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THE EFFECTS OF RESOURCE MANAGEMENT ON MICROFINANCE LOANS

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ABSTRACT

More than 2.5 billion adults worldwide do not have an account at a financial institution according to The Global Findex Database established by The World Bank (Demirguc-Kunt 2). Seventy seven percent of adults living on less than $2/day help to make up this population, and because the hurdles to maintaining a formal bank account are so high, many of the world’s poor have turned to moneylenders to provide them with the capital they seek. This form of financing can have incredibly high interest rates, forcing the borrowers to pay back all or most of the returns they received from the loan in the first place. Because of this, a new idea was born in the 1970’s to provide the rural poor with access to micro credit in an effort to eliminate moneylenders and allow these individuals to support their own businesses (Yunus 21).

Today, this idea has expanded into an entire network of microfinance institutions reaching over 130 million clients (Financial Institutions). Not only do these banks provide loans, but they also offer savings, insurance, and financial literacy programs. It is these institutions I will explore in my research, more specifically looking at the internal controls within microfinance organizations and how these programs instill confidence in both their borrowers and lenders. Finally, I will discuss what sort of controls and documents need to be in place in order for someone to establish a new microfinance branch in the future. Many of these documents gain their value in their clarity for potential borrowers to understand, and therefore should not be analyzed based on their complexity.
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Chapter 1

Introduction

Microfinance is a growing field for borrowers worldwide who want to kick start their small businesses without the minimum balances or geographic hurdles that more formal banking institutions require. While there are many similarities between the two, microfinance institutions (MFI’s) do not require cash nor collateral to secure a loan, and this small difference opens up banking to an entirely different world of creditors in developing economies (Microcredit). However, in order to instill trust in these loans without collateral, MFI’s need to establish procedures and controls to secure repayment and build faith with lenders.

Throughout this research, much discussion will revolve around resource management strategies MFI’s need in order to maintain control over their resources. Many of these strategies seek to replicate the internal controls within publicly traded businesses that allow shareholders to invest in these corporations. While microfinance institutions do not have shareholders, they do have stakeholders such as lenders, borrowers, governments, and non-government organizations that need to believe in the organization in order for it to succeed in its goal. Organizations such as Grameen and Kiva have mastered this borrowing and lending program on a large scale, however, this research seeks to apply control structures to one branch of a microfinance institution. With this goal in mind, the Appendixes were created to support a new microfinance branch in a developing area.
Chapter 2

Background on Microfinance

Originating in 1974 in Bangladesh, the concept of microfinance was born when Economics Professor Mohammad Yunus witnessed the struggle of poor entrepreneurs firsthand during the famine of 1974 and wanted to figure out a way to help. With just $27 he began experimenting with making small loans to the rural poor in Jobra and found that they were very likely to pay back the principle with interest on time (Yunus, 1999). From this initial step spurred an entire movement and in 1983 Yunus created the Grameen Bank, one of the first major microcredit institutions (Yunus, 1999). The goal of the bank was to help low-income entrepreneurs obtain loans and learn financial planning strategies in order to make sound business decisions. The business model was simple. Loan to the exact people commercial banks avoided, low income women in rural areas without collateral (TedxVienna, 2012). By taking a very different approach, Yunus opened up credit to a whole new world of borrowers.

In the 1990’s, the Grameen bank continued to experience success, and other microfinance branches began to appear in Brazil, Venezuela, and Indonesia (Krieger, 2006). World-wide interest was growing and on February 2nd to 4th, 1997, the first Microcredit Summit took place in Washington, D.C. Its goal was to bring together microcredit practitioners, advocates, educational institutions, donor agencies, international financial institutions, and non-governmental organizations in order to see where microfinance could be improved and expanded going into the future. In 2006, the Summit’s goals were refined to include reaching the poorest of
the poor, empowering women, creating financial self-sustainability, and generating a positive, measurable impact (About the Campaign).

More recently, from 2004 to 2011, global microfinance grew by 30% annually and now includes over 1,700 microfinance institutions (MFIs) worldwide according to MIX Market ("Poor Service"). According to Kiva, one of the leading western MFI’s, the success rate for microcredit loans is an astonishing 98.93% (About Us). This makes it look like a very safe investment since less than 2% of borrowers do not meet their debt obligation. However, despite the success of these loans, the average interest rate charged is 33% (Haase, 2013). This implies investors are hesitant to loan out money to these organizations unless they are offered incredibly high returns.

Recently, microfinance has come under attack after a number of institutions began entering the market for the wrong reasons. The height of criticism occurred in 2010 in Andhra Pradesh, India after loan collection officers harassed defaulting microfinance borrowers to the point that 200 individuals committed suicide. As Hugh Whalan writes in his article, The Danger of Demonizing Profit Making Companies That Serve the Poor, ”the exploitation of the poor has been led by profit-making companies which have quickly grown to dominate an industry that was once populated by non-profits,” (Whalan 2010). Therefore, many lenders with excess capital who were once attracted to the industry now proceed with caution because of the fear that someone other than the poor may be the real beneficiary of their money.

Another factor that makes investors nervous regarding microfinance loans is that they offer a very unique type of inherent risk. While borrowers will do everything in their power to pay back the funds, should political unrest break out in their country or a natural disaster occur (things completely out of the borrower’s control), the success of the entire business could be
wiped out. Therefore, lenders charge a premium to compensate for this risk. Another reason rates are so high is because MFIs have an operating cost of about 19% of the credit amount to cover the lawyers, accountants, etc. required to make the loans (Haase, 2013). Lastly, the lack of information and transparency regarding internal controls within a microfinance organization leads to uncertainty, and therefore higher rates. Should institutions find a way to limit these risks, the interest rates needed to satisfy lenders could go down and more people could be positively impacted by the effects of microfinance. This is the goal of creating strong internal controls and resource management strategies.
Chapter 3

Resource Management Strategies

Effective resource management strategies are needed to minimize the risks associated with microfinance. While ideally every individual globally should have access to financial services, controls are needed to make this possible. The goal is to make sure funds are getting to the right people and repayment rates are being secured. According to Jerold Zimmerman in his textbook, *Accounting for Decision Making and Control*, “all successful firms must devise mechanisms that help align employee interests with maximizing an organization’s value,” (Zimmerman 3). Key aspects of an effective resource management strategy include: (1) selecting the right people to manage the organization, (2) separating duties to maintain controls, (3) monitoring and evaluating the processes in place, and (4) providing incentives for individuals to make good decisions.

Selecting the Right People

Money in the hands of different people is not the same. While some people can multiply a fortune when given the opportunity to invest other people’s money, others will slowly deplete their resources. In his book, “Banker to the Poor,” Muhammad Yunus makes a compelling argument why governments fail to effectively manage other people’s money and why some services are best left to businesses. Extending credit to the poor, as microfinance institutions do, is one such service he argues that should be left to the private sector. While some countries enlist
the work of government departments or charities to create soup kitchens and homeless shelters, Yunus makes the point that these institutions have neither the incentives nor control structure in place to effectively manage their goals. Instead, social businesses should be put in place where the founders truly have a passion for the problems they’re combatting (Yunus, 1999). According to his framework, a social business is one that is driven by a social goal and seeks only to make enough profit to cover its cost. This is the first and most important quality to look for when selecting individuals to lead an organization. Without the self-motivation to tackle the issues, finding creative solutions to the problem becomes very difficult.

Next, individuals must also have the training and technical expertise to handle the problems they are addressing. While organizations such as Village HopeCore International and Kiva require a college degree, firsthand training by the organization and multiple years of field work experience for management positions are also required (Village HopeCore International). This ensures people with decision making powers have the knowledge base to make informed decisions, and that they are connected to the problems they are trying to solve.

Lastly, individuals must be honest and dedicated in order for management to trust them with oversight responsibilities. One way organizations test this is through preliminary background checks on new employees. However, agency costs can still occur. Arising when the goals of employees and management do not perfectly align, organizations attempt to minimize this effect by offering incentives and establishing controls so that both parties are prioritize the same interests (Zimmerman 684).
Establishing Controls

While managers would love to trust their employees to do the right thing, it is important for organizations to put controls in place to encourage this behavior. According to the Center for Financial Inclusion, “internal controls improve decision making by ensuring that information is timely, accurate, and complete,” (Campion 3). The most important guideline to follow within a business or new microfinance branch is separation of duties. The three key elements of control in an organization are: (1) custody, (2) authorization, and (3) record-keeping. Custody involves physical control of the assets in question. This could either be cash or inventory, though within a microfinance organization it would primarily be cash. Authorization is the ability to sign off on transactions involving this asset. This role is typically given to a higher ranking official who understands who should and should not be receiving funds. Lastly, record keeping maintains the accounting and journal entries for these transactions. This should be done by someone trustworthy and without motivation to unfairly alter or restate the numbers. These elements must be controlled by different individuals within the organization in order for checks and balances to be effective.

Next, decision rights must be divided among individuals within the organization to establish accountability and increase efficiency. Typically, one person will be in charge of making a given decision, but a team of people will provide input and make sure future performance corresponds with the decision made (Bain, 2013). With a new branch of a microfinance organization, separating decision rights can be difficult as there may not be many employees to separate duties between. However, review procedures should still be established in order to set a precedent for the future. Also, with separating decision rights comes the risk of expending influence costs. These include time and money wasted by employees in an effort to
influence those with decision rights (Zimmerman 145). In order to mitigate these risk, certain decisions should not be assigned, and instead be determined based on policies set by the branch. For example, the interest rate on loans or the system for receiving incentives should be set by policies, rather than decision rights.

Lastly, documentation is incredibly important to ensure all procedures are followed adequately and to establish credibility with the loans being issued. More advanced microfinance institutions perform internal audits and issue annual reports or financial statements, however, for a newer branch just beginning, having a general ledger, loan tracking system, and utilization reports is a good basis for keeping up to date books. Examples of these are included in the Appendixes.

**Monitoring and Evaluation**

Along with qualified employees and internal controls, a micro enterprise unit must have monitoring and evaluation systems in place in order to track the progress of the organization in reaching its goals and provide feedback to employees regarding their personal contributions. In order to do this, clear performance indicators need to be established for each stakeholder. According to the International Fund for Agricultural Development, “indicators should be results-based, emphasizing project and institutional performance and development impacts, rather than simply the achievement of a certain number of activities or inputs,” (IFAD 62). For example, a microfinance institution should track loan repayment rates, rather than the number of loans its field workers have distributed. This provides a better indicator of the success of the branch, rather than just the size.
When establishing monitoring and evaluation tools for a microfinance branch, focus on the big picture. Yale School of Management Professor Tony Sheldon in the video, “What are the Realities of Microfinance?” warns that it is important for microfinance branches to not focus on the number of individuals brought out of poverty, but rather to look at how sustainable that jump is and how many people are no longer vulnerable to falling back below the $2/day threshold. This becomes more difficult to quantify, and therefore many organizations are turning to randomized controlled trials (RCTs) in order to extract information from this data. To follow this methodology, research institutions compare the welfare of individuals who have accepted a microfinance loan, to similar individuals in the area who have not. They then see who has a higher household income, who has higher levels of voluntary savings, who can make better financial decisions, and a few other socio-economic factors such as child labor rates and education. This is meant to provide a more accurate analysis of the success of microfinance rather than looking at an individual before and after receiving a loan as their success or failure could be influenced more on macroeconomic factors. By using RCT’s, researchers are hoping to eliminate the effects of natural disasters, economic cycles, and government policymaking, and instead extract information regarding the actual success of the loan.

Incentives

The last resource management strategy to implement for a new micro enterprise branch is to establish incentives which will encourage compliance. According to the State of the Microcredit Summit Campaign Report 2009, the number of clients reached by microfinance institutions increased from 7 million to over 106 million borrowers from 1997-2007. Just three
years later, in 2010, the number increased to 205 million. However, though this is a great indication of the field's growth, it does not provide any information on the success of these loans relative to the borrower. Making sure that incentives put in place encourage choosing the right borrowers and helping them succeed, rather than just distributing as many loans as possible, should be the priority.

When looking for incentives for clients to pay back their loans, MFI's determined that clients were primarily focused on the Big Three: (1) food, (2) shelter, and (3) providing an education for their children (Wolfensohn). Therefore, offering packages and incentives to borrowers that focus on these areas should be a priority as these three also serve as primary indicators of escape from poverty. Many MFI’s allow borrowers with good repayment rates to take out loans to fund their children’s schooling. This provides an incentive for borrowers to repay on time, while also working to solve other problems associated with global poverty.

When it comes to employees, incentives should be offered that acknowledge good work, however, in an article by Forbes magazine the author discourages creating incentive plans that focus on quotas as these have the potential of creating negligent employees once they have hit the goals established by management (Quast). Therefore, rather than encouraging loan officers to distribute xx number of loans per month, instead offer incentives based on employee scorecard results that take into account an employee’s performance for the entire review period.
Chapter 4

Controls within Microfinance Institutions

Ideally, all microfinance branches would have strong internal controls that allow borrowers and lenders to have confidence in participating. However, in practice these can vary widely from organization to organization. Therefore, an analysis of three microcredit organizations was conducted in order to determine what controls are already utilized by organizations, along with what controls are lacking which could be applied to a new microfinance institution.

Grameen Bank

Grameen Bank was chosen for analysis because it was the first microfinance bank established, and therefore had to create its own system of policies and controls for its borrowers to follow. That bank focuses on the "double bottom line" in an effort to make both social and financial progress (Alam 87). However, in order to do this, it first needed to create an environment that supported innovation while respecting internal controls.

First, with regard to choosing the right people, Grameen has an extensive set of rules for both hiring new employees and taking on new borrowers. For borrowers, every individual who wants to take out a loan must undergo a one or two week training on the rules of Grameen and pass an oral exam before being accepted into the banking system (Alam 6). This guarantees that
new borrowers understands basic financial principles and the policies of the loan agreement. Appendix I: Training Manual provides information regarding these principles covered.

In order to provide control over employee hiring, Grameen tests the written and mathematical skills of new applicants. The organization also provides on-site training for new employees at field staff training, as well as the opportunity to get hands on practice in the field (Alam 95). This technical training ensures all employees follow consistent borrowing and lending procedures, while on-site learning teaches new employees the soft skills needed to succeed on the job.

With regard to internal controls, the bank has stricter loan-loss provisions and write off polices than even the central bank of Bangladesh (Alam 8). Also, Grameen keeps loan sizes small and makes repayments either weekly or bi-weekly to maintain strong oversight over receivables (Alam 62). Next, center meetings are required to be in the morning so that the money collected from all borrowers can be deposited in a commercial bank that same day (Alam 27). This minimizes the time the cash is vulnerable to theft. Grameen follows a policy of transparency in all transactions (Alam 39). This means that Grameen does not hide behind the small print when making loans, but rather, is upfront and honest with all borrowers about what is expected and required of them. Typically, this is in the form of policies and agreements signed at the beginning of a loan dispersal process. Look to Appendix B: Micro Enterprise Policies for an example agreement which provides control over policies and makes sure all loans are dispersed consistently.

Grameen also conducts internal audits of its operational and financial programs in order to make sure all employees and borrowers are following the rules of the bank. This constitutes unannounced trips by the center staff to field sites in order to evaluation performance.
Afterwards, recommendations for corrective action are provided (Alam 126). Internal audits are especially important when there are a high number of transactions at a given branch, when transactions are processed outside of the branch, or when borrowers are illiterate and require the guidance of loan officers for support.

In terms of monitoring, Grameen has field officers which report to branch officers which report to area officers which report to zonal officers (Alam 92). Also, strict credit discipline and close supervision are essential factors in Grameen-style programs. The strength of the credit function is evaluated by looking at repayment rates (the amount paid divided by the amount due) and growth (the increase in the amount of loans outstanding). Next, work progress reports are completed for each branch bi-weekly or once a month by branch managers, including recommendations and steps for improvement (Alam 40). This provides monitoring over branch employees and encourages constant reevaluations. Similar standards are maintained over loans, with loan utilization reports filled for every borrower. These reports serve four purposes, (1) income generation, (2) loan repayment, (3) capital accumulation, and (4) demonstration effect (Alam 44). In essence, loan officers make sure that the capital they provide is being used for an income-generating activity and that loans can be repaid with interest, following the rules of the bank. Lastly, supervision of field operations is key to comforting investors and making sure capital is being utilized honestly. Refer to Appendix H: Loan Utilization Review to see the criteria loan officers use to evaluate performance.

In terms of evaluation, Grameen has developed the Progress out of Poverty Index to determine if branches are achieving their objectives. This system incorporates a three step approach in which they (1) measure poverty outreach, (2) assess social performance, and (3) track poverty over time. Branches are moving away from poverty if they progress past country-
specific statistics connected to housing materials, children’s education, and health-related standards (About the PPI).

Lastly, Grameen developed its own star system as an incentive for employees and branches to do good work. There are five stars for which employees or branches can earn recognition. A green star indicates freedom from overdue loans and interest, a blue star means freedom from loss, a violet star is for freedom from the Grameen head office fund (deposits at the branch cover outstanding loans), a brown star indicates freedom from illiteracy, and the most prized red star means free from poverty (Alam 107). This system motivates employees to strive for excellence, without using monetary compensation which risks taking away from the capital that can be used for operations. In regard to borrowers, a member of the bank can achieve "Gold membership" by being a member for 5 years and maintaining a 100% repayment rate (Alam 9). This not only serves as a source of pride but also allows for higher increases in his or her loan ceiling.

**Kiva**

Kiva is a huge network of microfinance organizations, connecting 1.2 million lenders with 1.5 million borrowers. Originating in 2005, the program has grown to loan out over $690,000,000 (About Us). Therefore, their model was chosen for analysis because the enterprise has already made it past their initial creation phase and exhibited incredible success during their first decade of operation.

Kiva follows a substantially different model when it comes to managing risk. For the organization, all loans pass through field partners, which are organizations in a borrowing
country with a strong reputation of administering aid to the poor. Therefore, much of the risk Kiva incurs depends on field partners. To mitigate this risk and ensure partners establish adequate resource management strategies, Kiva has a rigorous application process potential partners must pass before joining the network. There are three processes potential applicants could go through, (1) full due diligence, (2) basic due diligence, and (3) experimental partnership (Kiva’s Role).

In full due diligence situations, the organization must be registered as a legal entity in its country of operations, have at least one year of audited financial statements, express a strong social mission, and have at least 2-3 years lending to the poor. The last requirement may be waived if it is not originally a microfinance institution, however, it still needs to have at least a 2-3 year history of providing socially valuable goals. Step 2 encompasses the application review, in which all financial statements, project reports, credit ratings, and management resumes are reviewed. This is done by Kiva investment analysts to determine if the partner will be able to successful manage its funds, similar to the equity research investment analyst would conduct before buying stock. Step 2 is primarily focused on preemptive monitoring and evaluation. Step 3 of the due diligence process is to verify the credibility of the company through an on-site visit. However, Kiva states that, “if the risk of traveling to the country where the organization is located is too great…. Kiva will leverage external sources,” (Kiva’s Role). However, this appears to be a huge internal control deficiency because the organizations who have the highest risk and need to be verified the most are the ones being skipped over. Step 4 involves preparing a report of the findings from step 3 and proposing a risk rating. This is based on a five star system where 5 star organizations have very few indicators to suggest a risk a default while 1 star organizations means institutional default is much more likely. Lastly, step 5
is the approval step by the Kiva investment team, and this is when a new organization officially becomes a field partner (Kiva’s Role). This process is by far the most strenuous for a new field partner, but it also involves the most internal control procedures and lends the most credibility to Kiva. It also provides the most comfort to investors who want to see procedures and evaluations being followed, before their money is distributed.

The second option Kiva allows for new borrowers is a basic due diligence review. This process is meant to be used for mid-sized partners to allow Kiva to expand to more locations that have less sophisticated banking options. Though a less intensive review of the organization is required, Kiva maintains control over these partnerships by maximizing the amount of money these organizations can borrow at $400,000. The three steps to this process are, (1) initial screening, (2) review application, and (3) prepare a report to submit for approval. Unlike the full due diligence process, this option does not require organizations to be issued a credit rating. Instead, Kiva analysts will manually issue a credit limit depending on the level of default risk calculated (Kiva’s Role). While flexibility is needed when working with smaller and more diverse organizations, criteria for credit limits should be established in order to calculate this number with less variability. Also, as with the full due diligence review, on site visits are needed to make sure money is being put into the right hands.

Lastly, Kiva also allows for experimental partnerships if an organization is interested in making small loans but doesn’t want to commit the time or resources for a full partnership. In these situations, organizations speak with members of Kiva’s investment team and are permitted to borrow up to $50,000. This allows for a trial run in order for organizations to see if Kiva is right for them. This process doesn’t have specific steps to complete, and the risk potential of these borrowers is not clearly known. Therefore, Kiva limits its exposure to these companies at
no higher than 2% of operations. This control feature helps to protect the company from taking on riskier businesses.

   Overall, Kiva does a good job establishing controls over due diligence partnerships. However, the smaller organizations it partners with could be more thoroughly analyzed. Also, relative to Grameen, more transparency in disclosure would have been helpful when evaluating Kiva’s controls. The lack of information Kiva provided could make it difficult as an investor, auditor, or third party to determine exactly who is granted partnership privileges and who is not.

   **Opportunity Fund**

   The last organization chosen for analysis is Opportunity Fund based out of San Jose, California. The organization was founded in 1994, and is actually twice as old as Kiva, however, it has remained local, expanding to San Francisco and Los Angeles, but not beyond California’s borders (Opportunity Fund History). It was chosen because of its size. Unlike Grameen and Kiva which are massive international organization, Opportunity Fund is relatively local, supporting the communities in which it operates, and therefore more comparable to an individual branch this analysis is meant to support.

   Opportunity Fund does not have a specific webpage that lists its risks or control features, however, analyzing the information it does provide explains how the organization operates and why investors trust them with their money. With a four star rating on Charity Navigator, Opportunity Fund holds itself to the highest level of accountability and transparency (2014 Annual Report, 3). This rating is based on results from the organization’s Form 990 Tax Return and information it makes readily available to shareholders on its website. Aspects the rating
takes into consideration include, having at least five independent voting members on the board, having audited financial statements, and having a conflict of interest and whistleblower policy (How Do We Rate Charities’). Independent voting members help provide control over the decisions of management. Audited financial statements provide reassurance that financial statements are reflective of the operations of the firm. Lastly, policies regarding conflicts of interest and whistleblowers encourage employees to speak out should they see something occurring against company standards. Therefore, while Opportunity Fund does not specifically state what controls it has in place, by including over 90% of the accountability and transparency categories Charity Navigator requires, the organization is holding itself accountable to transparency standards.

Also, according to Opportunity Fund’s financial statements, the organization has over $9,000,000 in restricted cash out of its $24,000,000 total assets, implying that investors or donors are placing qualifications on where their money can be used, providing yet another control over capital (2014 Annual Report 9). These extra steps should provide comfort for investors seeking to providing money to the organization.

Summary

From these organizations, clear standards for controls can be seen within each MFI. Though not all institutions follow the same resource management strategies, most have some form of control over cash and have checks and balances in place to monitor management. Also, policies are fairly consistent among organizations with regards to how they distribute loans to
individuals. All of these processes should be incorporated when establishing a new microfinance branch as well.
Chapter 5

Applying Controls to a Microfinance Branch

These internal control and resource management strategies are incredibly important in order to establish credibility within the microfinance community, so much so that they should be implement before a new branch is established. For individuals interested in starting up their own microfinance lending institutions, the most important documents to create before beginning include (as lettered by their Appendix reference):

A. Job descriptions of microfinance staff

B. Micro enterprise policies

C. Budget for the branch

D. Employee review scorecard

E. Loan tracking system

F. Loan proposal form

G. Evaluation of loan repayment ability

H. Loan utilization reviews

I. Business manual to assist new borrowers

Each of these forms will be discussed further in the following paragraphs.
Job descriptions are needed to establish accountability within an organization. Though most microfinance institutes function as a unit, developing decision rights and delegating responsibilities ensures all tasks are completed. Also, by assigning roles, internal controls can be put in place to segregate custody, authorization, and record keeping within the organization. A diagram of positions clarifies who reports to whom after the branch or regional loan office has grown. Lastly, this document also provides contact information should co-workers, or borrowers need to get in contact with a particular employee.

Second, writing out the microfinance policies that all borrowers and employees are expected to adhere to creates a document to reference, should discrepancies occur. Borrower and lender expectations will be specifically stated, and by clarifying the institution’s policies prior to issuing a loan, stakeholders should have more faith that you are being honest and treating all transactions fairly. A list of policies adds transparency to the organization and bolsters credibility.

Third, creating a budget for the branch works to help the unit manage limited resources. Though oftentimes budgets are not followed precisely by an organization, the value of budgeting comes from the process of planning for the annual expenditures, rather than the actual budget produced (Zimmerman, 230). By working in a financial services industry that serves the poor, it is expected that employees know how to manage capital. Also, a budget works to provide a control over cash. Should an individual or segment of the branch need more money, it must submit a request and the proposal must be reviewed and authorized. This simple set of checks and balances can help prevent unnecessary spending.
Fourth, employee review scorecards should be used as a way to provide encouragement and constructive feedback to employees at the branch. By implementing a feedback system every one to six months, depending on the experience level of the employee, the branch can more adequately establish a system of monitoring and evaluation. These scorecards could also work as an incentive program. Should employees get good scores, they may earn accolades such as the star system at Grameen or may be entrusted with more responsibilities. The purpose of the incentives is to allow every employee to know they are appreciated and reward positive efforts.

Fifth, a loan tracking system is necessary to maintain good record keeping and accounting practices within the organization. By tracking loans the branch can determine if any amount is unaccounted for, and can reconcile the amount of money issued and received with the amount of money in the branch’s bank account. Also, by keeping track of the dates they were issued, the branch can determine when a loan becomes overdue and follow up with late or defaulting borrowers. Finally, strong accounting practices also maintains trust with borrowers and investors, you want to make sure the organization is adequately monitoring its cash.

Sixth, a loan proposal form provides a way for new borrowers to iron out ideas regarding their business plans before receiving a loan. It also establishes controls so that individuals with legitimate income-generating activities may receive loans, while discouraging individuals simply looking to pay off an expense. The proposal form also asks for a list of the resources and assets the entrepreneur will need, thus making it easier for the program coordinator to decide on a loan amount that is right for the individual. Next, the form establishes accountability and encourages goal setting by pushing the borrowers to strive for the ideas set forth. Lastly, the proposal allows field officers to know more about the business before evaluating its success rate.
Seventh, an evaluation of loan repayment is needed in order to determine the ability of borrowers to repay their debts. Though microfinance is meant to reach the poorest of the poor, distributing loans to individuals without a clear business plan or method to pay the funds back becomes dangerous for both the organization and the borrowers. By evaluating an individual’s repayment abilities, the organization provides control over cash and protects borrowers from debts they may not be able to repay. Factors to be considered include the credibility and trustworthiness of the borrower, previous business experience, and previous loan repayment abilities.

Eighth, a loan utilization form is needed to monitor loans the branch distributes and evaluate the success of each entrepreneur’s business. On this form, loan officers will also report back with any business related questions the borrower may have, along with strategies that have worked well to support the entrepreneurial efforts of other microfinance borrowers. This utilization form is the primary source of monitoring over loans, and should be completed by officers who physically go out into the field in order to provide better control and oversight over the distribution of funds.

Ninth, and lastly, a business manual is needed to assist new borrowers and provide a framework for which to base the pre-loan training program. This manual should include concepts such as revenues and expenses, double entry accounting, basis cash flow tracking, and business planning strategies. This serves as a preventative control, making sure borrowers understand the basic principles of business and accounting before taking on a larger project. By incorporating education, the goal is to also help borrowers sustain their business in the loan term.
Chapter 6

Conclusion

Over the past 50 years microfinance has grown from an economics experiment in Bangladesh into a worldwide banking system for the poor. While this expansion can have many challenges, as especially evident in recent years, it also offers an incredible opportunity for individuals interested in putting their excess capital towards a social and sustainable mission. In an effort to keep a fair playing field for all stakeholders, new controls and resource management strategies have been applied. The four key strategies used by organizations include: (1) selecting the right people, (2) applying internal controls, (3) establishing monitoring and evaluation systems, and (4) offering incentives to do good work. These control features were further analyzed in well-known microfinance organizations such as Kiva and Grameen, and in smaller organizations such as Opportunity Fund. Finally, policies and documentation needed to practically apply these control features were created for use by a new microfinance branch. All documents discussed are included in the Appendixes.
Appendix A

Job Descriptions

Organizational Structure:

![Organizational Structure Diagram]

<table>
<thead>
<tr>
<th>Chart of Responsibilities:</th>
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<tbody>
<tr>
<td></td>
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<tr>
<td>Responsibilities</td>
</tr>
<tr>
<td>Program Coordinator</td>
</tr>
<tr>
<td>Administrative Assistant</td>
</tr>
<tr>
<td>Field Officer(s)</td>
</tr>
<tr>
<td>Accountant</td>
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<tr>
<td></td>
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<tr>
<td>Qualifications</td>
</tr>
<tr>
<td>management and communication skills</td>
</tr>
<tr>
<td>Lenders</td>
</tr>
<tr>
<td>Program Coordinator</td>
</tr>
<tr>
<td>Program Coordinator</td>
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<tr>
<td>Program Coordinator</td>
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<td></td>
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<tr>
<td>Contact Info.</td>
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<tr>
<td>Phone #; email</td>
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<td>Phone #; email</td>
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<td>Phone #; email</td>
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<tr>
<td>Phone #; email</td>
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</table>
Appendix B

Micro Enterprise Policies

Policies for Borrowers

1. Individuals who qualify for a loan will get $xx, to be distributed within 1 month, at an annual interest rate of 6%.
2. Individuals may qualify for a loan above the $xx amount only with approval from the Program Director and only after 6 months.
3. Individuals who receive a loan must complete a 4 hour training course on financial management and loan repayment administered by the Micro Enterprise Field Partner(s).
4. Loans must be used for business activities, not for school fees, emergencies, etc. Other policies are followed for these expenses.
5. Borrowers must meet with their loan officers at least once per month to discuss business management strategies and repay loans.
6. All borrowers must submit a completed loan application form (Appendix F) before being considered.
7. Borrowers cannot be the guarantor to another borrower.
8. Every borrower must submit a business plan, reviewed and approved by a field officer.
9. Late payments can disqualify loan clients from receiving future loans.
10. Two weeks after a loan distribution, field officers will visit borrowers at their households to assess if funds were used according to business plans. Any member who has not properly invested at least 2/3 of the loan can have their entire loan recalled with an additional charge of 50% of the loan.
11. Individuals who have been found to be uncooperative or non-communicative will most likely not be considered for the second funding.
12. Individuals can receive one additional loan within their loan cycle only if the first loan and all fines or charges are completely paid.
13. Before receiving additional loans, field officers must confirm the first loan was invested properly. Any evidence of poor investment might disqualify the member from receiving the additional loan.
14. If an individual’s business failed, it must be through circumstances beyond their control such as death of the animal due to sickness in order to still be considered for a second loan.
15. Discontinuing borrowers will not be reimbursed savings until all default balances and fines have been paid.
16. Cash payment should never be made to any microfinance employee; payment should only be made by deposit at the bank.
17. For first loan recipients, payments will start after a two-month grace period. The first payment will be made during the loan meeting with a field officer and will be considered late 24 hours after the loan meeting.
18. If clients do not repay after 7 days from the meeting, field officers will follow up.
19. Field officers will contact program coordinators concerning defaulting members after 1 month of nonpayment.
20. If clients do not pay for two months, they go into default and staff will devise a strategy with leadership to ensure the compliance of the defaulter. See the Default Management Appendix.

**Policies for Branches**

1. Loan application forms will be processed by the administrative assistant but reviewed for credit by the program coordinator.
2. A new borrower’s income must be assessed by the program coordinator and be in accordance with the branch’s policies prior to receiving funding.
3. All loan applications will be dated, stamped, and require the signatures of both the administrative assistant and program coordinator.
4. Branches must have an accountant who documents repayment and default.
5. The administrative assistant will stamp loan documents submitted to the micro enterprise and initial the date of receipt.
6. Only the accountant can accept deposit slips, collection forms, and issue receipts. Copies should be kept of all forms.
7. The accountant will update the general ledger for every loan payment made by borrowers.
8. The program coordinator is required to provide balances for the previous month of loan payments if the borrower requests it.
9. For individuals in default, loan officers should contact the program coordinator.
10. The loan officer is in charge of conducting loan utilization reviews and should fill out the form entirely.
11. Loan utilization reviews are to be conducted every 2 weeks for the first six months and every four weeks after that.
12. All forms submitted to the branch must be kept and filed by the administrative assistant.
13. It is the job of the program coordinator to make sure all regional and federal laws are followed.
Appendix C

Budget for the Branch

<table>
<thead>
<tr>
<th>GENERAL LEDGER ACCT. NO.</th>
<th>ACCOUNT NAME</th>
<th>BUDGET FOR YEAR</th>
<th>ACTUAL EXPENDITURES</th>
<th>PERCENT DIFFERENCE</th>
</tr>
</thead>
<tbody>
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</tbody>
</table>

Project Coordinator Signature ___________________________ Date __________

Secondary Signature ___________________________ Date __________
Appendix D

Employee Evaluation Scorecard

Name of Employee: ________________________________ Date: ____________________

<table>
<thead>
<tr>
<th>PERFORMANCE INDICATOR:</th>
<th>1 LOW</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5 HIGH</th>
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</thead>
<tbody>
<tr>
<td>1) Communication Skills</td>
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<td>2) Devotion to Work</td>
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<td>3) Interactions with Borrowers</td>
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<td>4) Interactions with Superiors</td>
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<td>5) Problem-Solving Skills</td>
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<td>6) Positive Attitude in the Workplace</td>
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<td>7) Punctuality to Team Meetings</td>
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<td>8) Willingness to Learn</td>
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<tr>
<td>9) Accounting Skills when Monitoring Loans</td>
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<tr>
<td>10) Timely and Complete Submissions of Paperwork</td>
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</tbody>
</table>

Signature of Reviewer: ________________________________ Date: ____________________
# Appendix E

## Loan Tracking System

<table>
<thead>
<tr>
<th>Name of Borrower</th>
<th>Value of Loan</th>
<th>Date of Issuance</th>
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<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>Final Repayment Date</th>
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</tbody>
</table>
Appendix F

Loan Application Form

Name: _______________________________ Date of Birth: ______________

Village: ______________________________

Marital Status: Single  Married  Separated  Widowed  Divorced

Level of Education: ____________________  Number of Children: _________

Monthly Household Expenditures:
1) Business: __________________________
2) Education: _________________________
3) Health: ____________________________
4) Other: ______________________________
   Total: _____________________________

Your Current Businesses/Activities:
1) Activity: __________________________ Income/Month: ______________
2) Activity: __________________________ Income/Month: ______________
3) Activity: __________________________ Income/Month: ______________
   Total: _____________________________

Spouse’s Businesses/Activities:
1) Activity: __________________________ Income/Month: ______________
2) Activity: __________________________ Income/Month: ______________
3) Activity: __________________________ Income/Month: ______________
   Total: _____________________________

Loan Will be Used To: Start a New Business  or  Expand an Existing Business

Type of Business: ________________________________

<table>
<thead>
<tr>
<th>Name of Item Needed:</th>
<th>General Description:</th>
<th>Value:</th>
</tr>
</thead>
<tbody>
<tr>
<td>1)</td>
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<tr>
<td>2)</td>
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<td>3)</td>
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<tr>
<td>4)</td>
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</tr>
</tbody>
</table>

Signature: _______________________________  Date: ______________
Appendix G

Evaluation of Loan Repayment Ability

Name: ____________________________  Town: ____________________________

<table>
<thead>
<tr>
<th>INDICATORS FOR REPAYMENT</th>
<th>N/A</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Prior Business Experience</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>2) Previous Repayment of Loans (if applicable)</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>3) Community Respect</td>
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<tr>
<td>4) Prior Behavior and Conduct</td>
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<tr>
<td>5) Strength of Current Business Plan</td>
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</tr>
</tbody>
</table>

Current Household Income: _______________________________________________________

Size of Loan Requested: _______________________________________________________

Additional Comments:
__________________________________________________________________________
__________________________________________________________________________

Status: Approved  Pending  Denied

Signature 1: ____________________________  Date: ____________________________

Signature 2: ____________________________  Date: ____________________________
Appendix H

Loan Utilization Review

Name: ________________________________     Village: ________________________________

Loan Officer: __________________________     Date: ________________________________

Type of Business: ______________________________________________________________

Is the Loan Being Used for its Intended Purpose?   Yes     No

If No, Explain:

__________________________________________________________________________________

__________________________________________________________________________________

What Business Strategies Have Worked Well for the Borrower?

__________________________________________________________________________________

__________________________________________________________________________________

What Needs to be Improved?

__________________________________________________________________________________

__________________________________________________________________________________

Date of Next Loan Utilization Check: ________________________________

Final Comments?

__________________________________________________________________________________

__________________________________________________________________________________
Appendix I
Training Manual

Welcome! Congratulations on becoming a new microfinance borrower. This is an exciting moment for you and your business, however, it can also be overwhelming determining how to best use this new capital. This training manual is meant to assist you with managing your money and operating your business. Feel free to reference it at your discretion. Best of luck as you begin this journey!

Terms to Know:

**Capital:** money provided for the purpose of generating business

**Expense:** money that goes out of the business

**Fixed Cost:** costs that are constant, regardless of the level of sales (similar to start-up costs)

**Market Price:** how much are similar goods being sold in the community for

**Revenue:** money that comes in to the business

**Selling Price:** must be enough to cover expenses and allow for a profit

**Variable Cost:** costs that increase as the number of units sold increases
## Determining Operating Income

### Part 1: Calculating Revenue

1. What is your primary business?
   (ex. Selling bread)

2. What is the selling price of 1 unit of your good?
   (ex. $2/loaf of bread)

3. How many units do you expect to sell per week?
   (ex. I expect to sell 20 loaves of bread per week)

4. **Revenue per week = step 2 x step 3**
   (ex. $2/loaf x 20 loaves/week = $40/week)

### Part 2: Calculating Fixed Expenses

5. What one time costs do you expect to incur?
   (ex: buying an oven, purchasing a food cart, etc.)

6. What is the cost of these one time expenses?
   (ex: an oven is $100)

7. How many months do you have to pay this back?
   (ex: I have 24 months to pay back the cost of the oven)

8. **Cost per month = step 6 / step 7**
   (ex: $100 over 24 months = $4.17/month)

9. **Cost per week = step 8 / 4**
   (ex: $4.17/4 weeks = $1.04/week)

### Part 3: Calculating Variable Costs

<table>
<thead>
<tr>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
</tr>
</thead>
<tbody>
<tr>
<td>Items Needed: (ex: flour, yeast, salt, etc.)</td>
<td>Price per Unit</td>
<td>Units Needed/Week</td>
<td>Total Cost/Week: (Column B x Column C)</td>
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</table>

10. **Total:**

### Part 4: Calculating Operating Income

11. What is your operating income/week?

   Step 4 - Step 9 - Step 10
**Budgeting**

Given the operating income found, it is now necessary to budget the money generated by the business. Here is a sample form to use. Because operating income is found on a weekly basis, list the possible expenses to budget for as weekly outflows as well.

<table>
<thead>
<tr>
<th>Operating Income</th>
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<tbody>
<tr>
<td>(from previous section)</td>
<td></td>
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<tr>
<td>Priority 1) ______</td>
<td></td>
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<tr>
<td>(ex. Cost of food/week)</td>
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<tr>
<td>Priority 2) ______</td>
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<tr>
<td>(ex. Medical costs)</td>
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<tr>
<td>Priority 3) ______</td>
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<tr>
<td>(ex. New supplies for the business)</td>
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<tr>
<td>Priority 4) ______</td>
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<tr>
<td>(ex. Home improvement costs)</td>
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<tr>
<td>Priority 5) ______</td>
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<tr>
<td>(ex. Cost of new shoes)</td>
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<tr>
<td><strong>Total Cost of Priorities</strong></td>
<td></td>
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<tr>
<td>(Add 1-5)</td>
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<tr>
<td><strong>Money Left Over (If any)</strong></td>
<td></td>
</tr>
<tr>
<td>(Subtract total cost from operating income)</td>
<td></td>
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</tbody>
</table>
BIBLIOGRAPHY


"How Do We Rate Charities' Accountability and Transparency? : Charity Navigator." Charity Navigator. Web. 02 Apr. 2015.


ACADEMIC VITA

Kara ‘Casey’ Crouse
Kcc5135@psu.edu

EDUCATION

The Pennsylvania State University, Smeal College of Business  University Park, PA
  Master of Accounting  Class of 2015
  Bachelor of Science in Accounting & Finance  Class of 2015
  Schreyer Honors College  Class of 2015
CES, University of Maastricht  Maastricht, Netherlands  Summer 2012

LEADERSHIP

Penn State IFC/Panhellenic Dance Marathon  University Park, PA
  Finance Captain, Administrative Assistant and Alternative Fundraising  Sept. 2013 - March 2015
  Worked with a team to ensure the largest student run philanthropy in the world accredited $13,343,517.33 in monetary donations to Penn State organizations correctly
  Responsible for reconciling the expense side of THON's bank account with all invoices recorded
  Conducted office hours to batch checks, maintain financial records, and deposit cash into THON’s bank account

Pennsylvania State University Office of Orientation and Transition Programming  University Park, PA
  New Student Orientation Leader  May 2013- Aug. 2013
  Guided over 8,000 new Penn State students through the transition from high school to college
  Facilitated discussions on topics such as campus diversity, safety, and personal responsibility
  Established a friendly and welcoming environment for new students and their family members
  Answered questions regarding Penn State's academic and social structure

Gamma Sigma Sigma, National Service Sorority  University Park, PA
  Executive Board Member, Alumni Liaison  Dec. 2013- May 2014
  Corresponded with past Gamma Sigma Sigma sorority members through our newsletter and website
  Managed the social media page for our alumni chapter, providing updates on current service events
  Organized our senior recognition program, making presents for all 35 of our graduating sisters

EXPERIENCE

Ernst and Young  Washington, D.C.
  Audit Intern  May 2014- Aug. 2014
  Gained experience with confirmations, work papers, and walkthroughs for financial services clients
  Helped to grow relations with the client through daily conversations and business meetings
  Learned how to use Microsoft Excel tools and shortcuts to improve efficiency

Pennsylvania State University Department of Economics  University Park, PA
  Assess daily classroom activities, homework assignments, and exams for +300 students
  Serve as liaison for students and the professor regarding course material and classroom dynamic
  Oversaw discussions of study materials and assisted in test preparation

Pennsylvania State University Department of Supply Chain Management  University Park, PA
  Supply Chain 200 Exam Proctor  Jan. 2012 - Present
  Instruct and enforce compliance with the Smeal Honor Code for SCM 200 exams
  Monitor test rooms and maintain security of exam documents

HONORS

Schreyer Honors College Academic Excellence Scholarship
Best Buy National Scholarship, national financial aid scholarship
Simpson P. Memorial Scholarship, national financial aid scholarship

ACTIVITIES

Smeal Alumni Mentoring Program  Sept. 2012 – May 2014
MAcc Program Student Association, Mentor  March 2014-Present
Case Competition, Participant (Smeal and KPMG)  Oct. 2013 & March 2014