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Corporate Governance in Microfinance : Credit Unions

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Abstract : As part of the tremendous development experienced by microfinance over the last few years, one type of institution has not generated all the attention that it could : credit unions. This can be explained by the frequent corporate governance weaknesses of this type of institution, which have been identified as a major limit and constraint to their development. This paper tries to deal with this issue by tackling the reasons why corporate governance of credit unions is so difficult to deal with, and by presenting various mechanisms and research areas which could play a role in solving this problem.

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Introduction

Over the last few years, microfinance has experienced tremendous growth all over the world, with more and more beneficiaries/clients served and more and more players being active in the field. One category of institutions which has been part of this trend is credit unions[4]. There are now 31,725 credit unions in Africa, Asia and Latin America, says Woccu (Woccu, Statistics, 2006) and their importance is increasingly recognized by academics, as well as by the microfinance industry itself.

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[4] In the literature, some authors do refer to credit unions, others to financial cooperatives (FC) or savings and credit cooperatives (SACCOs). Eventough some distinctions can sometimes be made between those terms, in this paper, we will consider them synonymous.

But, given everything that has happened in the field of microfinance for the last twenty years or so, it could be said that credit unions are often an underestimated or forgotten player. There are a number of reasons that could be used to explain this, but certainly one of the most important ones is the frequent weakness in corporate governance, specifically when credit unions are experiencing major growth (as has sometimes been the case in microfinance). Of course, they are not the only institutions to experience weakness on the corporate governance side. But, in their case, the issue may be more fundamental and structural than for others. This is the reason why we have decided to focus this paper entirely on this issue.

To accomplish this, it will be structured around five sections.

The first section will provide background on the origins of credit unions and why they matter to the microfinance field.

The second section will briefly develop credit unions' most frequent growth path through networking, as it is a key concept in understanding their growth pattern.

Then, the third part will focus on the corporate governance issues specific to credit unions, showing how these issues become even more complex in times of growth.

The fourth section will review the various corporate governance mechanisms in order to stress how tackling this issue could be much more complex than is commonly thought.

Finally, the fifth part will suggest a research agenda on "corporate governance in credit unions" in order to improve our knowledge of this widely recognized but understudied issue.

1. Why Credit Unions matter

"Credit Unions represent one the most important sources of financing for small-scale entrepreneurs in developing countries" (Magill, 1994, 144). This statement is now almost fifteen years old, and even with all the development microfinance has experienced, it still remains true. Some authors state that credit unions in some southern regions represent as much as 80% of the microfinance field (Gaboury, Quirion, 2006) and major academics stress their importance for the field : "Credit unions are playing an increasingly active role in the microfinance market today" (Armendariz, Morduch, 2005, 74). This is the key issue: not only is the role of credit unions important, but it has also been increasing lately.

Credit unions were born in 19th century Europe and Canada, where they became very successful. From there, they spread all over the world. This included most developing countries, which have experienced major development starting in the 1950's. Today, there are more than 46,000 credit unions, servicing about 172 million people in 92 countries (WOCCU, statistics, 2006).

Of course, not all of them are involved in microfinance, as many of them are active in developed economies. In 2006, it was estimated that Africa, Asia and Latin America had 31,725 credit unions, servicing more than 59 million members.[5] These numbers are impressive, but their growth is even more striking. In 1996 in Africa, Asia and Latin America, a total of 20,512 credit unions were servicing 16 million members. So, in 10 years, those regions have seen a growth rate of more than 54% in the number of institutions, and more than 268% growth in the number of members.[6]

Table of Credit Union growth in Africa, Asia and Latin America :

	2006		2005		2004		2003	
Areas	**CU**	**Members**	**CU**	**Members**	**CU**	**Members**	**CU**	**Members**
Africa	8 237	13 145 565	7 468	9 602 714	7 856	7 162 689	6 492	5 888 101
Asia	21 158	32 699 855	18 662	31 229 523	15 593	11 131 203	16 530	11 101 144
Latin America	2 330	13 895 915	1 983	12 386 384	1 819	10 180 180	794	6 385 433
Total for southern countries[7]	**31 725**	**59 741 335**	**28 113**	**53 218 621**	**25 268**	**28 474 072**	**23 816**	**23 374 678**
World	**46 377**	**172 010 203**	**42 705**	**157 103 072**	**43 147**	**136 299 943**	**40 421**	**123 467 445**
Percentage South/total	**68%**	**35%**	**66%**	**34%**	**59%**	**21%**	**59%**	**19%**
Annual growth in southern countries	**12,85%**	**12,26%**	**11,26%**	**86,90%**	**6,10%**	**21,82%**	**3,87%**	**19,87%**

	2002		2000		1998		1996	
Areas	**CU**	**Members**	**CU**	**Members**	**CU**	**Members**	**CU**	**Members**
Africa	4 406	3 065 797	3 267	2 135 463	4 053	2 360 809	3 383	2 275 781
Asia	16 586	10 897 528	14 338	8 801 241	14 215	8 689 213	13 578	9 071 452
Latin America	1 937	5 536 274	1 375	3 604 476	1 738	6 967 436	1 555	4 876 144
Total for southern countries	**22 929**	**19 499 599**	**18 980**	**14 541 180**	**22 004**	**18 017 458**	**20 512**	**16 223 377**
World	**40 258**	**118 268 624**	**36 512**	**108 261 819**	**37 623**	**100 752 861**	**36 543**	**89 802 750**
Percentage South/total	**57%**	**16%**	**52%**	**13%**	**58%**	**18%**	**56%**	**18%**
Annual growth in southern countries	**20,81%**	**34,10%**	**-13,74%**	**-19,29%**	**7,27%**	**11,06%**		

References: calculation was made with WOCCU statistics :
http://www.woccu.org/intl_system/global.php, « 2006 » *World Council of Credit Unions.*

Apart from this quantitative data, it should be stressed that credit unions are also important players in the microfinance field because their profile is somewhat specific in

[5] CU in southern countries represented 68% of the total CU and serve 35% of the total CU numbers. We can conclude that credit unions in southern countries have a smaller average size than credit unions in northern countries. Based on WOCCU statistics, see the table below.

[6] The world growth of credit unions for the last ten years (1996-2006) was 27% in terms of institutions and 91,5% in terms of members. So we can see that growth was higher in southern countries, especially in terms of members.

[7] The "Southern countries" appellation groups together Africa, Asia and Latin America (so it is an approximation;we do not take into account the Caribbean, the Middel East and Oceania).

what they provide to micro-entrepreneurs of developing countries. Two aspects should be mentioned.

First, credit unions can sometimes work better than other institutions, partly because they work out of local savings. This gives them a real advantage (Westley, Shaffer, 1997), as we now know that, in order to serve poorer customers, microsavings is at least as important, if not more important, than microcredit[8] (Robinson, 2001).

Second, as explained by Defourny and Develtere for the third sector as a whole, credit unions exist because they match a need, and because they can be based on a "collective identity based on a common faith" (Defourny, Develtere, 1999). As suggested by Gaboury and Quirion : "Financial cooperatives are institutions that have grown up from the base and are therefore organized in close proximity to the communities they serve. Typically they are often located in rural areas or in communities that are ignored by other institutions" (Gaboury, Quirion, 2006, 3).

But to be sure, this is not that different from what has been experienced in the past by developed economies. At the beginning, credit unions were born out of necessity and were the only institutions interested in the people they started with ; along the way they built up around a common identity which gave them their strength and very deep roots (their "cooperative gene" as some would say). If we take the famous Raiffeisen network as an example, we can stress with Armendariz and Morduch that "whereas villagers in the 1860s often had no choice but to deposit their saving in the Raffeisen cooperatives, their grandsons and granddaughters definitely had. It appears that villagers, after leaving their initial suspicion behind, came to regard the Raiffeisen cooperative more and more as an extension of their own business" (Prinz, 2002, 17 ;Armendariz, Morduch, 2005, 70).

Today, in developing countries, the situation is fairly similar. At the beginning, credit unions are often developed in rural areas, and based on models inspired from the North (Fournier, Ouedraogo, 1996). Their success is largely linked to their ability to build on a common identity, in order to secure all the personal investment – often benevolent – that the sound development of a cooperative requires.

2. Growing through networking

As stated previously in this paper, microfinance credit unions are clearly growing at the present time. This growth is almost always based on the development of networks, which generate many changes for those institutions : changes in the number of layers in the structure (at the local, regional, and sometimes national levels), changes in procedures (including the problems with aggregating data coming from different sources), and changes in human resources (from purely benevolent to paid employees and managers), among others.

[8] This difference is key when one wants to compare the services provided by credit unions with NGOs, as those are often not authorized to collect public savings. For some authors, many credit unions are able to manage small savings in a sustainable way (Hirschland, 2005). For others, however, this advantage should not be overemphasized as many credit unions have not yet taken full advantage of this characteristic (Magill, 1994).

In this context, before tackling corporate governance issues as such in the next section, it is first necessary to review how those networks emerge, how they work and their main characteristics. Indeed, understanding growing credit unions' corporate governance will largely be about understanding how this networking can be established and controlled without damaging the very essence of the credit unions that are part of it.

Based on the work of Coase and Williamson, transaction cost economics consider networks as one of the hybrid forms of organizations that are somewhere between "markets" and "hierarchies". This choice is supposed to be justified in that, by being so, credit unions can benefit from some integration, without going into the problems that a full merger would generate. Various reasons are often used to justify the choice of many growing credit unions to develop a network : economies of scale (to spread the cost of professional managers and computerization, among others), liquidity management (thanks to cross-operations between units), financing (because, as a bigger and more diversified player, it is often easier to get access to external funding, from either commercial or non commercial sources), exchanges of experience, and internal control. To focus on this last item, "networks provide substitute, hierarchy based, control mechanisms when size of the institution dilutes internal governance mechanisms thus discouraging subgoal pursuits and expense preferences, and possibly, economizing on bounded rationality both occurring in large financial cooperatives" (Desrochers, Fischer, Gueyie, 2003, 22).

However, networking also generates problems and costs which must be taken into account. The establishment of superior levels in the structure (at local, regional and national levels) is usually fairly costly, as those levels require investments in infrastructures and staff (usually better qualified and therefore better paid). In some case, the local units may not be profitable enough to sustain such a development, and the sustainability of those higher layers may be questioned (Fournier, Ouedraogo, 1996). Additionally, in developing a more sophisticated network structure and/or a more diversified membership, credit unions may sometimes endanger their core identity, as the development of the network might require choices which may not be entirely compatible with their original mission[9]

Of course, networks are very diverse and it is not possible to state "standards points of view" which would fit all situations. Credit union networks range from extremely lean and decentralized structures, to almost totally centrally integrated ones, based on factors both internal (such as history, culture, membership) and external (such as legislation, partnerships, financing supports).

Various classification systems have been suggested. We will mention some of them here.

Desrochers and Ficher (2005) establish three categories : "Atomized Network", "Consensual Network" and "Strategical Network". In the "Atomized Network", links between first tier credit unions are very weak, and few or no resources are pooled. The

[9] For instance, there are cases of rural born microfinance networks, which tend to move to urban areas in order to reduce their average costs of operation. This can make perfect sense in order to improve the network management, but can also lead the organization to move away from the rural areas somewhat.

central structure largely plays only a representative role.[10] The "Consensual Network" is more integrated than the "Atomized Network". It works in a consensual way and exploits economies of scale. The central structure manages the pooled resources and works to establish a unique image of the network, but first tier credit unions are not required to use network services, and keep strategic decision control and management in their hands.[11] Finally, the "Stategical Network" is the most integrated type of network. First tier credit unions are financially linked. They are required to follow collective decisions and to use network services. Strategic decision control and management are transferred to the central structure.[12]

Di Salvo (2006), who has worked on European financial cooperative systems, offers four categories: the "Centralised System at the national level", the "Centralised System at the regional level", the "Decentralised System but integrated on a legal base" and "Decentralised System but integrated on a voluntary base". The first type is the most integrated network, with a high level of power concentrated at the national level. The autonomy of the first tier credit union is very limited. Whereas, in the last type of network, the first tier credit unions keep their legal identity and are totally autonomous concerning decision control and management.

As we can see, the common criteria to the analysis is the level of integration adopted by the credit union networks. When relating this to governance issues, however, opinions may diverge. Gaboury and Quirion (2006) are fairly positive : "Federated networks facilitate supervision (external or internal) for two reasons: 1) standardization of operations facilitates the analysis of operations in each base unit and 2) a federated network, due to the contractual solidarity uniting the financial cooperatives, has a strong interest in developing its own internal control and surveillance mechanisms which could facilitate the work of control, if it is so desired. Integration in federated networks also allows a better monitoring of the cooperatives by establishing standards and transparent mechanisms of data collection." (Gaboury, Quirion, 2006, p11). Others, like Chao-Béroff and her co-authors think that the more complex the network becomes, the more difficult it becomes to secure good governance practices. For some institutions, working at the national level would therefore be an inappropriate goal, and other arrangements might be more appropriate. CVECAs (in Mali and Burkina Faso) are cited as an example. "The CVECAs have a two-level structure comprising village banks at the base and regional associations, and have opted for a regional dimension with a very decentralised modus operandi. They chose to use the existing banking system to handle the most complex banking functions. This type of structure follows the logic of decentralised financial systems by making the members and committees as accountable as possible. Moreover, it is efficient and inexpensive." (Chao-Beroff and al., 2000, p13).

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[10] According to Fischer and Desrochers, the following networks belong to the "Atomized Network" category : Confecoop (Colombia), Remaining Credit Unions (UK), Cooperative Rural Banks (Philipines) and Bolivian's Credit Unions (Bolivia).

[11] According to Fischer and Desrochers, the following networks belong to the "Consensual Network" category : Fenacrep (Benin et Perou), Otiy (Madagascar), Nyesigiso (Mali), Ontario's Credit Unions (Canada), Banca Popolare (Italy), Cajas Espanolas (Spain), Japan's Credit Unions (Japan), NCUA (United States).

[12] According to Fischer and Desrochers, the following networks belong to the "Stategical Network" category : Desjardin (Canada), Raiffeisen (Germany and Italy), ILCU (Ireland), Shinkin Banks (Japan), Cofac (Uruguay) et Pamecas (Sénégal).

To conclude this section, it can be said that credit union networks may vary widely from one region to another, based on many different internal and external factors, and that "the study of the causes, modalities and consequences of alliances and networks of systems of financial cooperatives is a fertile territory of research with important implications for financial cooperatives performances" (Desrochers, Fischer, 2005, 20).

3. The specificities of corporate governance issues for Credit Unions

Corporate governance tend to be more complex in cooperative structures, compared with classical firms, due to their democratic principle for decision-making, but also because their ownership is usually much more diffuse. This makes corporate governance a fairly touchy issue for credit unions, even more so when they enter growth dynamics.

In this section, we will first try to sum up the main governance problems that credit unions experience, and we will then show how they can be worsened in times of growth.

When reviewing the relevant literature, four types of conflicts seem to sum the main governance issues we should consider here. By far, the first two are the most essential ones, whereas the third and the fourth are present but less crucial. Let's take them one at a time.

First, there is the "moral hazard" conflict between "net borrowers" and "net savers". In a typical microfinance institution, some clients have more loans than savings, while others are in the exact opposite situation ; this is what makes them "net borrowers" or "net savers". In credit unions, the issue is particularly vital as they are all members of the credit union, and as such, they all have the same right to influence the management of the structure through the one person-one vote system. This can generate two main types of conflicts. In the first, the net borrowers tend to dominate ; in this case, the board may tend to prefer too favourable conditions in the providing of loans (conditions, interest rates, etc.), which can affect the viability of the credit union. In the second, the net savers tend to dominate ; in which case, the board may create to restrictive conditions for allowing credits (in order to protect their savings). Of course, both cases are sub-optimal as "experience has shown that better governance is achieved in credit unions that have a balance between net savers and net borrowers" (Branch and Baker in Rock, Otero, Saltzma, 1998, 27).[13]

Second, there is the conflict between owners and managers. For some authors, based on research conducted in Columbia, this is the most important conflict credit unions face (Fisher, Desrochers, 2002). It is the classical principal-agent agency theory case, where the whole debate is to identify how owners can assure that managers will make decisions aligned with their best interest. As with any other type of firm, two related issues are at stake : first the "expense preferences" issue, where the question is to verify that the choices made by the managers match the mission of the organization and not his/her personal interest ; and second, the "entrenchment" issue where the manager(s)

[13] It is possible to tackle the "borrower-domination" situation. Branch and Baker (1998) mention two keys : "Borrower-domination governance problems common to traditional credit unions are ameliorated or eliminated by avoiding external credit and upgrading savings services.".

make their choices based on securing their own permanence in the structure. For Fisher and Desrochers (2002), in the case of credit unions, these two types of behaviours have opposite impacts on their risk of bankruptcy : expense preferences translates into lower efficiency and higher bankruptcy risk, while entrenchment generates risk-averse choices and lower bankruptcy risk.

But unfortunately, some authors feel that "expense preferences" are even often more at work in credit unions than in shareholders structures. Desrochers, Fisher and Gueyie (2003) give three reasons for that : first, the one person–one vote principle which tends to increase the "free-riding" behaviour of all members (because no one member has enough influence to really care to check the others) ; second, the members' shares are not tradable (and therefore, there is no market mechanism to value the quality of the management and bring pressure for better management) ; third, there is no risk of being bought out.

As for the entrenchment issue, there is also reason for concern in the long run. Indeed, the issue at stake may not be so much the fact that some people tend to stay, but much more to identify how the structure will be able to face their eventual departure. From this point of view, credit unions often face a major challenge, as some key figures might be extremely hard to replace, which generates a major operational risk in the case of an unexpected departure.

Third, there is the conflict between the members and their elected board of directors. "Board directors are democratically elected by membership (one person, one vote) but they may remain beholden to individual members who have mobilized votes on their behalf" (Rock, Otero, Saltzman, 1998, 27). Additionally, as suggested by Chao-Béroff and her co-authors, "The classic governance problem experienced by mutualist systems occurs at several levels due to the diluted ownership of the cooperative structure which can encourage elected committee members to promote their own interest rather than those of the members" (Chao-Béroff et al, 2000, 14). This is even more of an issue when communication becomes a problem. In research conducted in Mali, Wampfler and Mercoiret studied a case where, because information did not flow properly between the members and their elected representatives, power tended to be monopolized by a few individuals (Wamplfler, Mercoiret, 2002, 13).

Fourth, there is the conflict between (paid) employees and volunteers. This is a typical problem of balance that many third sector nonprofit organizations face. When they start, credit unions often work with volunteers who understand their work as part of a personal commitment in a collective project which makes sense for their community. Later, when the structure becomes bigger, it is often necessary to recruit some employees. These people often have a higher education (in order to be able to handle the more complex business of the credit union), but a different type of vision. At that stage, it is essential to properly redefine everyone's job. "Once the credit union achieves a scale which allows it to hire professional staff, it needs to separate decision-making and decision-control functions. As credit unions move to this level of professional operation, problems of governance impair operation if volunteer board members engage in decision-making rather than in decision-monitoring behaviour" (Branch, Evans, 1999, 7).

Of course, the four types of conflicts that we just described are not the only ones that are be found when studying the relationship between all the stakeholders linked to credit union development. But, they sum up reasonably well the most frequent ones from a general point of view.

In the case of growth, the situation may become even trickier. “Credit unions (…) face constraints as they grow : they lose their information advantages, they are forced to rely on salaried rather than voluntary managers and they must increasingly count on formal sanctions to enforce contracts. Growth compels credit unions to act increasingly like formal financial intermediaries. With growth, the altruistic motives that may have led to the formation of the credit union are replaced by hard-headed business decisions. (…) Principal-agent problems, transaction-costs, and prudential regulation also become increasingly important as credit unions grow” (Adams, 1999, 48). Fundamentally, the issue is to make sure that the organization does not give up the original principles and specificities that make it special for its members (Magill, 1994, Fournier, Ouedraogo, 1996). In order to give a better overview, we have identified three risks which may influence the development and governance of credit unions in times of growth.

The first risk is linked to a change in the nature of the membership, which can lead to a change in mission, and a higher risk of free-riding among the members. When a credit union decides to grow, it can do so in a number of ways. To limit ourselves to two “classical cases”, it can focus on the same type of members but try to cover a wider geographical area (eventually utilizing the network system that we discussed in the previous section), or it can stay in the same area but open itself to members working in different activities than the original founders of the credit union. Both scenarios offer pros and cons for the institution. On the “plus” side, by opening themselves, credit unions attract new customers with different financial profiles (in terms of cash flow cycles and credit and savings needs), allowing the credit union to have a better mix of financial profiles in its portfolios. On the “minus” side, the more diverse and diffuse the members base is, the more risk there is that members stop identifying themselves with the credit unions, thereby more easily adopting a free-riding attitude, which would ultimately result in lower scrutiny and weaker corporate governance (CGAP, 2005). Of course, some compromise can be found. For instance, a credit union could open to other members for daily operations, while structuring the decision-making process in such a way that the original founders maintain control of the institution’s structures in practice. In its research on governance, CERISE has documented the case of CECAM in Madagascar, which is an example of this type of compromise (CERISE, IRAM, 2005, 42).

The second risk is linked with the recruiting of (significant numbers of) new staff in times of growth. In any firm, when facing extensive growth, recruitment will tend to be an issue. Not only there is a need (which is not always easy to fulfil) to find enough of the right people at the right time, but there is the huge challenge to integrate the new people properly into the structure. When a structure is hiring progressively, newcomers tend to be influenced by former workers and managers and therefore they adapt to the structure by incorporating progressively the procedures and culture of the firm. When growth is happening fast (especially in decentralized network structures), the number of newcomers will be such that often there won’t be enough “old” employees to format the newcomers. In such a situation, it may therefore happen that growth by itself generates a loss in procedures and culture, resulting in management problems[14]. In the typical credit union’s context, all this may happen and be worsened by the conflict

[14] Even if it has not been the case so far, norms and values in microfinance institutions deserve to be studied, as shown by Hudon (2008).

mentioned above between "old volunteers" and the "professional salaried" newcomers. Not only will there be many new people to accommodate, but they will be of a different profile, resulting in even more complex problems to deal with.

The third risk results from the increasing complexity of the products, the organisation and the structure of the credit union network (with an increasingly longer distance from the local units). First, the increasing complexity of products and organisation can lead to inadequate members' knowledge and thus reduce members' control. Branch and Baker (1998, 5) notice this issue : "As organizations become larger and more complex, they require specific knowledge and skills to make a range of specialized decisions. Individual owners are not likely to possess the required managerial skills and technical knowledge." Second, as we have seen in the previous section, growth in credit unions often happens through networks based on different layers (local, regional, and national/federal). When this happens, the chances to see a certain distance established between the local credit unions and their "roof" structure is quite high. As mentioned by Chao-Beroff and her co-authors : "The federal level of the mutualist networks is the most susceptible to risk. Because of the existence of multiple layers of delegated power, elected members at this level are almost completely immune to the social control of grass-roots members" (Chao-Beroff et al, 2000, 15). This sometimes translates into a divergence in strategies, with managers sometimes being more inclined toward growth than local members (Fournier, Ouedraogo, 1996, 78).

4. The search for the right mechanisms

Corporate governance mechanisms can be defined as the whole set of mechanisms which put pressure on the organizations and their managers in order to make sure that the decisions made match the mission of the organization. In the case of credit unions, because of the democratic principle, the mission is defined by the members, who are also in charge of controlling the organization. This makes credit unions quite different from other microfinance organizations. When dealing with corporate governance mechanisms for traditional banking institutions, the attention is usually focused on two of them : the action of the board, and the incentives provided to managers (Marsal, Bouaiss, 2007). Of course, those mechanisms are of prime importance, but others exist.

Charreaux has identified a wide range of corporate governance mechanisms. He has sorted them in four categories, based on two criteria : on the one hand, are they spontaneous (meaning, "generating corporate governance but without having been created for this purpose") or intentional (meaning, "mainly created in order to improve corporate governance") ? On the other hand, are they specific (meaning, "specific to a firm") or non-specific (meaning, "applying to all firms of the industry") ? (Charreaux, 1997). This framework has received wide acceptance in the corporate governance research field, and some work has already been done in order to show what it could provide to the understanding of corporate governance for nonprofits (Labie, 2005). We will therefore use it in order to formalize our analysis by reviewing the four categories in the case of credit unions.

First, the intentional and specific mechanisms, created for each specific firm and aiming to improving corporate governance. They are the most well-known and the most studied. A good example is the "board of directors". Many authors insist on the way it should function in order to secure better corporate governance. As an exemple, we can quote Niederkohr and Ikeda who wrote that "First, WOCCU recommends the board be composed of an odd number of members, no less than five and no greater than nine. [...] Second, World Council recommends that consideration should be given to the rotation of directors. [...] Third, interested credit union members, compliant with the individual governance standards of integrity, competence and commitment, should be allowed to stand for the nominating process." (Niederkohr, Ikeda, 2005, p5). But in the case of credit unions, it is not always easy to match those recommendations for two reasons. First, because board members are usually volunteers from the union membership, they often lack the kinds of skills that such a role would require (Rock, Otero, Saltzman, 1998). "Boards dominated by volunteer non-professionals can be very responsive to local community social issues but fail to have the financial and business expertise required for a financial institution" (Branch, Evans, 1999, 7). Second, the rotation of board members is often hard to obtain (Chao-Béroff et al, 2000), resulting in easier entrenchment behaviours[15].

Another intentional and specific mechanism is the use of incentives to reward managers (and/or employees). There is abundant literature on incentives in corporate governance considering the various advantages and shortcomings of the different ways to implement them. In the case of credit unions, the question has not really emerged. Some authors think that incentives are hard to implement in credit unions because success is more than just financial, and therefore harder to assess. Besides, stock options are not an option, as credit unions don't have tradable shares (Pellervo, *the Confederation of Finnish Cooperatives*, (2000)). Others mention that some cases of incentives-based success exist in microfinance credit unions, naming CVECA in Mali as an example (Ouattara, Gonzalez-Vega, Graham, 1999).

Second, the spontaneous and specific mechanisms, of which corporate culture, cross-control between managers and informal trust relationships are potential examples (Charreaux, 1997). In the case of credit unions, those mechanisms seem to play a key role, mainly in their start-up phase where they might even be more important than the intentional mechanisms set up in order to provide good governance. At that stage, the union will succeed or fail based on the strength and dedication of its members, who often act as volunteers. This is the period of "social control" or "peer monitoring" as it is often called. "Members repay their loans not only due to social pressure but also because the money they are repaying is their own and that of their neighbours. They know that, if they do not repay their loans, in the future there may be no money at the credit union to borrow." (Morris, 1999, p26). In such a context, "the design of cooperatives encourages peer monitoring and guaranteeing the loans of one's neighbours" (Armendariz, Morduch, 2005, 73). Later, when credit unions grow and external funding sometimes becomes available, those mechanisms may become weaker. In fact, we can even make the hypothesis with Krahnen and Schmidt that "external funding tends to weaken peer monitoring. By expanding the volume of available funds, a credit union seeks to reach more members and possibly also to increase de size of each individual loan. The credit union may grow beyond the optimal size of peer monitoring." (Krahnen, Schmidt, 1999, 22).

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[15] In some credit unions, a credit committee and/or a supervising committee are established. Theoretically, they should strengthen the corporate governance by reinforcing the internal control. However, in practice, it often needs to be well-defined in order to avoid an unnecessary sophistication of the structure perceived as without use (Pellervo, 2000).

Third, the intentional and non specific mechanisms. In this category, Charreaux mentions items like the legal framework, the role of legal authorities, or trade unions (Charreaux, 1997). In the credit union field, the main two are clearly the regulation and supervision frameworks and procedures established either at the country level, or – as with "the Parmec law" - at a more regional level (Western Africa in that case). Of course, in that area, there is often a wide gap between the official statements and what is really done in the field, and in many cases, supervision is weaker than it should be. As for how to do so properly, it is not totally clear yet which scheme is most appropriate. For Fisher and Desrochers, "the increasing common approach adopted in Africa, Asia and Latin America to fold FC *(Financial Cooperatives)* under the same R&S *(Regulation and supervision)* framework used for (stock owned) commercial banks is inappropriate and dangerous. Basle standards of R&S simply lack the focus on the control of agency conflicts that is so essential to prudential supervision of mutual intermediaries" (Fischer and Desrochers , 2002, 23). At the same time, for Adams, "when credit unions are mobilizing significant amounts of deposits and handling other public funds, they should also be prudentially regulated by an agency that is capable of doing so, and that is not itself involved in the promotion of credit unions".(Adams, 1999, 49). So, defining how regulation and supervision should be implemented is not that easy. But what is obvious is that in order to support good governance, specific regulation and supervision should be carefully implemented.

Fourth, the spontaneous and non-specific mechanisms. They include a whole set of items that belong to the environment of the firm, and may have an indirect influence on its governance. For Charreaux, these include various markets (market for goods and services, credit market, labour market), the social and political environment, and the business culture of the country where the firm operates (Charreaux, 1997). In the credit unions' case, those seem to play a much lesser role, even though we can imagine cases in which the "subsidies market" or the "banking refinancing market" could generate some indirect pressure, with credit unions using good corporate governance practices as a means to signal themselves to donors (and/or bankers).

When we consider those four categories in the specific case of credit unions, we can imagine that, to some extent, all may be present at different stages in the growth process. Social capital, peer monitoring, and a culture closely linked to the mission and the cooperative spirit are certainly essential at first. Later, when the organization grows and becomes progressively more complex, with a larger geographical coverage and with a combination of volunteers and professional paid staff, one could imagine that other mechanisms start to play a more active role. At that stage, corporate governance could become more and more of an explicit concern, and specific and intentional mechanisms will probably receive more attention. This leads us to a fairly interesting dilemma. In Charreaux's classification, structure is part of the intentional and specific mechanisms, because one of the goals when establishing a structure is indeed to make sure that the organization does what it is supposed to do, and do it well. But with credit unions, the evolution of the structure is also, as we have seen, a fundamental consequence of growth, resulting in network management which may represent in itself a challenge for the governance of the unions.

5. A research agenda

Obviously, the corporate governance of microfinance credit unions is a promising field for research : doubts and questions are numerous, and the consequences of right or wrong choices seem to clearly matter. Credit unions represent a tremendous potential force for providing financial services to many people who have been previously excluded from formal financial intermediation. Right now, as we have seen, credit unions are multiplying and growing, often through network structures. A key question therefore appears to be : can credit unions provide good governance and experience growth at the same time, without giving away their very essence ? In order to tackle this question, we think that – at least – four research projects should be led.

The first one could focus on the understanding of what makes a credit union. Legal title is obviously not enough. Some organizations, while not working under the cooperative title are very close to be doing so ; while on the other hand, there are many cooperatives which are no longer animated by the cooperative spirit. Therefore, being able to define and therefore to identify which organizations we intend to deal with seems a fundamental but necessary step. This could also lead us to another related question, which is to define the criteria which would allow us to point out when a cooperative structure stops working like one. This is, of course, of high interest if we want good governance because, working on good governance for credit unions only makes sense if really applied to true credit unions. As part of this research, the attention provided to education and training as part of the cooperative mission could also be assessed.

The second research effort could focus on the networking structures adopted by credit unions when growing. What are the consequences, in terms of governance, of getting structured as a network ? What are the real differences generated by the various types of networks ? Does it make a difference if the credit unions' network is linked to another organization (for instance a farmers' association) ? These are questions which have not been thoroughly considered yet.

The third research effort could then focus on the relationship between governance and growth. Is it only that growth is influencing the corporate governance practice (in quality, mechanisms favoured, and so on), or could it also be that, depending on the type of dominating governance mechanisms, growth could be generated more or less easily ?

Fourth and last, the question of which mechanism is really crucial at each stage of the development of the credit union is fundamental. In this paper, we have tried to show that there is enough material to build a framework of analysis and formulate some reasonable hypotheses. But of course, these still need to be tested.

Corporate governance is a concept that has won its legitimacy in the context of profit-driven, pure private companies. Using it thoroughly to offer a better understanding of how credit unions can grow under relevant control without losing their "cooperative gene" remains to be done.

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