charges on use of the asset.

Term	Definition
Average outstanding balance	Statistic calculated by totaling the loan fund amounts outstanding at the end of each month during a period and dividing the sum by the number of months in the period. It is used in formulas that cover activities over more than one month of time because it gives a more accurate picture of portfolio activity over the period.
Balance sheet	Financial statement that identifies company's net worth as of a specified point in time. It provides an accounting picture of assets owned by a company and of claims against those assets. One part of the balance sheet lists assets, while another part shows liabilities and equity. The two parts must be equal.
Breakeven	The point at which all revenues cover all expenses. *Breakeven analysis* involves determining the appropriate balance between interest rates (and any fees charged) and the loan volume to achieve breakeven.
Cash flow	A detailed breakdown of the net cash inflow or outflow for an entity during a specified period. For accrual accounting, there is a critical difference between cash flow and the income statement. A cash flow includes only transactions conducted in cash during the period, while the income statement also includes revenues (and expenses) that are recorded in the accounting records during the period but that have note yet been received (or paid) in cash. For example, an income statement includes accrued interest as a revenue item, while a cash flow does not include interest until the cash is actually received.
Collateral	Assets pledged to secure the repayment of a loan.
Commission (or fee)	**A** charge (usually based on a percentage) for services offered. In lending programs, commissions are fees paid to an agent/loan officer for services performed as part of the cost of credit extension. Usually stated as a flat fee or percentage of the loan amount.
Default	*A defaulted loan* is a loan that the lender is quite certain will not be paid back by the borrower. Usually, a loan is considered in default when the debtor has stopped payment on a loan for more than two or three payment periods, regardless of petitions by the lender and/or legal actions against the borrower. The *amount defaulted* depends on how much is outstanding when the borrower stops making payments. Amounts that will have to be "written off" or counted as "loan loss" may be different from the amount defaulted if the lender can collect collateral or guarantee.
Delinquency	See *arrears.*
Equity	Total assets less total liabilities. Equity is made up of paid in capital (the contributions of owners) plus retained earnings (see *retained earnings*).
External account	That portion of a village bank's funds that have been borrowed from the implementing agency and, generally, member repayments in transition back to the agency.

Term	Definition
Fee	See *commission***.**
Formal financial institution	Financial entities such as credit unions, development and rural banks, and postal systems.
Grace period	Period of time granted after loan disbursal during which no principal has to be repaid. Interest payments may or may not have to be made.
Income	The amount earned in an accounting period (also referred to as revenue). Net income is income less expenses.
Inflation	An increase in the volume of money and credit relative to the available supply of goods, resulting in a rise in the general level of prices. The *official rate* is usually determined by the government using the change in a specified basket of goods. The *real rate* is the actual increase in the price of a set combination of goods and services over time, as experienced in the marketplace.
Interest calculation method – declining balance	Interest for each payment period is calculated based on the amount of the loan outstanding during the period, not on the original loan amount. The amount of interest the borrower pays decreases as the principal amount owed is reduced by payments.
Interest calculation method – flat	The amount of interest is fixed over the life of the loan. The amount paid for each period is calculated by multiplying the nominal interest rate of the period by the original loan amount.
Interest rate – commercial	Rates published by commercial banks based on cost of capital, loan losses, and cost of administration, including a profit margin.
Interest rate – effective	Effective rates treat all of the direct financial costs of a loan (including commissions, fees, calculation method, and other loan requirements) as interest for the purpose of calculating an interest rate.
Interest rate – positive / negative	*Positive rates* are those higher than the rate of inflation. *Negative rates* are those lower than the rate of inflation.
Interest rate types – real	Rates that have been adjusted to compensate for the effects of inflation. Real interest rates are either *nominal* or *effective rates* of interest less the inflation rate. In countries experiencing hyperinflation, real rates are computed with the following formula: $R=\frac{1+N}{1+I}-1$ where R the real interest rate, N = the nominal rate, and I = the rate of inflation.
Interest rate types – stated	The quoted or nominal rate (for example, 2% per month.

Term	Definition
Internal account	That portion of a village bank's funds that are actually owned by the village bank and bank members (equity). Some village banks also include bank member repayments on external account debt until such time as these borrowed funds are repaid to the implementing agency.
Liabilities	What a business or organization owes to others. Usually divided between *current liabilities,* those due within one year, and *long-term liabilities,* those due within more than one year.
Liquidity	The ability to meet current obligations or demands for cash as they become due.
Loan fund capital	Amount of capital the entity has that is to be used to lend to borrowers. Some may be in the portfolio (that is, lent out), and some may be temporarily on deposit for future lending.
Loan loss	Amount of principal an entity loses because a borrower does not repay a loan. Should be the same as the amount "written off" for that loan, but may be different from the amount defaulted if the institution can recover some of the collateral.
Loan term	Period from the date of disbursal to the final due date of the loan
Loans outstanding	The *portfolio,* or *active portfolio.* It is the amount owed to an institution by its borrowers that the institution expects to receive. Gross portfolio is the amount outstanding, while net portfolio is the gross portfolio minus the loan-loss reserve.
Microenterprise	Generally, a sole proprietorship with fewer than five employees that has not had access to the commercial banking sector, and can initially utilize a loan of under $15,000. Most microenterprises have fewer than three employees, and the majority are operated by the owner alone.
Net worth	See *equity*.
Operational costs	Those costs incurred by an entity to maintain operations during a specified period. They do not include investments, but do include recurring costs such as salaries, rent, transportation, etc. Depending on use, they may or may not include financial costs of borrowed money.
Past due	Term that must be defined by the microenterprise institution. It determines when a loan becomes delinquent or in arrears. It should indicate when the risk of nonpayment increases. See *arrears.*
Portfolio	See *loans outstanding***.**
Portfolio income	Includes all interest income, commissions and fees collected from borrowers to secure and pay back a loan. This, along with interest-generated income on investments, is referred to as *internally generated income* or *funds* as opposed to grants or donations given to an institution, which are externally, *generated funds.*
Principal	The face or stated amount of the loan upon which interest is calculated. *Outstanding principal* is the amount owed by the borrower at any time, excluding interest.

Term	Definition
Profit / loss (income statement)	The *financial statement* that shows how much an enterprise earns (or loses) during a specified period of time. It is different from cash flow because it may include income not yet received and expenses not yet paid.
Refinancing	The process of developing a new loan agreement before a previous one is completed. It can include increases in principal amount, extension of term, etc.
Repayment	Payment of principal in the process of amortizing a loan; may include payment of interest, but payment of interest alone does not constitute a repayment. See the Table of Formulas for a method to calculate *Repayment Rates.*
Repayment schedule	See *amortization schedule.*
Rescheduling	Process of changing the payment period and/or the size of payments, on an outstanding loan. It is usually done to prevent a borrower from falling in arrears, or so that a borrower is no longer in arrears and is more likely to meet payments on time.
Reserves	Preestablished amounts of money (usually a percent of a loan portfolio) that are kept aside, either physically or as a separate account on the balance sheet, in order to offset unpaid loans or bad debt. Most countries have a law requiring that financial institutions maintain loan loss reserves.
Retained earnings	Net profits kept to accumulate in an enterprise after dividends are paid; also called undistributed profits or earned surplus.
Savings deposit liabilities	The amount an institution is holding that actually belongs to others. Although it is a liability for the institution, it is different from borrowed funds because there is no due date or amortization schedule.
Self-sufficiency	Financial indicator. An organization's percent or level of self-sufficiency can be calculated for a specific period (monthly or yearly), cumulative since a certain date, or cumulative since the program's inception. *Operational self-sufficiency* occurs when internally generated income (investment and operational) is equal to or greater than expenses. *Financial self-sufficiency* occurs when internally generated income (investment and operational) covers direct operating and financial costs, and is sufficient to maintain the real value of the credit portfolio. See the Table of Formulas for methods to calculate self-sufficiency.

Term	Definition
Spread / margin	*Margin* is the difference between gross and net amounts of income. *Spread* or margin on interest rates is the percentage points between the cost of money (to a financial institution) and the interest rate charged the borrower. The spread on a loan must be sufficient to cover all operational costs, risk reserve, inflation, and some profit (to help capitalize a loan fund and/or reinvest in the institution – computers, training for staff, etc.) for that institution to obtain self-sufficiency and grow.
Sustainability	Sustainability is the ability of a microcredit program to maintain its operations and continue to provide service to its customers or clients. A program is sustainable when a combination of external grants, loans, and internally generated revenues are sufficient to cover all program expenses over the long term Full sustainability occurs when internally-generated income (investment and operational) and long-term, dependable sources of externally-generated income (such as donations) cover direct operating and financial costs, and are sufficient to maintain the real value of the credit portfolio.
Write off	That point where a financial institution removes a bad, or nonperforming loan, from the assets side of the balance sheet and shows it as a loss. This usually occurs after all attempts have been taken to activate or collect a portion of the loan. The write-off policies of financial institutions should spell out at what point loans are written off.
Village Bank	Community-based credit and savings associations of 25 to 50 self-employed poor (generally women). Participants choose members, elect officers, and establish savings requirements. The group’s loans are backed by solidarity collateral: a group promise to support each individual loan.

Index

A

B

C

D

E

F

G

H

I

L

M

N

O

P

R

S

T

U

V