The Challenge of Core Costs

It is important to have a clearly stated policy on how your organisation will cover its core costs. These costs have to be funded just like any other cost incurred in an NGO.

The starting point is to produce a separate budget for core costs so they do not get overlooked or ignored.

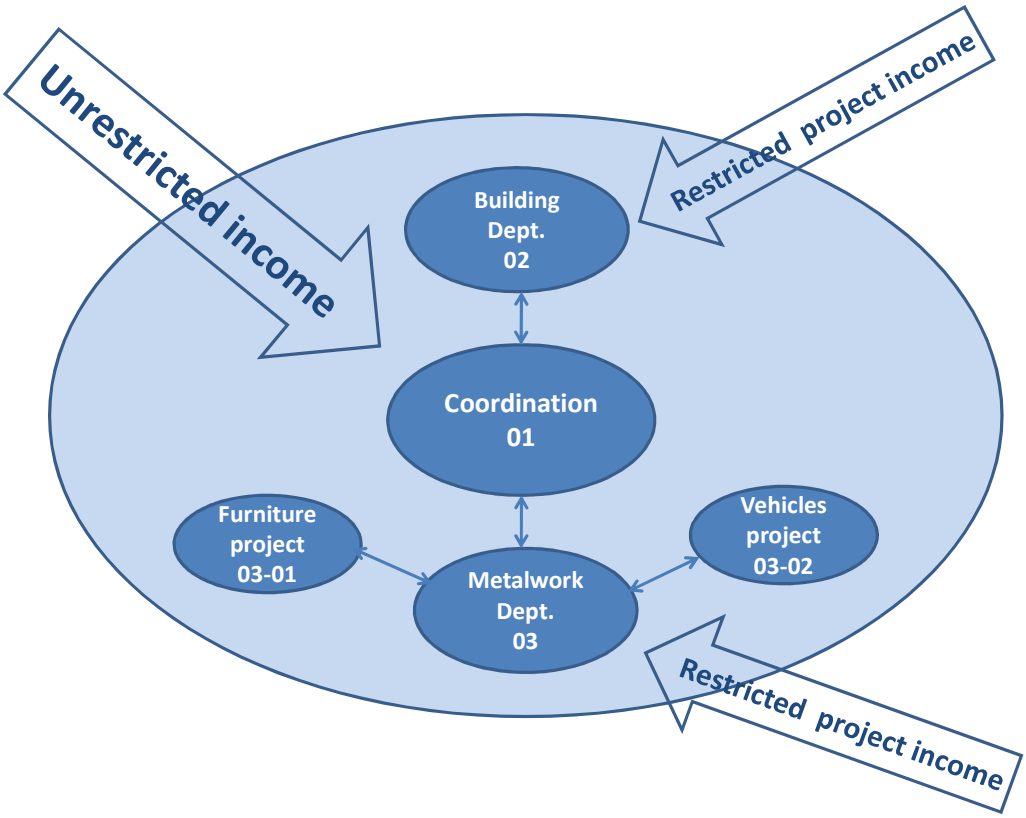
There are essentially two ways – or a combination of both – to fund your core costs:

- Use unrestricted funds (ie money given to the organisation for general purposes) to cover all or part of core costs; or
- Charge core costs out to projects using a pre-arranged apportioning ratio.

The diagram below shows how this works in practice for Milestone. Their restricted funds come in and get recorded at project level; unrestricted funds come in centrally are used to help pay for some of the core costs. Some project funds are also used to contribute to the core costs of the Coordination Department.

The methods which can be used to charge out core costs to projects are covered in a later chapter.

Figure 3.4: Financing Milestone's Core Costs



The Challenge of Multiple Donor Programmes

When a programme or project has more than one donor, it can present a number of financial planning problems. In particular,

- Donors have different budget formats and layouts, which they require you to use when applying for funds.
- Budget line items and descriptions vary, so it is not clear exactly what each category includes or excludes, eg 'Transportation' vs. 'Travel' vs. 'Vehicle Running costs'
- It is not always clear who is paying for what activity or item.
- Different donors have different policies on core costs. It is not always clear if all the core costs are covered.
- Sometimes double funding occurs for certain budget items whilst other items are under-funded.

Some Solutions

A carefully designed and detailed Chart of Accounts

If the Chart of Accounts is detailed enough, it will be able to cope with different donor budget formats. For example, the category 'Transportation' in an NGO's Chart of Accounts is extended to:

- Fuel & Lubricants
- Vehicle Maintenance
- Vehicle Insurance
- Public transport
- Air travel
- Distribution costs…etc

Use the budget worksheet approach to cost all projects

Because this approach provides a very detailed budget it is possible to transfer the information to any other budget formats as required. The level of detail provides maximum flexibility.

Include some 'indirect costs' as direct project costs in project budgets

Include as many project costs as possible in the project budget, including a share of the indirect project costs, such as office rent or a percentage of the Director's salary.

Take care: all costs must be justifiable.

Prepare a 'funding grid'

A funding grid is a special table which provides an overview of which donor fund is paying for what part of a budget.

It is an internal planning tool which should be updated regularly as new information becomes available. It is also useful for re-negotiating funding agreements and identifying fundraising needs.

How it works:

- The overall project or programme budget is detailed in column 1.
- Donor budgets are entered in the next columns and reconciled to the overall project or programme budget.
- Unrestricted funds are then entered to 'plug the gaps'.
- The final column identifies any double funding and remaining funding gaps.

Table 3.4 Example Funding Grid –Milestone Project (extract)

		Milestone's Confirmed Funding					
		RESTRICTED FUNDS			UNREST'D FUNDS		
Budget item	**Total Budget**	**DFID**	**Smile Trust**	**Vanguard**	**General donations**	**Total expected funds**	**Surplus/ (deficit)**
	USD	*USD*	*USD*	*USD*	*USD*	*USD*	*USD*
Admin.	38,100	9,000	9,000	0	13,200	31,200	(6,900)
Staff	71,000	18,000	18,000	9,000	26,000	71,000	0
Travel	51,000	11,000	11,000	2,000	6,500	30,500	(20,500)
Training	111,200	52,000	52,000	10,000	0	114,000	**2,800**
TOTALS	**271,300**	**90,000**	**90,000**	**21,000**	**45,700**	**246,700**	**(24,600)**

In the example above, we can see that:

- there are some predicted funding gaps for the Admin and Travel budget lines (indicated by the negative figures in brackets);
- a predicted surplus of funds on the Training budget line of USD 2,800 (indicated by the positive figure); and
- overall, Milestone *appears* to be USD 24,600 short of the funds it needs.

However, Milestone must not assume that it can keep the 'extra' USD 2,800 on the Training line and use it elsewhere in the budget: these funds are restricted and – strictly speaking – this presents a 'double funding' situation.

In this case, Milestone must contact the donor(s) and make a request to re-allocate the surplus funds on the Training line to other budget lines where there are funding gaps. If the donors refuse, the surplus restricted funds must be given back to the donor.

Chapter 4

Understanding Accounts

An Introduction to the Mysteries of Accounting Concepts and Jargon

This chapter:

- Discusses why an NGO needs to keep accounts
- Describes the different methods used to keep track of financial transactions
- Outlines which accounting records to keep
- Defines and explains key financial accounting concepts and terminology
- Describes the financial statements which are prepared from the accounts

Why Keep Accounts?

Good financial records are the basis for sound financial management of your organisation:

Information

All organisations need to keep records of their financial transactions so that they can access information about their financial position, including:

- A summary of **Income and Expenditure** and how these are allocated under various categories.
- The **outcome** of all operations – surplus or deficit, net income or net expenditure.
- **Assets and Liabilities** – or what the organisation owns and owes to others.

Credibility

NGOs especially need to be seen to be scrupulous in their handling of money – keeping accurate financial records promotes integrity, accountability and transparency and avoids suspicion of dishonesty.

■ Legal requirement

There is often a statutory obligation to keep and publish accounts and donor agencies almost always require audited accounts as a condition of grant aid.

■ Future planning

Although financial accounting information is historical (ie happened in the past), it will help managers to plan for the future and understand more about the operations of the NGO. With information spanning two or three years, it is possible to detect trends.

Accounting Methods

Keeping accounts simply means devising appropriate methods for storing financial information so that the organisation can show how it has spent its money and where the funds came from. Accounting records can be kept in a manual format – ie hardback books of account – or in a computerised format in one of many accounts packages available.

There are two main methods for keeping accounts:

- ✓ Cash accounting
- ✓ Accruals accounting

The two methods differ in a number of ways but the crucial difference is in how they deal with the timing of the two types of financial transaction:

- **Cash transactions** which have no time delay since the trading and exchange of monies takes place simultaneously.
- **Credit transactions** which involve a time lag between the contract and payment of money for the goods or services.

Significantly, the method we choose to record transactions will produce different financial information – so as managers we need to know the basis of accounting to better understand financial reports.

■ Cash Accounting

This is the simplest way to keep accounting records and does not require advanced bookkeeping skills to maintain. The main features are:

- Payment transactions are recorded in a Bank (or Cash) Book as and when they are made and incoming transactions as and when received.
- The system takes no account of time lags and any bills which might be outstanding.
- The system does not automatically maintain a record of any money owed by (liabilities) or to (assets) the organisation.
- The system cannot record *non-cash* transactions such as a donation in kind or depreciation.

When summarised, the records produce a *Receipts and Payments Account* for a given period. This simply shows the movement of cash in and out of the organisation and the cash balances at any given time.

See Appendix 7 for a sample Receipts and Payments Account.

■ Accruals Accounting

This involves '*double entry*' bookkeeping which refers to the dual aspects of recording financial transactions to recognise that there are always two parties involved: the giver and the receiver. The dual aspects are referred to as debits and credits. This system is more advanced and requires accountancy skills to maintain.

- Expenses are recorded in a *General Ledger* as they are incurred, rather than when the bill is actually paid; and when income is truly earned (ie we are 100% certain it will be paid) rather than when received.
- By recognising financial obligations when they occur, not when they are paid or received, this overcomes the problem of time lags, giving a truer picture of the financial position.
- The system can deal with all types of transactions and adjustments.
- The system automatically builds in up-to-date information on assets and liabilities.

These records provide an Income and Expenditure Account summarising all income and expenditure committed during a given period; and a Balance Sheet which demonstrates, amongst other things, moneys owed to and by the organisation on the last day of the period.

Table 4.1 Summary of differences between Cash and Accruals Accounting

	CASH	ACCRUALS
Accounting system	Single Entry	Double Entry
Transaction types	Cash only	Cash and Credit
Terminology	Receipts and Payments	Income and Expenditure
Main Book of Account	Bank (or Cash) Book	Nominal (or General) Ledger
Skill level	Basic bookkeeping	Advanced bookkeeping
Non-cash transactions	No	Yes
Assets & Liabilities	No	Yes
Reports produced	Receipts & Payments Report	Income & Expenditure Report with Balance Sheet

■ Hybrid Approach

Many NGOs adopt a 'half-way house' approach. They use the cash accounting basis during the year and then (often with the help of the auditor) convert the summarised figures at the year-end (or more frequently) to an accruals basis for the final accounts and audit.

This includes keeping separate books to record and identify accruals and prepayments (see examples below), unspent grants and capital purchases during the accounting period.

See Appendix 10 for a Schedule of Creditors and Debtors, identified for Milestone's year-end adjustment process.

Example of an Accrual

An electricity bill covering the last month of the financial year is not received until 4 weeks after the year-end. Even though the payment will be made during the new financial year, the expenditure must be recorded in the financial year that the electricity was consumed. It shows up as a liability on the Balance Sheet

Example of a Prepayment

Office rent is paid six months in advance. Half of the payment covers the first quarter of the new financial year and is therefore deducted from the office rent account for the current year at the year-end. It is carried forward to the rent account for the financial year when the rent falls due and shows up as a prepayment on the assets list in the Balance Sheet.

Which Accounting Records to Keep

For a small NGO with very few financial transactions, a simple bookkeeping system is all that is needed. As an organisation grows and takes on a number of projects and different sources of funding, its reporting requirements, and therefore its financial systems, will become more sophisticated.

Accounting records fall into two main categories:

- ✓ Supporting Documents
- ✓ Books of Account

■ Supporting documents

Every organisation should keep files of the following original documents to support every transaction taking place:

- Receipt or voucher for money received
- Receipt or voucher for money paid out
- Invoices – certified and stamped as paid

- Bank paying-in vouchers stamped and dated when money is taken to the bank
- Bank statements
- Journal vouchers – for one-off adjustments and non-cash transactions.

With these documents on file it will always be possible to construct a set of accounts. Other useful supporting documents include:

- Payment Vouchers (PVs)
- Local Purchase Orders (LPOs)
- Goods Received Notes (GRNs)

Books of account

The minimum requirements for books of account are:

- Bank (or Cash) Book for each bank account
- Petty Cash Book

For organisations with salaried staff, valuable equipment and significant levels of stock, the following records, where relevant, may also be kept as part of a full bookkeeping system:

- General/Nominal Ledger
- Journal or Day Book
- Wages book
- Assets Register
- Stock Control Book

Supporting Documentation

It is very important to maintain supporting documents in the form of receipts and vouchers for all financial transactions. These should be cross-referenced to the books of account and filed in date or number order.

RECEIPTS EXPLAIN:

- When?
- How Much?
- What?
- Who?
- Why?

Apart from being required by the external auditor to support the *audit trail*, certified receipts also provide protection to those handling the money. Mislaid or incomplete records can result in suspicion of mismanagement of funds.

Keep separate files for receipts for money coming into the organisation and money going out. Mark invoices 'paid' with the date and cheque number to prevent their fraudulent re-use by an unscrupulous person.

Well maintained files provide invaluable information to the organisation such as the trends in price increases, details of equipment purchased, past discounts, etc.

Bank Book Basics

The Bank Book – or Cash Book or Cash Analysis Book – is the main book of account for recording bank transactions (ie 'cash' transactions). It is normal to maintain a separate Bank Book for each bank account held as this makes it easier to reconcile each account at the end of the month. [See Appendices 3 and 4 for a sample Bank Book.]

With a manual (paper based) Bank Book, receipts are usually entered on the left side and payments on the right and each page is ruled into columns (see Figure 4.1 for a typical layout). The number of columns required will depend on the type and volume of transactions.

Each transaction is entered on one line of either the Receipts page or the Payments page in date order. The column headings prompt you to enter key information – eg date, cheque number, payee, description, amount, category of transaction, etc. The columns are totalled at the end of each page or accounting period.

Analysis columns

These are what make the Bank Book such a useful record. These columns (numbered 1 to 9 in **Figure 4**.1) include the main categories of income and expenditure as identified in your Chart of Accounts and your budget. They allow you to sort and summarise transactions by budget category which in turn helps to compile financial reports quickly and easily.

Figure 4.1: Typical Bank Book layout

LEFT SIDE																			**RIGHT SIDE**
Receipts of Money Into The Bank										Payments Out of The Bank									
Date/details	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**Date/details**	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**

Bank Reconciliation

The Bank Book should be checked with the bank's records – the bank statement – at least once a month. This is called the *bank reconciliation*. The purpose of this process is to make sure that the organisation's own records agree with the bank's records and to pick up any errors made by the bank or the organisation.

A bank reconciliation involves taking the *closing bank statement balance* for a particular date and comparing it to the *closing Bank Book balance* for the same date. If there is a difference between these two closing balance figures, the difference must then be explained.

In practice, there will almost always be a difference because of timing delays, such as:

- Money paid into the bank which is not yet showing in the bank's records
- Cheques issued to a supplier but not yet banked by the supplier
- Bank charges and bank interest which get added to the bank statement by the bank periodically
- Errors either made by the bank or when recording entries in the Bank Book.

See Appendix 6 for a completed bank reconciliation form and Appendix 19 (p age A23) for a blank form to help you with this process.

Petty Cash Book

Petty cash records are kept in a similar way to the Bank Book records. As both sets of figures will eventually have to be combined to produce financial reports, it makes sense to set out the books in a consistent manner. A sample Petty Cash book can be seen in Appendix 5.

The Petty Cash Book can either be kept in a loose leaf or bound book format. It does not however, require more than one analysis column on the Receipts side because the only money that is paid into petty cash is the float reimbursement.

The Petty Cash Book will also require fewer analysis columns for payments because petty cash will not (usually) be used to pay for larger items such as salaries, office rent, etc.

There are two ways of keeping petty cash:

- ✓ fixed float or *imprest* system
- ✓ variable or non-imprest system

■ Fixed Float or Imprest Method

With the *imprest* system you have a fixed float of, say, $50 and when the cash balance gets low, you top up the float by exactly the same amount that you have spent since the float was last reimbursed.

<u>Example:</u>

Receipts/vouchers for cash spent total:	$34.60
Cash remaining in cash box counted::	<u>$15.40</u>
TOTAL FLOAT:	**$50.00**
∴ Reimbursement cheque written for:	$34.60

An advantage of this system is that at any time you count the money plus vouchers in the tin, they should always add up to the fixed float amount. Also, it is much easier to incorporate petty cash spending into the accounts as the reimbursement cheque is entered in the analysed Bank Book.

See how the reimbursement cheque for the petty cash book in Appendix 5 has been written in to the Bank Book in Appendix 4. Look for cheque no. 13583 on 12/01.

■ Variable float or non-imprest method

An alternative is to draw cash from the bank in round sums as required.

If you use the non-imprest method you will need an extra column in your Bank Book headed 'petty cash withdrawn'. When reconciling this float you will have to add up all the petty cash withdrawals since the last reconciliation and add on the cash balance brought forward to get a total of the cash float for the period. This total should then be the same as the total spent since the last reconciliation plus the cash left in the tin.

A more complicated and time consuming process!

Full Bookkeeping Systems

Organisations requiring a full bookkeeping system use a series of *ledgers* (this just means books of account), depending on the activities of the organisation.

■ The General or Nominal Ledger

This is a central record which pulls together basic bookkeeping information from the main working books of account (Bank Book, Petty Cash Book, Sales and Purchase Ledgers). It is like a series of 'pigeonholes' used to sort basic financial information and is especially useful when an organisation has several projects and different donors requiring different reports.

The General (or Nominal) Ledger has one page for each category of income, expenditure, assets and liabilities and information is 'posted' from the other accounting books into each pigeonhole. It plays a central role in the double-entry bookkeeping system and is the basis for the Trial Balance (see below), the starting point for preparation of financial statements.

■ Other Ledgers

Other elements in a full-bookkeeping system include:

- Sales ledger and sales day book (but only if you have sales)
- Purchase ledger and purchase day book
- Stock ledger
- Journal

These, together with the Bank Book and Petty Cash Book are the day-to-day working accounts books. It is quite possible to set up a General Ledger without these additional ledgers; the choice will depend on the activities of your organisation.

The **Journal** is used to record unusual, one-off transactions which cannot be recorded easily in other books of accounts. These will include non-cash transactions (such as *depreciation* and donations-in-kind), adjustments and corrections.

A *journal entry* follows the rules of double entry and will always include entries to at least two accounts. For example, a donation-in-kind in the form of rent-free office space would be recorded as income under 'Donations' and expenditure under 'Office Rent'.

■ Wages Records

Employers have a statutory duty to maintain records of all wages paid and deductions made and failure to do so could result in a heavy fine. Be sure to familiarise yourselves with the arrangements of your own Department of Taxes and get hold of the latest tax deduction tables.

Larger organisations should also keep a separate Wages Book, which brings together all information on staff salaries and deductions. These can be purchased from stationery suppliers in a pre-printed format and they help to facilitate the year-end reconciliation or available as add-ons to accounting software packages.

What is a Trial Balance?

The *Trial Balance* (or what accountants often refer to as the 'TB') is simply an arithmetical check on the accounts maintained using the Double Entry method of accounting. It is also the basis for the preparation of accruals-based financial statements.

At the end of an accounting period – usually monthly – all the accounts categories having a balance in the General Ledger are listed on a summary sheet to form a Trial Balance. Providing no errors have crept in during the recording and summarising stages, the total of debit balances on the list will equal the total of the credit balances.

Figure 4.2: Trial Balance leading to financial statements

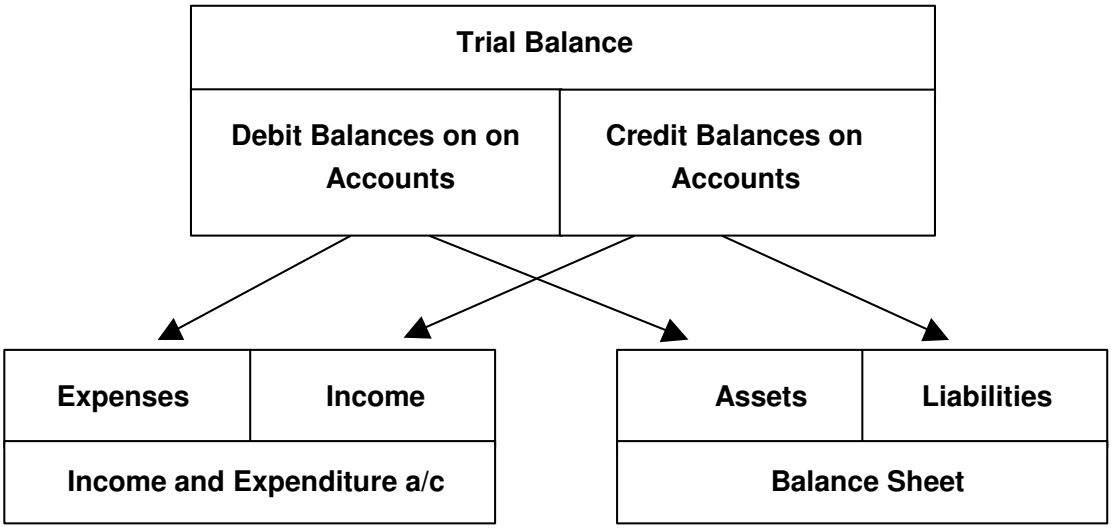
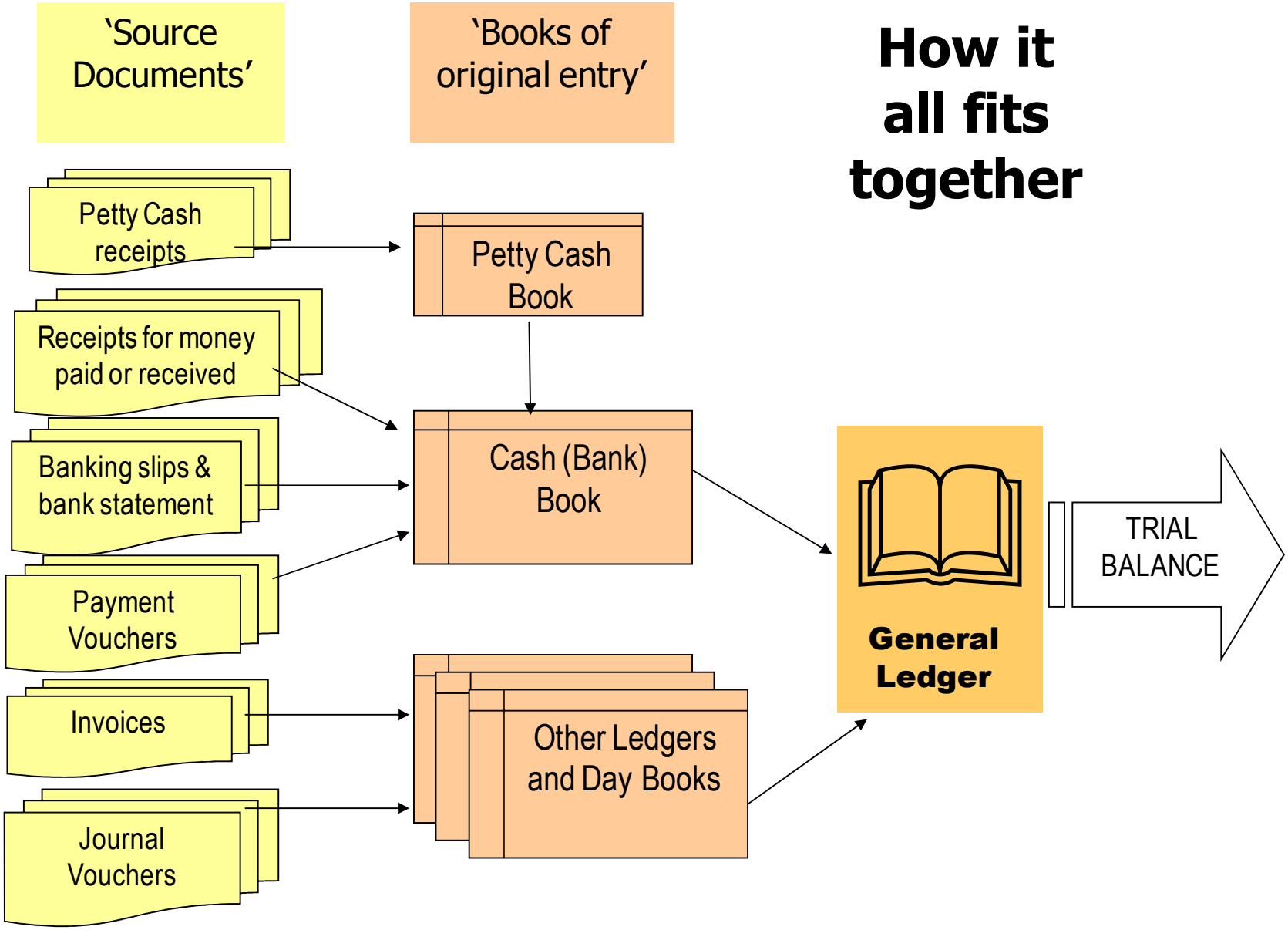


Figure 4.3 shows how the Trial Balance is the final stage of the accounting process – the result of recording, classifying and summarising the many different transactions that take place in an organisation. **Figure 4.2** illustrates which figures from the Trial Balance end up where in the annual financial statements.

Figure 4.3: How it all fits together



What are Financial Statements?

Financial statements are a product of the financial accounting process. They are a summary of all the transactions for a specified period and show the financial position of an organisation.

Financial statements can cover any period of time – for example, a month, a quarter or one year. The annual financial statements are used as the basis for an annual external audit.

The simplest of all financial statements is the Receipts and Payments report. This is a summary of the Cashbook (see Appendix 7) and includes details of cash balances at the start and end of the reporting period.

The other two main reports relevant to NGOs are:

- ✓ The Income and Expenditure report
- ✓ The Balance Sheet

Together these contain a lot of useful information. In the chapter on Financial Reports, we look at how to analyse the information in the financial statements.

The Income and Expenditure Report

In the not-for-profit sector, the equivalent of the Profit and Loss Account is the Income and Expenditure Report (or Account). See Appendix 8 for an example.

It is either produced from a *Trial Balance* (as described above) where the accruals-based system of accounting is used; or it is based on a Receipts and Payments account with adjustments for 'loose ends'.

It records as a summary:

- all categories of income and expenditure which belong to that year;
- all income not yet received but belonging to that financial year; and
- all payments not yet paid but belonging to that financial year

Income items usually appear first in a list down the page, followed by the summary of expenditure items. The difference between total income and total expenditure, often called the *outcome*, appears on the bottom line and is expressed either as:

- 'excess of income over expenditure' where there is a surplus; or
- 'excess of expenditure over income' where there is a deficit.

This excess figure is then included on the Balance Sheet under the heading Accumulated Funds.

Note that there should be an accompanying Balance Sheet for the same date that the Income and Expenditure Account is prepared at.

The Balance Sheet

The purpose of a Balance Sheet is to assess the financial position – or 'net worth' – of an organisation at a given date. If the organisation ceased operating at that date and all of its assets were converted into cash, and all of its debts were paid off, then what was left over would be what the organisation was 'worth'. See Appendix 9.

> *The balance sheet is a list of all the assets and liabilities on one particular date and provides a 'snapshot' of the financial position of an organisation.*

■ Components of a Balance Sheet

The Balance Sheet is in two parts. One part records all balances on **assets** accounts; the other records all balances on **liabilities** accounts plus the income and expenditure account balance. The Balance Sheet will either be presented with the Assets listed on the left and the Liabilities presented on the right of the page, or more commonly nowadays, listed down the page with Assets presented first then Liabilities deducted from them.

Fixed assets

These are the tangible, long-term, assets such as buildings, equipment and vehicles, having a value lasting more than one year. Fixed assets are shown on the balance sheet after an allowance for wear and tear – or *depreciation* – has been made (see an explanation of what depreciation is later in this chapter).

Current assets

These are the more 'liquid' assets such as cash in the bank, payments made in advance and stocks. These, in theory at least, can be converted into cash within 12 months.

Liabilities are also divided into current liabilities and long-term liabilities.

- **Current** or **short term** liabilities – including outstanding payments, and short-term borrowings – ie those having to be paid within 12 months.
- **Long-term** liabilities such as loans that need to be paid after 12 months. (However, for NGOs such borrowings are not common.)

Accumulated Funds

Accumulated Funds and Reserves are separated out from other liabilities and act as a balancing item on the Balance sheet. They represent the true worth of the organisation – in the form of capital and/or cash reserves which have been built up from surpluses in previous years. Accumulated Funds are classified as liabilities since, in an NGO, the funds are held in trust for the organisation in pursuance of its objectives.

Liquidity

The term liquidity is used to describe how easy or otherwise assets can be turned into cash. So money held in a bank account is deemed to be very liquid, while money tied up in a building is clearly not liquid at all.

Working capital

This is the same as *net current assets,* that is, the short-term assets remaining if all immediate debts were paid off. These are the funds that the organisation has available as a cushion or safety net for running the organisation's operations.

The table below summarises the main components and typical layout of a balance sheet, although note that terminology does vary.

Table 4.2 Components of a Balance Sheet

Component:	Description:
FIXED ASSETS:	The less liquid assets – those having a significant value lasting more than one year.
CURRENT ASSETS:	The more liquid assets – can usually be converted into cash within one year.
- Cash	Funds held in the bank and as cash.
- Debtors	Money owed to the organisation such as loans and unpaid sales invoices.
- Prepayments	Value of items paid for in advance such as insurance premiums or equipment rental.
- Grants Due	Grants owed to the organisation for projects already started in the reporting period.
- Stocks	The value of raw materials or supplies such as publications or T-shirts for sale.
CURRENT LIABILITIES:	Those paid within one year of the year-end.
- Creditors & Accruals	Money owed by the organisation at the year-end such as bank overdrafts, unpaid bills.
- Grants in Advance	Grants received for a particular purpose but not yet spent in full, so carried forward to the next financial year.
OTHER LIABILITIES:	Longer term commitments and General Funds.
- Reserves	Money set aside for specific purposes, eg replacing equipment. Although designated funds, they form part of the organisation's General Funds.
- Accumulated Funds	Accumulated surplus of income over expenditure achieved since the organisation opened.

What is Depreciation?

Capital expenditure, such as that on buildings, computer equipment and vehicles, is expenditure which covers more than one accounting period and retains some value to the organisation.

Depreciation is the way that accountants deal with the cost of wear and tear on fixed assets. It allows the original cost of the item to be spread over its 'useful life'.

The amount calculated for depreciation is shown as an expense in the accounts and deducted from the previous value of the asset. As it is a non-cash transaction, depreciation is entered in the accounts using a journal entry.

There are several methods used to calculate the cost of depreciating assets, but the two most commonly used are: Straight Line method and Reducing Balance method

In the **Straight Line method** the amount to be depreciated is spread evenly over a pre-arranged period. For example, a computer purchased for USD 1,000 expected to last for 4 years will be depreciated at USD 250 per year for 4 years. At the end of 4 years the computer will have a zero *net book value* – ie it will have no value as far as the accounts are concerned. In reality, it may have a second hand market value.

The Reducing Balance method fixes a percentage reduction in value so that the item loses more value in the earlier years.

Example:

A car is purchased for USD 10,000. It is decided to depreciate it over 4 years – ie by 25% per year. The table below shows how the equipment is depreciated over its useful life (all figures are rounded to nearest dollar).

Depreciation schedule

Year	Depreciation calculation	Net Book Value
Year 1	$10,000 x 25% = $2,500	$7,500
Year 2	$7,500 x 25% = $1,875	$5,625
Year 3	$5, 625 x 25% = $1,406	$4,219
Year 4	$4,219 x 25% = $1,055	$3,164

Note that when using this method, the asset is never completely written off. At the end of the 4th year it will still have a *residual value*. In this example, the car will be valued in the accounts at USD 3,164. This recognises that the item may have a resale value when it comes to replacing it.

Accounting for Shared Costs

Core costs are usually shared out between cost centres in a pre-arranged ratio. This can either take place as the transaction is entered in the accounting records or at the end of the reporting period by making one adjustment entry. The decision on how to apportion costs between cost centres can be based on different criteria according to what is known as the *cost driver*, for example:

- Number of employees in the projects
- Number of cost centres
- Size of each project budget
- Project staff costs
- Amount of space used by department
- Number of clients/beneficiaries
- Actual consumption, eg kilometres travelled, photocopies made.

There is no hard and fast rule for allocating overheads to projects; rather logic should be applied and the criteria chosen should be justifiable.

For example, in allocating central support staff salaries to projects, the number of employees in the project could be used; and for apportioning the cost of office rent, the actual space occupied by project staff is applicable.

Whatever method is chosen, it must be fair and justified, and once established it should be applied consistently.

Chapter 5

Financial Reports

Making Sense of the Numbers

Introduction

This chapter:

- Identifies the who, what, when and why of financial reporting
- Explains how to interpret financial statements using trend and ratio analysis
- Explains how to compile and use the information in management accounts
- Outlines the important features of donor reports
- Outlines reasons for reporting to our beneficiaries

Who Needs Financial Reports?

As we have seen, one of the main reasons for keeping accounting records is so that information about how the organisation is being run can be obtained. Having set up accounting systems and budgets, the next step is to produce financial reports to report on and monitor the organisation's financial affairs.

Providing the accounts are kept in a suitable way and have been checked for accuracy, putting together a financial report is not as time-consuming as you might think.

Financial reports must be timely, accurate and relevant

Financial reports are needed primarily by those responsible for managing the organisation and by current and potential donor agencies; but those responsible for financial management of an NGO also need to 'give an account' of their stewardship to a wide range of stakeholders.

Table 5.1 summarises the main users of reports and why they need this information.

Table 5.1: Who needs financial information about NGOs?

Stakeholder	Why do they need it?
Project staff	To know how much money and resources are available for their projects and what has been spent so far.
Managers	To keep an eye on how project funds are being used, especially compared to the original plans. To help plan for the future.
Finance staff	To make sure that there is enough money in the bank to buy the things the NGO needs to run its programmes.
Board of Trustees	To keep an eye on how resources are being used to achieve the NGO's objectives.
Donors	To make sure that their grants are being used as agreed and that the project's objectives are being fulfilled. To consider whether to support an organisation in the future.
Government departments	To make sure that the NGO pays any taxes due and that it does not abuse it status as a 'not for profit' organisation.
Project beneficiaries	To know what it costs to provide the services they are benefiting from and to decide if this is good value for their community.
The general public	To know what the NGO raises and spends during the year and what the money is used for.

From this list, we can see that there are many different users of financial reports – both internal and external stakeholders – using financial information for management and accountability purposes. It is not surprising, therefore that we need different kinds of reports for different users, as summarised in **Table 5.2** below.

- During the financial year accounting information is summarised and turned into *Management Accounts* for internal monitoring of progress against the budget.
- At the end of the year, the *Annual Accounts* (ie the Balance Sheet and Income and Expenditure Account) are produced to report on the outcome to external stakeholders.
- At intervals during the year, an NGO will also be required to complete special *progress reports to donor agencies*.

Table 5.2: Different Reports for Different Users

	Programme management	Stakeholder accountability
Internal	Management Accounts – Budget Monitoring reports and Cashflow reports	Board reports
External	Donor progress reports (financial and narrative)	Donor reports Audited Financial Statements Reports to beneficiaries

What are the Annual Accounts?

We return to the Balance Sheet and Income and Expenditure Account. These annual financial statements show in summarised form:

- where money has come from;
- for what purpose it has been received;
- how it has been spent; and
- what the outcomes of operations are.

They should be prepared as soon as possible after the end of the financial year – for example within six weeks – and made ready for the external audit. The organisation's constitution will often specify the deadline for presentation of accounts to the members.

The Annual Accounts, accompanied by the Annual Report, form the main publicity and information package available and will be of interest to many users. For this reason, the annual accounts should:

- present the organisation in the best possible light;
- help to promote its work;
- meet the needs of those using the accounts; and
- meet the requirements of auditors.

If an NGO's annual accounts show large accumulated funds, it may give the impression that the organisation is well resourced and donors may be less inclined to give support to new initiatives.

There are however, good reasons why an organisation will have cash reserves – for example, funds put aside to replace equipment or a building appeal fund. An explanation must be provided to reassure potential donors that their support really is needed.

Interpreting Financial Statements

The aim when reviewing an NGO's financial reports is to assess the health of the organisation and to check that funds are being used as intended – ie to achieve organisation objectives.

Numbers taken on their own don't tell us very much. We need something to measure them against – such as comparing them to similar organisations, standard measures or targets, or previous years' accounts.

When we interpret the Balance Sheet and Income and Expenditure statement we use two types of financial analysis:

- **Trend analysis** which asks: How are we doing compared with the last period?
- **Ratio Analysis** which provides a means of interpreting and comparing financial results.

Trend Analysis

Trend analysis takes at least two sets of figures compiled using the same accounting techniques and showing information for two consecutive periods, usually year on year. By comparing the figures it may be possible to detect trends and use this information to forecast future trends or set targets.

Trend analysis is more meaningful if also combined with financial ratio analysis.

Financial Ratio Analysis

Financial *Ratio Analysis* is used widely in business to assess the profitability and efficiency of companies. Ratio analysis in the not-for-profit sector is less common, but is nonetheless very useful if adapted for the sector.

Ratios allow comparison of reports expressed in different currencies and between organisations of different scale by converting them into a like measure. Donor agencies often use this technique when assessing performance, especially to compare relative costs – such as central administration – between similar organisations or projects.

The importance of ratios is in the clues they may provide to what is going on, not as absolute measures of good or bad performance. Ratio analysis helps Board members and managers answer three important questions:

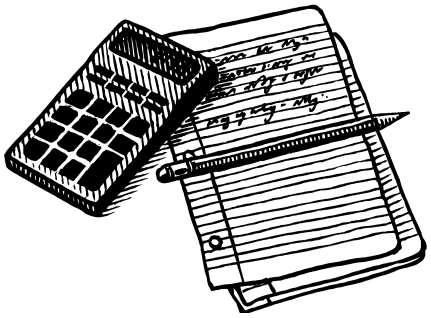
- **Financial sustainability** – will our organisation have the money it needs to continue serving people tomorrow as well as today?
- **Efficiency** – does our organisation serve as many people as possible with its resources for the lowest possible cost?
- **Effectiveness** – is our organisation doing a responsible job of managing its money?

Analysing the Income and Expenditure Account

You can use ratios on the Income and Expenditure report by converting each line item into a percentage of total income (that means to divide each item by total income and multiply by 100). This gives a guide as to the relative importance of different areas on the statement. For example, the relative costs of administration versus direct project costs. This is useful for drawing attention to the important areas and away from insignificant issues.

This calculation will also give an indication of the level of **donor dependency** – by dividing the total of donor grants by total income and multiply by 100. If your financing strategy is leading you towards less dependence on external aid, the dependency ratio will help to set and monitor your target level.

A further level of analysis can be obtained by comparing the ratios for the current and previous years' figures to detect trends.



Analysing the Balance Sheet

Again try dividing everything by the total income figure shown on the accompanying Income and Expenditure statement to give an indication of the relative importance of items on the Balance Sheet.

A **'Survival Ratio'** can be calculated by dividing general reserves , sometimes called 'free reserves' (that's the part of the Accumulated Funds which are unrestricted, not held as capital and for general use) by total income (from the accompanying Income and Expenditure statement).

If you then multiply the resulting figure by 365 this will give an indication, in days, of how long the organisation could survive in the coming year if income dried up and levels of activity remain the same. Of course, this is a highly hypothetical scenario as in practice the organisation would contract operations if its income was drastically reduce.

The **Acid Test** or Quick Ratio asks the question: *Can we pay off our debts now?* It divides Current Assets less the less 'liquid' assets such as stocks and prepayments (in other words, short term debtors and cash balances only) by Current Liabilities (short-term creditors and overdrafts). The resulting ratio should ideally be in the range of 1:1. A ratio of 1:1 suggests an organisation has sufficient cash to pay its immediate debts.

The **Current Ratio** asks the question: *Can we pay off our debts within 12 months?* It divides total Current Assets by total Current Liabilities to find a further test of an organisation's (longer term) liquidity. A result of 2:1 is considered satisfactory. Again, convert the figures for both years shown on the Balance Sheet to detect significant trends.

Ratio Analysis – Quick Reference Formulas

RATIO:	FORMULA:
1. **Donor Dependency:** Expressed as %	TOTAL DONOR INCOME / TOTAL INCOME X 100
2. Income Utilisation: Expressed as %	EXPENDITURE ITEM / TOTAL INCOME X 100
3. 'Survival Ratio': Expressed in weeks or days	GENERAL RESERVES* / TOTAL INCOME X 52 or X 365 * these are un-restricted funds for general purposes under Accumulated Funds. Alternatively use Net Current Assets.
4. Acid Test or Liquidity Ratio: Expressed as a ratio n:n*	CURRENT ASSETS – PREPAYMENTS / CURRENT LIABILITIES *Answer should be in the range of 0.8 to 1.2:1. A result of 1 to 1 means there are sufficient funds to cover immediate debts.
5. Current Ratio: Expressed as a ratio n:n*	CURRENT ASSETS / CURRENT LIABILITIES *A result of 2:1 is considered satisfactory – enough to pay off the debts within 12 months.

Management Reporting

Managers need financial information throughout the financial year to monitor project progress and manage budgets effectively. If reports are produced on a timely basis, any problems can be addressed early on and action taken to put things right.

■ How often?

Ideally, the management accounts should be produced every month and within a few days of the end of the accounting period (any later and the information becomes out of date and less useful). The minimum frequency for management reports is once a quarter.

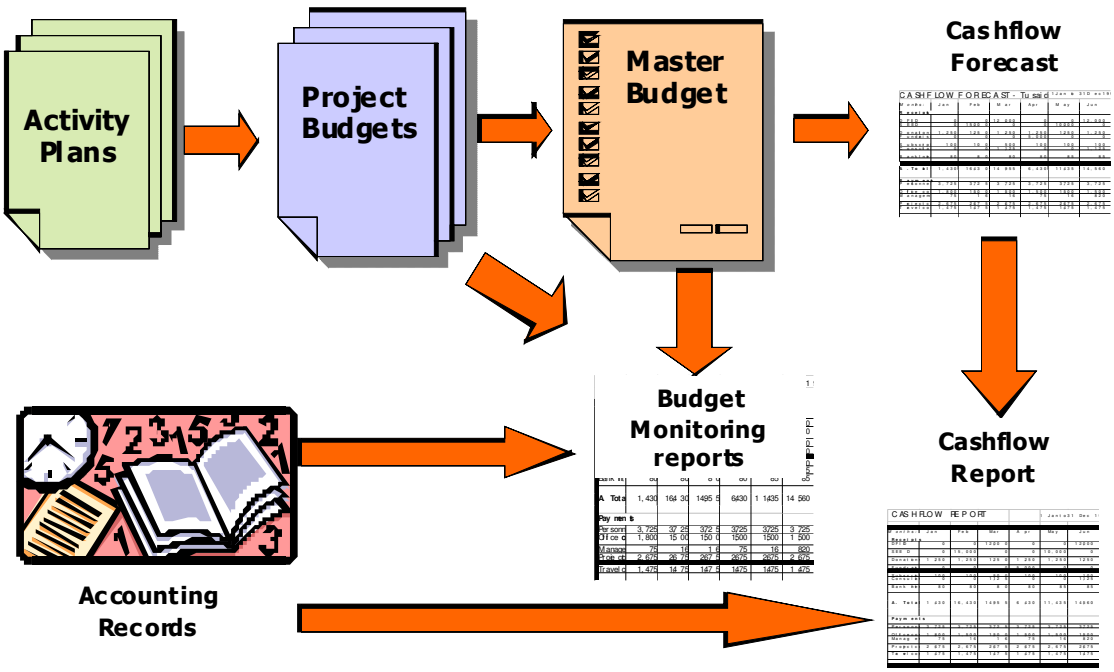
Since the reports are produced so that managers can take decisions about the future management of the organisation, the meetings of the governing body should be set to coincide with the Management Accounts cycle so that the information is still timely.

■ Where do the figures come from?

Figure 5.1 shows how the financial planning and financial accounting processes come together to produce management reports.

The reports are compiled by taking summarised figures from the main books of account and the budget for the same period. Providing the accounts and budgets have been set up to use the same Chart of Accounts codes and descriptions, this should be a very quick process and no additional work is required.

Figure 5.1: Management Reporting Flow Chart



- **Which reports?**

The main reports that will be useful to managers are the:

- Cashflow Report
- Budget Monitoring Report
- Forecast Report

The Cashflow Report

The cashflow report is the cashflow forecast updated with actual receipts and payments each month, plus any new information about future spending or fund-raising plans. It allows managers to predict periods when cash balances are likely to be insufficient to meet commitments and make the most of any surplus funds during the year.

Where cash resources are limited, it is important to monitor for the ability to pay creditors on time and to take action when there are early warnings of potential financial difficulty. Options available for managing cashflow include:

- Exercise good credit control – chase debtors for prompt payment
- Review grant schedules– encourage payment in advance rather than in arrears
- Bank all monies received daily
- Request special payment terms from major suppliers (and stick to them)
- Pay certain overheads by instalment – eg insurance premiums
- Prioritise major payments
- Defer action that will lead to additional expenditure – eg recruitment, taking on leases, purchasing equipment
- Negotiate an overdraft facility as short term – but expensive – remedy

The Budget Monitoring Report

This report has several different names (eg Budget Compared to Actual, Budget Variance and Budget Versus Actual) and can take different forms. But as the titles suggest, the reports take the *budget* for the reporting period (preferably the *phased* budget) and compares that with the *actual* income and expenditure for the same period. See a sample report in Appendix 14.

The difference between the budget and the actual result is known as the v*ariance* and this can tell us a lot about what is happening in a project. Variance figures will be positive negative or zero, depending on what has happened. Often, budget monitoring reports also show variances as percentages.

For example, the amount of the budget or grant used up so far is known as the budget or grant *utilisation ratio* or the *burn rate* (see below for how to calculate percentages.)

We can see the *Plan-Do-Review* process in action in Rudi's trip to the Cinema. He set out his plans for the evening and what each activity would cost (*PLAN*) and then went out with his friends (*DO*). But it did not all go as planned and his actual spending varied as a result. If we look at the variance column in Rudi's Budget Compared to Actual Report (REVIEW) in **Table 5.3** it is possible to see the story behind the figures...

Table 5.3 Rudi's Budget Compared to Actual Report

A	B	C	D	E
Budget Item	**Budget** $	**Actually Spent** $	**Variance** $	**Budget Utilisation** %
Travel	1.50	0.75	0.75	50%
Food	3.50	3.00	0.50	86%
Entrance Fee	3.00	4.00	(1.00)	133%
TOTAL	**8.00**	**7.75**	**0.25**	**97%**

For example, we can see the effect of Rudi arriving too late to buy the cheaper cinema tickets: he spent USD 1.00 (or 33%) more than planned on the entrance fee. And because he then didn't have enough money left to buy his bus fare back home (he got a free lift home instead) he also under-spent on his Travel budget, using up only 50% of that line.

When we review the figures, and in particular the variance column, it helps us to understand why we did not fulfil the plans and build in that learning to the next cycle.

In Rudi's case, he learnt that he needs to get to the cinema early to buy a cheap ticket (and his mother learnt that it might be a good idea to give Rudi a bit extra for emergencies to make sure he gets home safely!)

■ How to Calculate Percentages

The budget variance percentage can be calculated in one of two ways. You may use either method but it is important to be consistent:

a. $\frac{\text{Budget variance \$}}{\text{Budget for } \textbf{period} \text{ \$}} \times 100$ — Under-spends will result in a positive % and over-spends will produce a negative %

b. $\frac{\text{Actual for period \$}}{\text{Budget for } \textbf{period} \text{ \$}} \times 100$ — Under-spends will result in a figure <u>less</u> than 100% and over-spends will be <u>more</u> than 100%

% Budget Utilised (or 'Burn Rate'):

$\frac{\text{Actual spend \$}}{\textbf{Total} \text{ Budget \$}} \times 100$ — A resulting figure of over 100% means the <u>total</u> project budget is overspent.

Forecast Reports

Forecast reports are especially helpful from the second quarter onwards for predicting the outcome for the year and helping with the budget process for the next year.

See Appendix 17 for a sample Forecast Report.

With a fair degree of accuracy you should be able to tell whether the organisation is going to run a surplus or deficit. This is all-important in your relationship with donors:

- A large deficit can make the organisation appear to be out of control and poorly managed
- A small deficit can demonstrate a great need and even a sense of good housekeeping
- A small surplus can suggest good management
- A large surplus can indicate a failure to meet needs or inexperience in budgeting.

There are various ways of reducing a surplus at year-end, including purchasing new or replacement equipment, ordering stocks of stationery and office supplies. There is very little that can be done about a large deficit except to provide an early warning and a very good explanation to stakeholders and hope that there are sufficient reserves to cover it.

Analysing Budget Monitoring Reports

Budget monitoring reports help to identify problem areas and provide an early warning when key targets are not being met. They may also help detect fraud and errors in the accounts.

■ What should we look for?

Here are some key areas to focus on when you pick up a Budget Monitoring Report:

- What is the **accounting basis** of the report – is it compiled on the cash or accruals basis? Are there outstanding commitments (see note below)? If so, how does that affect the results?
- What does the **bottom line** tell you? Overall, is the budget over-spending or under-spending and is it significant at this time in the life of the project tor program me? An outcome of plus or minus 10% from the budget is considered to be a reasonable variance.
- What is the result within budget **'family groups'** (ie budget items in the same area, such as Staff costs, Project inputs, Admin costs etc)? Is spending overall on target across the group? Again, if the result is within plus or minus 10% from the budget, that is generally acceptable.
- Look for unusual or **unexpected results** - could this be an indication of a mis-coding or abuse?

- Are there any **significant variances** in the individual line items? Are the reasons for the differences explained? For example, the Subsistence Expenses budget is substantially and unexpectedly over-spent. Do not just concentrate on over-spending – remember that under-spending is just as critical for an NGO.
- Do **linked budget line items** (eg activity-related costs) tell the same story or do they contradict? For example, the project materials budget is under-spent suggesting delayed activities but the vehicle running costs are high, which is not logical.
- Do the budget report figures tell the same story as the **narrative** project report?

Sometimes the figures just do not look right: trust your instincts and follow up your concerns.

A note on Commitments

Commitments refer to (significant) expenses which have been incurred for a project or organisation in a particular period but haven't yet been accounted for or belong to a future reporting period. Commitments usually occur in a cash accounting system or where there are time delays in reporting all expenditure, eg from field offices.

If significant commitments are not taken into account when compiling budget monitoring reports, the results may under- or over-count the true level of expenditure and give a distorted view when compared to the budget.

It is important to be aware of outstanding commitments when monitoring a budget or grant because decisions are based on the reported variances and balances available. It could appear that there is more (or less) money available to spend than there really is.

Here are two solutions if figures exclude outstanding commitments:

- Include an extra column in the budget monitoring report to record known commitments
- Add a note about known commitments in the comments column or covering note.

Variance Analysis techniques

Variance analysis involves looking at variations from budget to identify significant or unusual variances and what has caused them to happen. This helps us plan the next phase.

The first task is to identify whether the variance is a positive or negative one. Positive variances are sometimes described as *favourable* (ie generally good news) and negative ones as *adverse* (ie generally bad news):

A **favourable variance** happens when:

- actual income is higher than the budgeted amount, or
- actual spending is lower than budgeted (but note that this is not always good news for an NGO).

An **adverse variance** happens when:

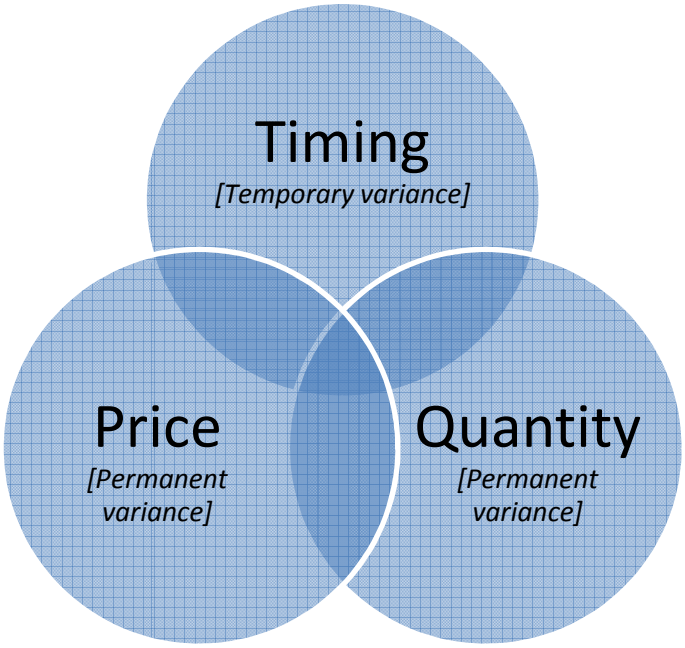
- actual income is lower than the budgeted amount, or
- actual spending is higher than budgeted.

The next step is to understand what has caused the variance to happen. In all cases, a variance represents a change from the original plan but what lies behind it? Generally, we can say that variances will be the result of a change in one or more of:

- the **timing** of the activity
- the actual **price** achieved or
- the actual **quantity** of goods or services taken.

Sometimes a variance on a report will be due to an error in the figures rather than a change in plan, for instance a mis-coding in the accounting records.

Figure 5.2: What causes variances?



We classify variances using the three criteria in **Figure 5.2** to highlight where management attention and action is required. This helps to decide if the variance is temporary or permanent – will the variance continue or will it work through the system out over time?

Temporary variances

Variances caused by a change in the planned timing of an activity (eg due to delays or rescheduling) are described as *temporary* variances because they will most likely work themselves out during the course of the year. These are therefore generally less of a concern and no corrective action is required.

Example

The project plans to purchase a vehicle in month 1 but supplies are held up at the port by Customs. The budget monitoring report will therefore show a big positive variance on the Vehicles line (because the budget has not been used yet).

By month 2 the vehicle arrives and is purchased – just a bit later than planned.

The budget monitoring report will no longer show a zero spend on vehicles and the previous large variance will be gone as it was a *temporary* variance due to a timing issue.

Permanent variances

Variances caused by changes in the price or quantity of particular budgeted items generally fall into the *permanent* variances category because once this has happened, there is no going back. The only way to recover the situation is to make an action plan, eg to reduce spending on future items.

These variances are therefore generally more serious and management attention and corrective action is required.

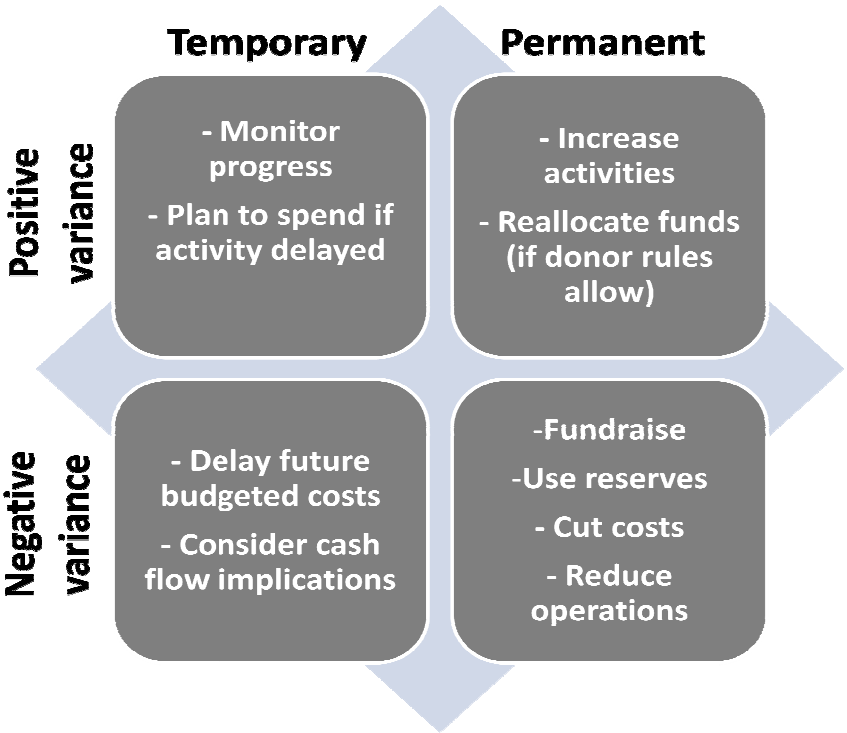
Example

The invoice for the vehicle is paid in month 3. The price of the vehicle has increased by 10% due to a fluctuation in the exchange rate.

The budget monitoring report for month 3 now shows a negative variance on the vehicles line equal to the difference between the budgeted price and the actual, higher price paid. This is a *permanent* variance caused by a change of price. A decision has to be made on how to fund the additional 10% on the cost of the vehicle

Figure 5.3 summarises the actions open to managers to take on variances, once analysed using the classifications systems described above.

Figure 5.3: Action to take on Variances



Action Planning

Having analysed the figures in management reports, it is then important to work out appropriate corrective action, if needed. Deciding on the action to take, will depend on many factors including:

- knowledge of the project – where it is now and what the activity plans are for the next period
- awareness of external factors – eg inflationary trends, dependence on other programmes meeting their targets
- how serious the variance is
- how controllable, or otherwise, the budget items are
- what the impact would be to take no action
- donor rules and conditions.

It is useful to use a Budget Management Action Planner table to help you manage and control your budget. It can be used to discuss action plans with manager and the project team and to monitor progress of the action plan.

See **Table 5.4** for an example format and **Table 5.5** for an explanation of how to use it.

Table 5.4: Budget Management Action Planner Format

Budget Management – Action Planner					
1	2	3	4	5	6
Line item description	**Variance % or £/$**	**Varianc e Type**	**Contro -llable?**	**Impact on project and grant if not corrected**	**Action required / by**
Smile Trust Grant	($12,500) 100%	Temp.	Yes	The delay is causing project delays too as we cannot buy vehicle	CEO to contact donor and explain this is causing project delays.
Salaries	$2,000	Perm't	Yes	Under spend due to vacant post. This is now filled but project activities delayed which could cause problems with donor.	Contact donor to explain why there are delays and request use of under-spend to hire additional staff for a short period to help catch up

Table 5.5: How to use the Budget Management Action Planner

Column heading	What it means
1 Line item description	The budget line that requires some corrective action.
2 Variance % or monetary value	Include items that exceed +/- 10% variation from the budget and which represent a significant sum.
3 Variance Type	Permanent or temporary? Remember that temporary variances will work their way through the system but very large ones might still have an impact, eg on cashflow.
4 Controllable?	To what extent can you control use of the budget, eg to restrict its use or make savings if over-spent or stimulate its use if under-spent.
5 Impact on project & grant management if not corrected	eg Cash flow, achieving targets, meeting timeframes, allowable costs.
6 Action required/by	What should be done (and by who) to minimise the impact and get the project back on target and/or to meet donor requirements? Eg budget reforecast or adjustments; advise donor of delays or request 'no-cost' extensions; request unrestricted funds to cover over-spends; change activity plans; put efforts into reducing costs or stimulate spending; etc.

Reporting to Donor Agencies

It is worth remembering that donor agencies are themselves accountable to stakeholders (trustees, government, tax-payers, etc.) and they rely on you to provide them with the information they need.

■ Accountability

Financial accountability requires that you demonstrate to the donor that their funds have been used for the purpose for which they were intended. The reference point is the original funding application and guidelines are usually provided with the confirmation of grant aid and the contract or agreement signed by both parties.

It is important to comply with the conditions and meet reporting deadlines to establish credibility and encourage confidence, and to make sure your grant arrives on time.

■ Terms and Conditions of Grant Aid

It is important always to check what you have agreed to do as part of the agreement for funding from each of your donors. Conditions imposed by donors vary enormously but can include:

- **Progress reports** – frequency, format and style of reports, usually quarterly to coincide with release of grant instalments.
- **Scope and designation of funds** – what funds may, or may not, be used for; whether funds can be carried forward from one financial year to the next.
- **Administrative overheads** – the specific items that are allowable or excluded, or a percentage limit based on the total grant.
- **Budget line items** – specific budget headings/account classifications which correspond with the original grant application.
- **Virement policy** – ie permission (or otherwise) to transfer surpluses in the budget from one budget heading to another, and within what limits.
- **Accounting method** – Accruals or Cash accounting.
- **Bank Accounts and interest** – separate bank accounts are required by some donors and/or they do not allow you to keep any interest earned on sums invested.
- **Depreciation policy** – how to treat fixed assets purchased with a grant.
- **External Audit** – some donors require a separate external audit.

■ The Donor Report

Donors require that an NGO is able to demonstrate financial soundness before granting the release of funds. This is why the donor report is so important. In most cases the report will include a budget compared to actual summary, accompanied by a narrative report on the activities being undertaken. See Appendix 15 for a sample donor report.

Where there are several donors it is important to set up the accounting systems so that the information required by the donor agency can be easily retrieved.

Otherwise the organisation will be involved in a tedious information gathering exercise every time a report is required. The use of Cost Centres is particularly useful here.

When putting together a report to donors do:

- meet reporting deadlines (or request an extension)
- produce accurate and verifiable figures
- not conceal under-spends or over-spends
- explain any significant variations
- keep the donor informed of any potential problems

Finally, bear in mind that donors have a lot of experience of working with groups like your own; they will almost always respond positively to requests for advice.

Presenting Financial Reports

We spend a lot of effort when preparing reports so it is important that they are used and not just put to one side. So do spend some time thinking about who the reader is and what they will find most useful.

■ 'Exceptions' reporting

Managers and Board members are busy people and they rarely have the opportunity to fully read all reports that get sent to them. With financial reports it is good idea to provide an *exceptions report* – a brief cover note that draws attention to key areas or need decisions.

The exceptions report is usually no more than one or two pages long and should avoid using technical jargon. It should be brief and easy to read. A suggested layout:

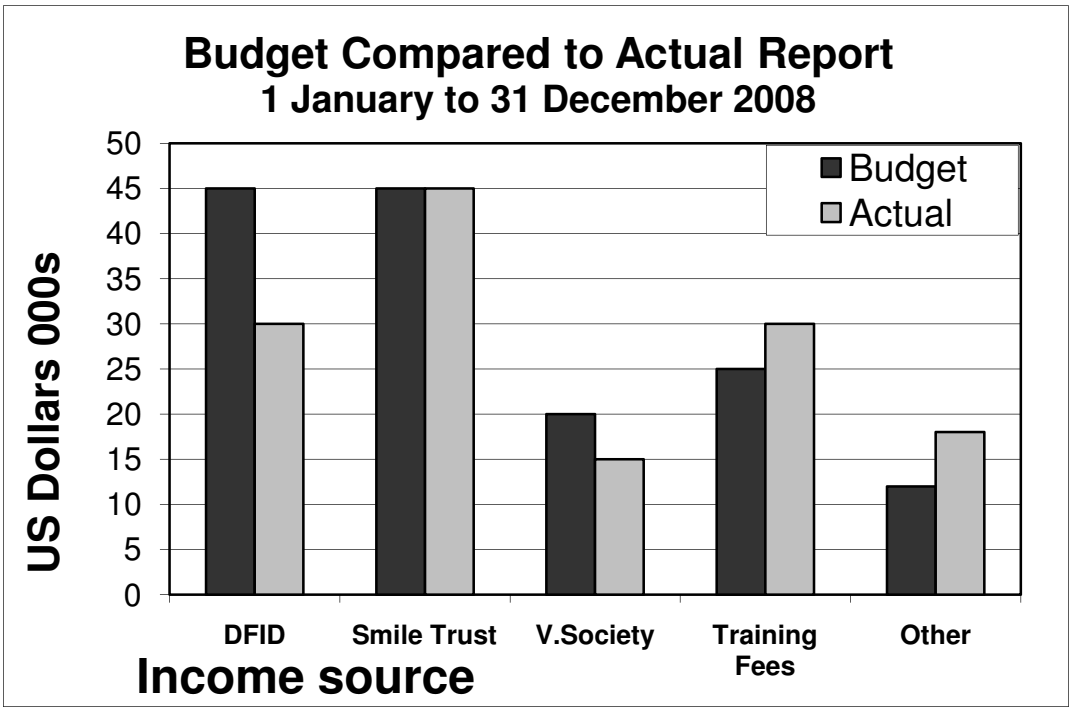
- **Overview** of the period being reported – ie dates covered; how figures have been compiled; what activities are covered by the attached reports; and author of report.
- **Significant variances** - Highlight the most significant variances from the budget and explain the reasons behind the variances. This should not just concentrate on over-spending of budgets – under-spending can also be a problem, especially when related to donor-funded projects.
- **Recommendations** for action – ie corrective action required to deal with the key issues identified in the previous section. For example, strategies to avoid a cashflow crisis in future months; revised activity plans to get projects back on target; restricting use of vehicles where running costs are running too far over budget.

■ Presentation of figures

- **Negative figures** in project financial management reports can be represented in two ways: – 1,234 or (1,234)
- Figures are usually **rounded** to the nearest whole number – the cents are not relevant to the overall review of the results. This sometimes may result in figures being out by 1.

■ Alternative formats

Figure 5.4: Using graphics for financial reports



Graphical formats – for example using a bar chart for a budget-actual report (as in **Figure 5.4**) or a pie chart for an income and expenditure report – are a welcome alternative to tables of figures, especially for people who are less confident around figures.

Similarly, rather than present figures, we might simply present a list of statements such as in this example of an alternative Balance Sheet format:

Milestone Project Financial position on 31 December 2008:

a) Our programme equipment and vehicles – after a deduction for wear and tear – had a value of **UC112,091**.

b) We had **UC8,095** help as cash and in the bank.

c) The Smile Trust owed us UC10,000 for the final quarter grant; and we had some outstanding fees and other small amounts owed to us totalling UC2,459.

d) We owed a total of UC3,262 in unpaid invoices.

e) This means that if we paid off everything we owe from our available funds, we would have **UC 17,292** to continue our operations.

f) Our overall reserves, including the value of our equipment and vehicles, total UC129,383.

See also some very interesting ideas on alternative ways to present financial information from Little Fish in Australia: http://www.littlefish.com.au

Reporting to Beneficiaries

Most NGOs recognise the need for downward accountability – ie reporting to the communities they work with. But few have set up systems to deliver it: most NGO systems focus on upward accountability, such as reporting to donors, Boards and Head Offices.

To participate fully in an NGO's work, beneficiaries need access to information about the NGO's plans, resources and activities. Increasing transparency and accountability to beneficiaries has many benefits including:

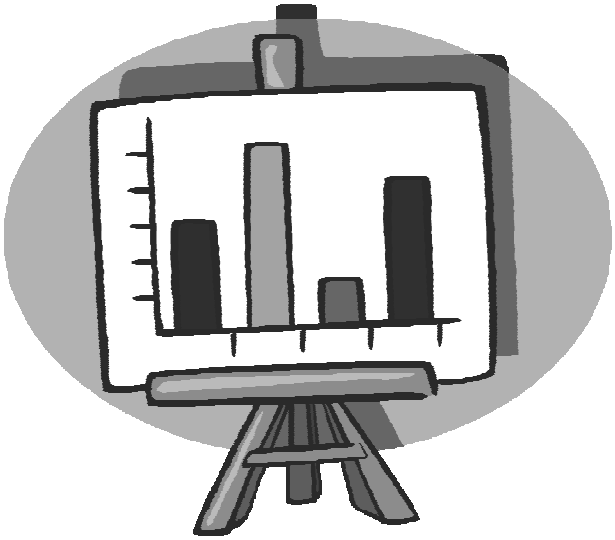
- Strengthening trust and respect between NGO staff and beneficiaries
- Improving the quality of programme decisions, as beneficiaries provide feedback on how funds are being spent
- Empowering beneficiaries to make their own decisions on their own behalf
- Reducing the risks of inefficiencies and fraud
- Encouraging finance staff to get more involved with NGO field work

Introducing this level of financial transparency may naturally hit some obstacles, such as adding to the burden of already busy staff. But if sensitively done, the benefits generally far outweigh the costs.

Some good practice ideas on how to practically report to beneficiaries include:

- Making information easier to understand by using graphical presentations
- Using white-boards outside offices to display budgets, the amounts of funds available for each area and a monthly update of expenditure.

For more ideas on how to report to beneficiaries and information about Mango's "Who Counts?" campaign, please visit: **www.whocounts.org**.



Summary: Twenty Questions

Here are 20 questions to ask when reviewing financial information:

Auditors Report on the Annual Financial Statements

1. How long ago was the last audit conducted?
2. What does the Auditor's Opinion say – is it qualified or unqualified?

Balance Sheet

3. Does the organisation have enough ready cash (see 'Cash at Bank' listed under Current Assets) to pay off its immediate debts (see Creditors)?
4. How long could the organisation survive if all of its funding dried up? (Calculate the 'survival ratio') How does this compare to last year?

Income & Expenditure (or Profit and Loss) Account

5. Is income and expenditure broadly in balance? (Look for net income/expenditure)
6. Is there a significant increase or decrease in activity levels from the previous year?
7. What is the balance of direct project costs vs. admin costs? Is it reasonable for the size and nature of the organisation?
8. How 'donor dependent' is the organisation? (Calculate the 'donor dependency ratio')

Budget Monitoring Report

9. Is expenditure broadly in line with the budget? (+ 10%)
10. Is income broadly in line with the budget?
11. Are there any significant variances? If so, have they been satisfactorily explained?
12. What action is being taken to correct significant variances – eg under-spending as a result of delayed activity plans?
13. Are there any large bills outstanding which could substantially affect the figures shown?
14. Are we owed any large sums of money? What is being done to retrieve them?
15. Are there any un-budgeted expenses which may occur in the rest of the year?
16. What is the projected end-year outcome? Is this outcome satisfactory? If not, what steps can be taken to change the result?

Cashflow forecast

17. Is there enough cash in the bank to fulfil the activity plan in the next six months?
18. What grants are due and are they still expected to come through on time?
19. Are spare cash balances invested to produce the best return?

General

20. What non-financial figures are being produced to show how the programme of activities is progressing?

Chapter

6

Safeguarding Your Assets

'It is more sensible to establish a system to deter fraud rather than one to discover it'.'

This chapter:

- Explains the importance of introducing internal controls
- Outlines the principles of delegation of authority and separation of duties
- Highlights the importance of cash control and reconciliation
- Discusses ways to manage and control fixed assets
- Provides some tips on how to detect fraud
- Gives advice on how to manage incidences of fraud and other irregularities

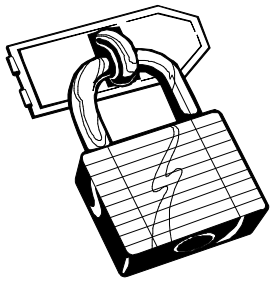
Managing Internal Risk

Here we are concerned with managing internal risks facing an NGO on a day-to-day basis. This is achieved with a series of controls, checks and balances, which, if operated properly, will avoid losses and detect errors and omissions in the accounting records.

Controls are also very important in protecting all those who handle the financial affairs of the organisation as they remove any suspicion of, or temptation to, dishonesty.

There are several different categories of internal controls:

- Delegated Authority
- Separation of Duties
- Reconciliation
- Cash Control
- Physical Control



Delegated Authority

The Board of Trustees delegates authority through the Chief Executive for the day-to-day running of the organisation. In a large and busy organisation it is not practical to expect one person to make all the decisions and authorise all transactions. The Chief Executive will, therefore, further delegate authority to members of the staff team to relieve the load and to ensure smooth operation during absences of key staff.

■ Delegated Authority Document

Every organisation should decide in advance who should do what in finance procedures. It is good practice to record what has been decided in a **Delegated Authority document**; its purpose is to clarify who has the authority to make decisions, commit expenditure and sign legal undertakings on behalf of the organisation so that there is no confusion about responsibility. [See an example in Appendix 2.]

The Delegated Authority Document should include instructions for such duties as:

- Placing and authorising orders for goods and services
- Signing cheques
- Authorising staff expenses
- Handling incoming cash and cheques
- Access to the safe and petty cash
- Checking and authorising accounting records
- Signing legal undertakings

The Delegated Authority document must be approved by the governing body and should be reviewed every year to ensure it is still appropriate to current needs. It should also outline deputising arrangements to cover for absence of key personnel. A breach of delegated authority is a serious matter and should be dealt with accordingly.

■ Authorisation rules

When writing a delegated authority document there are some basic rules which should be observed:

- **The lowest level of authority is defined** – it is taken for granted that those higher up the management ladder will also have the same authority.
- No one should authorise any transaction from which they will personally benefit. This makes the individual vulnerable to accusations of abuse.
- **Sub-ordinates must not authorise payments to managers** – they must be passed to someone who is more senior in the management structure.

Any limits or conditions that apply to delegated authority must be clearly defined. For example, a person may be authorised to commit expenditure up to a specified amount or within certain categories of expenditure or within budget.

Separation of Duties

In order to protect those operating the procedures and to prevent any temptation to mis-use funds, there must be a separation of the various duties within the finance procedures.

For example, the duties of ordering goods, receiving goods, authorising the payment, keeping the accounting records and reconciling the accounts should not fall entirely on the shoulders of one person. Apart from weakening financial control, this puts too much responsibility on one person and if they should leave the organisation or are absent for long periods, then the finances will grind to a halt.

As far as possible then, duties should be shared between the staff team and/or committee if there are only one or two staff members.

■ Procurement Procedure

A Procurement Procedure sets out the steps and conditions that have to be followed by staff to acquire goods and services so that the objectives of the organisation can be fulfilled efficiently and effectively. See below for the typical stages in a procurement process.

This is a prime example of separation of duties in action. The procedure will:

- outline the process and authorities for ordering, receiving and paying for goods and services (see below);
- describe which method of payment or acquisition is to be used for different goods and services – for example, when it is acceptable to use petty cash (this should be rare), bank transfers (eg salaries) or suppliers' accounts (eg stationery, petrol);
- clarify when it is necessary to obtain quotations from suppliers – eg 2 quotations for all expenditure over $100;
- include a list of Approved Contractors or Suppliers, if used.

■ Signing cheques

Each organisation should have a panel of cheque signatories from which to select the required number of authorising signatures; there should be sufficient people nominated to ensure efficient administration of payments. Signatories should be regularly reviewed and the list updated when people leave the organisation.

It is usual to have more than one signature on a cheque to help avoid fraud.

> *NEVER ask signatories to sign blank cheques for future use as this defeats the whole purpose of having more than one signatory.*

■ Checking and authorising accounting records

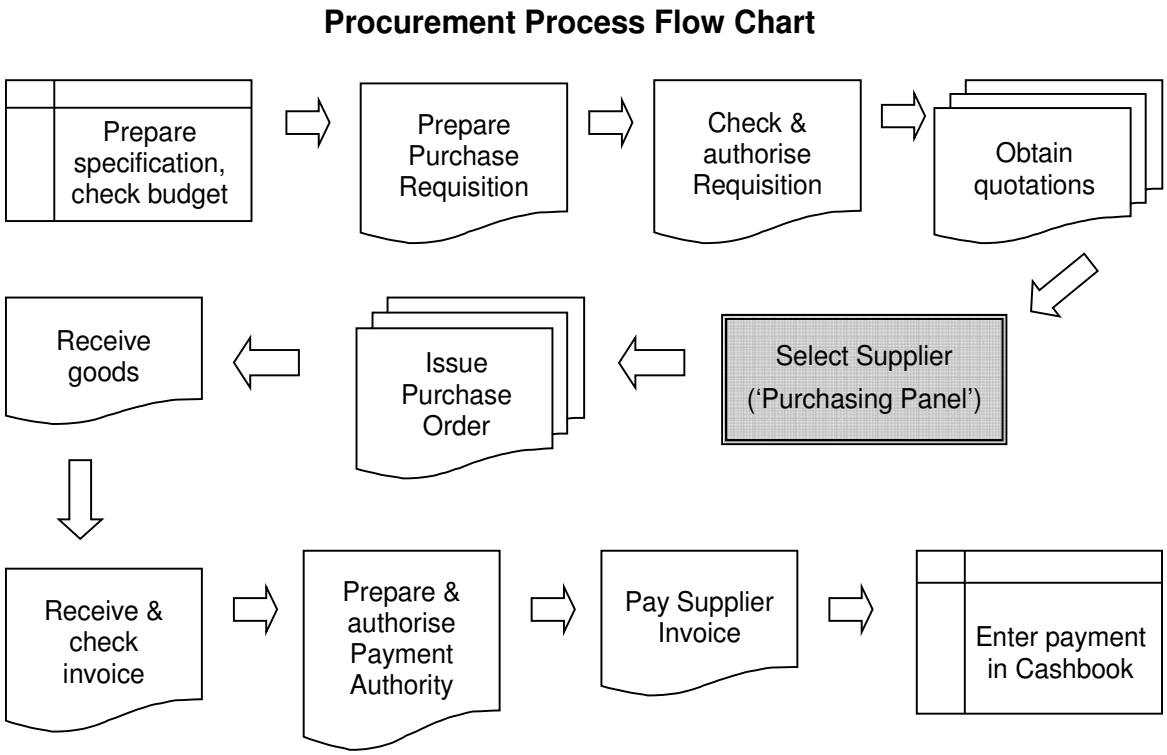
A key responsibility of managers (the Chief Executive or Financial Controller in a larger organisation or a Treasurer in a smaller one) is to check and authorise records, count the petty cash and review orders for supplies, from time to time.

The Procurement Process

Each organisation must design a procurement procedure which suits its own circumstances. **Figure 6.1** shows some typical stages in the process to demonstrate separation of duties in action.

Note that the procurement stages described here are for major orders not small cash purchases.

Figure 6.1 Typical Procurement Process



1. Specify goods or services to be purchased, check budget

The standard, quantity and price of goods or services required, as described in the activity plans, is clarified so that it is clear what needs to be purchased. The amount currently available in the budget for the item to be purchased should be checked at the specification stage in case the price has changed since the budget was prepared.

2. Prepare Purchase Requisition

An internal request is prepared – usually on a standard form for that purpose – to formally request the purchase of the goods or services specified. The request will include a description of the purchase and state why it is required.

3. Authorise Purchase Requisition

The purchase requisition will usually be checked and authorised by the budget holder or other nominated person to verify that there is a genuine reason for the purchase. The available budget will usually be checked again at this stage.

4. Obtain Quotations

Quotations from reputable independent suppliers are requested (in accordance with internal procedures and donor rules) to make sure the organisation gets best value for money and to minimise the risk of collusion.

5. Select Supplier

Quotations are reviewed and a supplier is selected based on price, quality, delivery times and 'after sales' terms to ensure value for money. For larger purchases, it is usual to have a Purchasing Panel – a small group of managers who take responsibility for selecting the supplier.

6. Issue Purchase Order (PO)

A Purchase Order is sent to the selected supplier with a copy kept on file with the supplier's quotation. This is a legally binding contract.

7. Receive Goods from Supplier

When supplies are delivered and received, a Goods Received Note (GRN) is usually signed to confirm receipt and a copy filed for later reference.

8. Receive and Check Supplier Invoice

The invoice should be checked and matched up with the GRN, PO and quotation, usually by the finance team.

9. Prepare and Authorise Payment Authority

The Payment Authority is attached to the invoice and all the supporting documents. It includes budget and accounting codes and must be checked and authorised by the budget holder or other nominated person.

10. Pay Supplier Invoice

Payment should be made to the supplier within the specified payment terms, usually 30 days.

11. Enter Payment into Cashbook

The final stage is to record the payment in the organisation's books of account.

The Reconciliation Process

Reconciliation involves verifying accounting records to make sure that there are no errors or omissions that have so far gone undetected. Records that should be reconciled at regular intervals are:

- Bank Book
- Petty Cash Book
- Stock control records
- Salaries and Deductions schedules

Once the records have been successfully reconciled, the reconciliation statement must be passed on to be independently checked with the source records by a line manager or a committee member. As noted above, this checking duty is a key responsibility of the manager or Treasurer.

■ Bank Book

The Bank Book should be reconciled to the bank statement at least once a month. The purpose of this exercise is to make sure that the organisation's own records agree with the bank's records which are rather like a parallel set of records. This is achieved by taking the closing bank statement balance for a particular date and comparing it to the closing Bank Book balance for the same date, then explaining the differences.

This is an important check not only for accuracy and completeness of records, but also as an early indication of fraud.

■ Petty Cash Book

The petty cash should be counted and reconciled at least weekly. If the imprest system is in use, this is a very easy operation as it is simply a matter of counting up all the payments made since the last reimbursement and counting the cash in the tin. The two totals together make up the total float. If a discrepancy is found, it must be noted in the petty cash book as either an 'expense – unidentified' or a 'surplus – unidentified' and allocated to an appropriate category. Discrepancies must be reported to a manager.

■ Stock records

Stock records must be checked against the supplies held in the store and receipts from sales to ensure that no errors have crept in (and no stock has crept out).

A **Sample Stock Control Sheet** for some T-shirts is reproduced below in **Table 6.1**. It shows the value of the stock the last time it was reconciled. Then it lists new stock purchases and new sales. This gives us an *expected* stock value, on paper at least.

Note that the table lists both the cost value (ie what the organisation paid the T-shirts supplier) and the resale value (ie what the organisation expects to sell the T-shirts for).

However, when the T-shirts in the stock room are physically counted and checked, the actual value is less than expected. (The brackets around the bottom line figures indicate the stock value is short.)

What do you think might explain this difference?

Table 6.1 Sample Stock Control Sheet

	Cost Value $	Resale value $
Value of stock at 1 Jan 200x	3,000.00	6,000.00
Add: Value of purchases between the period 1 Jan. to 31 Mar. 200x	800.00	1,600.00
Deduct: Value of sales during the period	1,300.00	2,600.00
EXPECTED STOCK VALUE:	2,500.00	5,000.00
ACTUAL STOCK VALUE	2,450.00	4,900.00
Difference	**(50.00)**	**(100.00)**

This difference might be caused by one of several things:

- **The value of new purchases could be wrong** – eg the stock delivered was short. This could happen if a delivery is not properly checked against the delivery note and invoice when received from the supplier.
- **The value of sales could be wrong** – eg the wrong amount could have been charged or a sale not recorded or coded properly.
- Stock could have been stolen.
- **Stock could have been given out** as gifts or for publicity purposes and not recorded as such in the accounts.

Whatever the explanation, the difference would have to be investigated and systems reviewed if necessary. This demonstrates well the importance of regular stock reconciliation.

■ Wages Book

The wages records, and particularly deduction records, are notorious for containing inaccuracies and for abuse in the form of 'ghost employees' (ie people on the payroll who do not exist and where a salary is paid and collected by a fraudster).

Wages records must be reconciled every month to ensure that the correct deductions are being made and passed on to the relevant authority. Failure to do so could result in severe penalties and interest being imposed – and cause discontent amongst the staff.

Cash Control

It is important to observe the **Seven Golden Rules for Handling Cash** as follows:

1. Keep money coming in separate from money going out

Never put cash received into the petty cash tin, it will lead to error and confusion in the accounting records. All money coming into the organisation must be paid into the bank promptly and entered into the records before it is paid out again. Failure to do so will distort financial information.

For example, a training course is run by an organisation and a charge of $25.00 is made to each of the 10 participants. The cost of food and room hire is $150.00 and this is paid from the course fees received on the day. The balance of fees – $100.00 – is paid into the bank as Training Fees.

Why is this a problem? The cost of providing food and room hire has not been entered into the accounts and cannot therefore be reflected in a financial report. Similarly, as only the net amount of fees received has been paid into the bank, it would appear that only a few people actually attended the course and the income generating potential of running such a course has been disguised.

2. Always give receipts for money received

This affords protection to the person receiving the money and assures the person handing it over that it is being properly accounted for. Receipts must be written in ink, not pencil, and preferably from a numbered receipt book.

3. Always obtain receipts for money paid out

Sometimes this may not be possible. For example, when purchasing materials from a market; in this case the cost of each transaction should be noted down straight away so that the amounts are not forgotten and these can then be transferred to a petty cash slip and authorised by a line manager. Remember – no receipt means there is no proof that the purchase was made.

4. Pay surplus cash into the bank

Having cash lying around in the office is a temptation to a thief and the money would be better managed if it were earning interest in a bank account. A casual approach to cash on the premises might also lead to people wanting to 'borrow' from it – many a sorry tale of fraud has started in this way. Every attempt should be made to pay cash into the bank on a daily basis or, at the very least, within 3 days of receipt.

5. Have properly laid down procedures for receiving cash

To protect those handling money, there should always be two people present when opening cash collection boxes, etc. Both should count the cash and sign the receipt.

6. Restrict access to petty cash and the safe

Keys to the petty cash box and the safe should be given only to authorised individuals. This should be recorded in the organisation's Delegated Authority document.

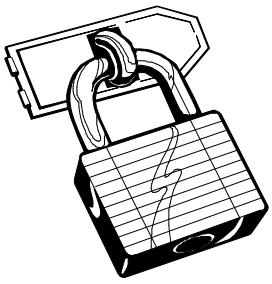
7. Keep cash transactions to an absolute minimum

Petty cash should only be used to make payments when all other methods are inappropriate. Wherever possible, suppliers' accounts should be set up and invoices paid by cheque. The advantage of paying for most transactions by cheque is that this has the effect of producing a parallel set of accounts in the form of the bank statement. Also, it ensures that only authorised people make payments and it reduces the likelihood of theft or fraud.

Physical Controls

Physical controls are additional common sense precautions taken to safeguard the assets of an organisation.

■ Having a safe



Having a safe – or a safe place – to keep cash, cheques books, legal documents, etc. is an important consideration. A proper safe is worth considering especially if your organisation has to keep large sums of money on the premises overnight. Safes are however, expensive and if resources are tight then it may be better to improve on banking procedures.

■ Insurance cover

It is the responsibility of the Chief Executive to ensure that there is adequate insurance cover so that if 'assets' are lost, damaged or stolen they can be replaced or compensated. There are many different types of insurance to consider, including

- Office contents against fire and theft
- Buildings against fire, floor and storm damage
- Vehicles against accident and theft.

The decision whether or not to insure property is a good example of managing risk – weighing up the pros and cons of paying for insurance is a common dilemma for managers.

■ Safeguarding Fixed Assets

Fixed assets may represent considerable wealth held in the form of land, buildings, vehicles, machinery and office equipment and, often over-looked, require special attention to ensure their value is maintained and that they do not disappear through lack of vigilance.

The measures to safeguard these assets will include Assets Registers, a vehicle policy and maintenance policies for equipment.

The Assets Register

An *Assets Register* should be established with an entry or record sheet for each item. Each asset should be tagged with a unique reference number for identification purposes. The register will record important information about each asset, such as:

- where and when the item was purchased and how much it cost
- where it is held or located
- how much it is insured for
- repair history
- serial numbers
- details of guarantees or warranties.
- depreciation rate and method, where relevant.

The record sheet should also state who is responsible for its maintenance and security. The Assets Register should be checked by a senior manager or committee member every quarter and any discrepancies reported and appropriate action taken. See Appendix 19 (page A21) for a sample Assets Register record sheet.

Building and Equipment Maintenance policy

To preserve the value of buildings and equipment, an organisation must have a pro-active policy of maintenance. For buildings this may require a professional planned maintenance contract for which a realistic budget must be provided.

Office equipment such as photocopiers and electrical equipment should also receive regular services by qualified technicians to ensure they are safe and operating properly.

Vehicle policy

Every organisation that owns vehicles should have a vehicle policy. This will set down the policy on a range of issues such as:

- Depreciation
- Insurance
- Purchasing, replacement and disposal
- Maintenance and repair
- Private use of vehicles by staff
- What to do when accidents happen
- Driver qualifications and training
- Carrying of passengers

The costs of repair and replacement must be also adequately reflected in the budget process.

For each vehicle there should be a log of journeys so that the running costs per KM can be assessed and private use closely monitored. (See Appendix 19, page A24 for a sample.) Once you have 12 months information on the costs of running a vehicle, it is possible to calculate its average running costs per kilometre.

See below for a worked example.

Table 6.2: Calculating Vehicle Running Costs

Vehicle make/model:	Toyota Hiace Van	
Date purchased:	26 December 2007	
Purchase price:	$20,000	
Depreciation period /method:	5 years, straight line method	
Maintenance:	Service every 6,000 km or every 3 months	
KM run	*From 1 January to 31 December 2008:* Km on clock on 31/12/08 LESS Km on clock on 01/01/08 Total KM run during year:	 20,601 (201) 20,400
1. Depreciation		$
Purchase Price	= $20,000	
Depreciation period	= 5 years	
Annual depreciation charge	= $20,000 / 5	4,000
2. Fuel consumption		
Total fuel bills for the year		5,500
3. Maintenance costs		
Total of invoices for the year for: repairs, service costs, spare parts, tyres, etc		900
4. Insurance and tax		
Insurance, road tax for the year		3,300
TOTAL VEHICLE RUNNING COSTS:		**13,700**
Cost per Km calculation: Total costs for the year Total no. of Km run	 = $13,700 20,400 km	 $0.67

In conclusion: using the information from our accounts and the vehicle log sheet, we can see that each kilometre run with the Toyota Hiace Van cost approx. 0.67 cents.

Top Tips on the Warning Signs of Fraud

***Remember**: "Prevention is better than cure!"*

The following ideas may be an early indication of fraud or abuse. Use with care!

From the accounting records:

- Lots of corrections to the manual cashbook – this may include extensive use of white-out or blocked out figures
- Pristine records – ie a manual cashbook that look as if they have all been written on the same day in the same hand. Could be an indication of rewritten/duplicate books
- Delayed banking of cash received – shown up by bank reconciliation. Could be 'teeming and lading'?
- Records not being kept up to date – ie deliberately delayed so managers cannot detect false accounting going on.
- Missing supporting documents – eg certain bank statements destroyed to cover someone's tracks, or a project officer who regularly claims to have 'lost' receipts.
- Debtors rising unexpectedly – eg if debtors have paid but the cash is being pocketed. This may occur if there are poor controls in issuing receipt books as someone could take an unused book and issue valid receipts without them ever being entered into the accounting records.
- Hand written supporting documents with errors and corrections on them. Indicates possible changes made after the goods or services were purchased.
- Cash counts not reconciling to the accounts but reconciling at the next cash count – possible borrowing of funds by the safe key holder.

Reports:

- Budget monitoring reports showing inconsistent behaviour between line items - eg project-related expenditure is under-spent due to delays – except for fuel which his over-spent. This could indicate abuse of the vehicle.
- Vehicle log books not maintained in an appropriate level of detail. This could indicate abuse of the vehicle.
- Budget monitoring reports delayed – to cover up something?

Non-financial areas:

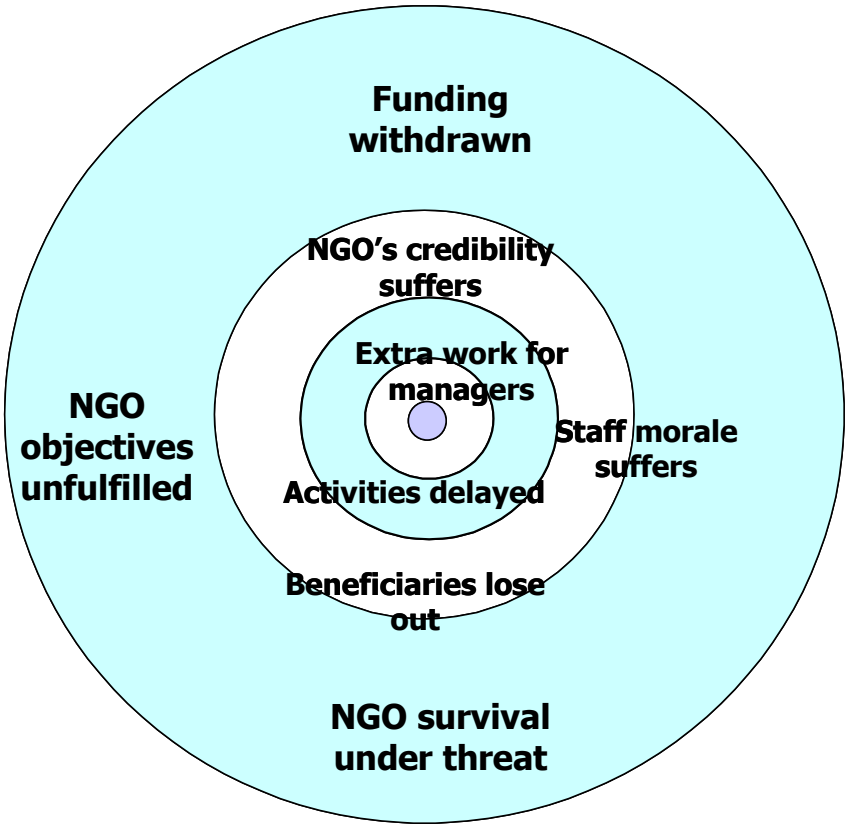
- Working very long hours – first in last out of the office? Could mean that they are having to do extra work to cover tracks?
- Never taking holidays – can't afford for someone else to see what they are doing!

- Change of lifestyle – spending patterns don't match their income (eg designer clothes, social habits, expensive car…)
- Creating 'smoke screens' – where someone is making a false accusation about another team member to give them time to cover their tracks or make a getaway!

And some Ideas on fraud prevention:

- Make sure you have robust internal control systems in place.
- Visit projects, and see if the activities carried out roughly match the expenditure.
- Share financial reports with beneficiaries, and ask if they think they have had value for money (find out how: **www.whocounts.org**).
- Hold regular meetings with other staff at all levels (eg project and administrative staff, board members, etc) to discuss financial reports, making budgets and reports openly available.
- Help non-finance staff and managers improve their financial skills, for instance by reading Mango's Guide to Financial Management (available on the CD-Rom in your training pack.)

Figure 6.2: The Ripple Effect of Fraud



Dealing with Fraud and Irregularities

There will be occasions when internal control systems fail to prevent losses through theft, fraud or other irregularities.

Fraud is defined as: *a deliberate, improper action which leads to financial loss to the organisation*. This includes theft of goods or property; falsifying expenses claims; and falsification (or destruction) of records to conceal an improper action.

Fraud does not include:

- accounting errors
- actions condoned by established practice
- cases where no loss is incurred.

'Irregularities' include unauthorised activities for private gain: eg 'borrowing' from petty cash; use of vehicles; or abuse of telephones and other equipment.

Inevitably, the impact of fraud has a damaging effect on the organisation. Imagine a stone falling into a pond: the initial splash is the loss of funds or equipment but it does not stop there, as **Figure 6.1** above illustrates.

Incidents of fraud and irregularities require sensitive handling to minimise the long-term impact. It is important to be prepared to deal with any occurrences of fraud or financial irregularity by having a written procedure which covers steps that need to be taken.

■ Deterrence

The procedure should state clearly that routine controls, checks and balances are in place to safeguard the assets of the organisation and to protect staff from any suspicion of, or temptation to, fraud or other impropriety. Paid staff and volunteers are therefore obliged to co-operate fully with internal control procedures and failure to do so will be dealt with as appropriate within the organisation's disciplinary code.

■ Types of irregularity

The procedure will identify different types of irregularity; how seriously they are viewed; and how they will be dealt with. For example, all instances of theft and fraud will be viewed as Gross Misconduct and will result in immediate dismissal and loss of terminal benefits. A clear statement of the organisation's policy on the circumstances in which the Police will be informed must also be made. This must take in account local circumstances.

■ Detection

A procedure for reporting suspicions of irregularities should be made clear to all. This should make it easy for people to report concerns in confidence and without fear of retribution.

When an irregularity is reported or detected, record the details in writing; report it immediately to a superior. Follow up all reports or suspicions immediately; do not allow rumours to spread or let the 'trail' go cold.

Investigation

When an irregularity comes to light, it must be dealt with quickly and sensitively; look for corroboratory evidence before instigating a formal investigation. If all the evidence points to an irregularity, the individual(s) involved should be formally interviewed with a third person present to take notes.

Protect documents and records by either removing access to them by those involved in the irregularity or by suspending the people involved during the investigation. The policy will identify who is responsible for conducting a formal investigation. This will depend on the nature of the irregularity; it could be conducted by the senior manager, the internal auditor, the external auditor or, in more serious cases, the Police.

The Aftermath

Don't under-estimate the long-term and less tangible impacts of fraud. It will involve a lot of a managers' time during the investigation and afterwards. In particular:

- People will be distressed by the experience and need to be supported. Colleagues will suffer all the mixed emotions of bereavement: anger, guilt, disappointment and loss. They will be worried that their own jobs are under threat.
- New staff may need to be recruited and trained.
- Donors will need reassuring that their resources are safe and the project will not suffer.

Summary

Here are some tips on how to deal with fraud and other irregularities – to keep **RISKS LOW**:

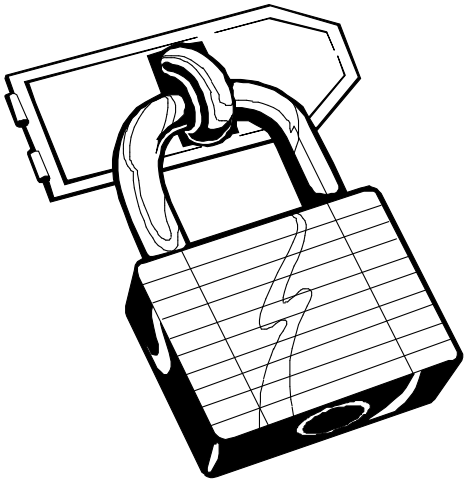
DO

- **R**eport the incident to a superior or Board member
- **I**nvestigate incidences, gather the facts
- **S**ecure the assets and records
- **K**eep calm!
- **S**wiftly act

DON'T

- **L**ook the other way
- **O**verlook the 'fall out' of a fraud
- **W**ithhold information to protect others

Above all, remember that prevention is better than cure!



Chapter 7

Managing Audit

An Independent Check on Accounting Records and Systems

This chapter:

- Explains what an audit is
- Describes the different types of audit
- Provides an overview of the audit report
- Gives advice on how to prepare for and manage the external audit

What is an Audit?

An audit is an **independent** examination of records, procedures and activities of an organisation, resulting in a report on the findings.

There are two kinds of audit:

- ✓ The Internal Audit
- ✓ The External Audit

As the name implies, an external audit is primarily for the benefit of those outside the organisation, eg stakeholders and funders. Internal audit is undertaken for the benefit of those inside the organisation, ie trustees and management.

The audit should be a positive experience and not one to be feared; it is an opportunity to receive feedback on strengths and weaknesses in systems. Use your auditor to discuss ways of improving your accounting systems and procedures.

■ Why do NGOs need audit?

Audits are important for NGOs as they demonstrate a commitment to transparency and accountability and bring credibility to the NGO. It is also a legal requirement in most countries to have the financial statements reviewed by an independent auditor once a year.

Internal Audit

Internal audit involves a structured review of systems and procedures, as set by the Board and managers, to ensure efficient and effective practices. It is not an internal 'policing' function, rather an opportunity to improve systems and build internal capacity.

The internal auditor's report will highlight findings and make recommendations for action, where needed. It may be carried out by someone within the organisation, or an outsider may be engaged to carry out an 'internal audit'.

An internal audit will include a range of checks as part of the independent review, including:

- financial accounting systems and procedures;
- management accounting systems and procedures;
- internal control mechanisms.

The internal auditor reviews the adequacy of the design of the systems of procedures, and checks that they are being appropriately implemented. A report is presented to the governing body and management, who respond by taking corrective action, perhaps changing a procedure, or training a staff member.

The 'Three E's' influence an internal auditor's approach:

- **Economy:** paying no more than necessary for the resources needed.
- **Efficiency:** getting the greatest benefit with the fewest resources.
- **Effectiveness:** how successful we are at meeting objectives or 'doing the right thing'.

External Audit

An external audit is an independent examination of the financial statements prepared by the organisation. It is usually conducted for statutory purposes (because the law requires it). External auditors may also be engaged to do other specific assignments, (eg a fraud investigation).

Purpose

The purpose of external audit is to verify that the annual accounts provide a true and fair picture of the organisation's finances; and that the use of funds is in accordance with the aims and objects as outlined in the constitution.

The purpose of an external audit is NOT:

- To act as a fraud investigation
- To prepare the accounts
- To provide a certificate to say "there are no problems"
- Proof that internal control systems are effective
- Evidence that accounts are 100% error free

Although it is not the prime role of the audit to detect fraud, this may of course come to light during the checks that take place. Auditors have thus been described as 'watchdogs not bloodhounds'.

■ Appointment

An external audit can be conducted either as part of the annual review of accounts or as a special review by a donor agency. It is conducted by a firm of accountants with recognised professional qualifications.

Auditors are appointed by the Board of Trustees (or Annual General Meeting) or by a donor for a special audit. They are independent of the organisation employing them. Being independent means that the auditor must not have been involved in keeping the accounting records and is not personally connected in any way with the organisation being audited.

■ What is involved?

Auditors only have a limited time in which to complete their work, so they concentrate on testing the validity of a sample of transactions and results rather than vigorously checking everything. Although an auditor's independence must be respected and observed at all times, they are nonetheless providing a service for a fee – you have a right to expect value for money.

Auditor-speak de-mystified:

Material: An item is said to be 'material' if it is considered to be significant to the users of the financial statements.

Test basis: A representative sample, the rest of the transactions are assumed to be similar to the sample tested

■ The audit report

An audit results in a report addressed to members which gives an 'audit opinion' as to the 'true and fair' view given by the financial statements (of the state of affairs of the organisation and operations for the period.)

Auditor-speak de-mystified:

'**True'** means that the transaction did take place and that an asset exists.

'**Fair'** means that a transaction is fairly valued and that assets and liabilities are fairly stated.

If the auditors do not agree with the financial results as presented by the organisation, they may issue a report saying that, in their opinion, the accounts are not fine. This could be disastrous for an NGO seeking donor support.

The table below summarises the types of opinion.

Table 7.1: The status of the External Auditor's Opinion

Auditor Opinion	Comment
Unqualified	The accounts do give a true and fair view – 'clean' audit report.
Qualified: Subject to	The accounts are basically OK, apart from specific identified issues, eg an incorrect accounting policy, or specific unsupported expenditure.
Qualified: Disagreement	There are so many errors that the accounts do not give a true and fair view.
Qualified – disclaimer	The auditors are unable to give an opinion, because the records are so poor or incomplete. This is very bad indeed.

If the auditors propose any adjustments or changes to the draft financial statements, these must also be approved by the Board. The audit report is addressed to the members and it is usual to formally accept the report at the Annual General Meeting.

Auditors will also often provide a **Management Letter**. This is separate to the audit report and is addressed to management. The report highlights weaknesses identified in the internal control systems and makes recommendations for improvements. Managers have an opportunity to respond to the findings outlined in the management letter and explain what action they will take.

■ Project (or Donor) Audit

On occasion, donor agencies may request an independent external audit of records and activities and will appoint a qualified person to undertake a review. The primary purpose of such a review is to check that grants are being used as intended and in accordance with the budget in the original funding agreement.

The auditor or evaluator will almost certainly wish to interview staff and committee members and may even request to observe the organisation in pursuance of its activities. Every co-operation should be given during such visits and an effort made to be open and honest about organisational strengths and weaknesses.

Summary: Different Types of Audit

Area:	*Internal*	*External*	*Project*
Main purpose	Check effectiveness of systems & procedures	Verify the published accounts give a 'true & fair' view	Check that funds used in accordance with the funding agreement.
Focus of review (starting point)	Systems and Procedures manual	Financial statements & underlying records	Grant agreement
Appointed by	Management (but have direct line to the board)	Board (or members)	Donor, but may use normal external auditor if on approved list
Scope	As per planned schedule based on risk assessment. May be for a specific department, grant or period.	All financial transactions in the accounts, whole organisation	Usually limited to the project and related grant funding.
Report includes	Findings and recommendations for improvements	Auditor's opinion and Management letter	Usually, auditor's opinion(s) and recommendations
Employed by	The NGO or external body (outsourced)	External body	External body (sometimes donor themselves)
Qualifications	No formal requirement	Must be qualified & registered accountant	Usually qualified & registered accountant

What Does the Auditor Need?

An auditor will need a quiet place to work where the checks can take place without interruption. If individual staff members are to be interviewed, then a private room where confidential discussions can take place will also be required. Depending on the type of audit taking place, the auditor will usually give advance notification of the records needed.

Ensure that all the records are up-to-date and properly filed as this will facilitate the routine checks and cause minimal disruption for the organisation. This will also help to save on audit fees. A checklist of records and other documentation which might be requested by the auditor follows over page.

■ An Auditor's Checklist

Group of Records	Description of item
A Primary records of account:	❑ Cash Books completely up to date to the year-end ❑ File of invoices/vouchers for all items of expenditure ❑ File or book of receipts for moneys received ❑ Bank statements, paying in slips and cheque books ❑ Wages book and records ❑ General Ledger, if kept
B Summaries and reconciliation statements:	❑ A Trial Balance and/or a summary of all receipts and payments by budget category ❑ Bank reconciliation statements for all bank accounts at the year-end cut-off date ❑ Petty cash reconciliation statement to the year-end cut-off date ❑ Stock sheets
C Schedules:	❑ Schedule of Creditors (money owed by the organisation) ❑ Schedule of Debtors (money owing to the organisation) ❑ Schedule of Grants Due ❑ Schedule of Grants Received in Advance ❑ Fixed Assets Register
D Other information:	❑ A letter from bankers to confirm balances [this will be requested by the auditors themselves] ❑ Constitution of the organisation ❑ List of Committee members and staff ❑ Minutes of Board and management meetings ❑ Donor agencies funding agreements and audit requirements

Acknowledgement: Grateful thanks to Samantha Musoke, ACA, of ACLAIM Africa, Uganda, for her input to this chapter.

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APPENDICES

Appendix 1: Chart Of Accounts – Milestone Project

Account Description	Category Code	Comments
INCOME: DONOR		
- DFID	1010	*For grants received from this donor*
- Smile Trust	1020	*For grants received from this donor*
- Vanguard Society	1030	*For grants received from this donor*
INCOME: GENERAL		
- Bank Interest	1110	*Interest received on bank accounts*
- Donations & fund-raising	1120	*Fund-raising activities, miscellaneous donations*
- Sales	1130	*Sales of trainees' work*
- Training fees	1140	*Course participants' contributions*
EXPENDITURE: ADMINISTRATION		
- Audit/accountancy	3010	*Audit fees, other accountancy expenses*
- Bank charges	3020	*Service fees, interest charged on OD balances*
- Board meetings	3030	*Room hire, refreshments, AGM expenses*
- Depreciation	3040	*Cost of depreciation of fixed assets*
- Postage & stationery	3050	*Postage, office and photocopier consumables*
- Publicity	3060	*Posters, leaflets, advertising training courses*
- Rent, insurance & utilities	3070	*Office rent, insurance and utilities*
- Repairs & renewals	3080	*Servicing, small items of equipment, office repairs*
- Telephones/fax	3090	*Telephone accounts, not repairs*
EXPENDITURE: PERSONNEL		
- In-service training	4010	*Course fees, meals & accommodation*
- Recruitment	4020	*Recruitment advertising costs, interview expenses*
- Salaries & benefits	4030	*Gross salaries, housing, medical aid and pensions*
- Travel & subsistence	4040	*Per diem, meal and overnight allowances, bus fares*
EXPENDITURE: VEHICLE RUNNING		
- Fuel	5010	*Petrol, diesel and oil costs*
- Vehicle insurance/tax	5020	*Vehicle Insurance premiums and road tax*
- Vehicle maintenance	5030	*Service, repairs, tyres, spare parts, car wash*
EXPENDITURE: TRAINING		
- Fees & honoraria	6010	*Guest speakers' & external trainers' fees/expenses*
- Food & accommodation	6020	*Room hire, food for trainees*
- Training materials	6030	*Tools, protective clothing, papers, pens, metal, concrete, etc*

FIXED ASSETS:		
- Office Equipment	0110	*Computers, printers, desks, chairs, etc.*
- Project Equipment	0120	*Large tools and training equipment*
- Vehicles	0130	*Cars, mobile workshop*
CURRENT ASSETS:		
- Bank Deposit Account	0210	*High interest call account*
- Bank Current Account	0220	*Cheque account*
- Petty Cash	0230	*For adjustments to the petty cash Imprest float*
- Debtors & prepayments	0240	*Money owed to us and prepaid amounts*
- Advances	0245	*Staff loans and working advances*
- Grants receivable	0250	*Grants due for this year from donors*
- Stocks	0260	*Stocks of raw materials*
LIABILITIES:		
- Creditors & accruals	0510	*Money owed by us and accrued expenses*
- Grants In advance	0520	*Designated donor funds received for this year and not yet spent*
- Reserves	0530	*Funds designated for use in future years*

PROJECT COST CENTRES

Description	**Code**	**Comments**
- Co-ordination	01	*Transactions to be allocated to the Co-ordinator's Department*
- Building Department.	02	*Transactions to be allocated to the Building Trades Department*
- Metalwork Dept.	03	*Transactions to be allocated to the Metalwork Department as a whole*
- Metalwork: Furniture Project	03-01	*Transactions to be allocated to the Furniture section of the Metalwork Department only*
- Metalwork: Vehicles Project	03-02	*Transactions to be allocated to the Vehicle section of the Metalwork Department only*

Appendix 2: Sample Delegated Authority Document

AREA OF AUTHORITY:	LIMITS APPLIED:	DESIGNATED PERSONS:
▪ *Legal documents (where not covered below)*		Any two from: Ch, Tr, Se, CE.
▪ *Leases on property and equipment*	Up to $25,000 Over $25,000	Any one from: Ch, Tr, Se, CE. Any two from: Ch, Tr, Se, CE.
▪ *Current Account Cheques*	up to $2,000 Over $2,000	Any two from: Ch, Tr, Se, CE, one other designated BM Any two from: Ch, Tr, Se, one other designated BM.
▪ *Bank Account Transfers*	Up to $25,000 Over $25,000	Any two from: Ch, Tr, Se, CE, one other designated BM Any two from: Ch, Tr, Se, one other designated BM.
▪ *Staff advances/loans*	Max. $2,000	CE (or in case of CE, Ch or Tr)
▪ *Staff expenses*		LM for all staff below CE level Ch or Tr for CE
▪ *Board Member expenses*		Ch or Tr
▪ *Orders for Goods & Services*	Up to $1,000 Up to $5,000 Up to $25,000 Up to $50,000 Over $50,000	SO, providing within budget OM, providing within budget CE, providing within budget Ch or Tr, providing within budget Any 2 BM and minuted by full Board Meeting.
▪ *Petty Cash expenditure*	Up to $50 (single transaction) Over $50	AO FC
▪ *Safe Keys*		FC and Tr
▪ *Receipt of cash & cheques*		AO
▪ *Banking of cash & cheques*		AC
▪ *Annual / sick leave*		LM
▪ *Maternity / Paternity Leave*		CE (or in case of CE, Ch or Tr)
▪ *Contracts of Employment*	All staff	Ch, Tr or S

KEY: Ch = Chairperson; Tr = Treasurer; S = Secretary; BM = Board Member
CE = Chief Executive; OM = Operations Manager; FC = Financial Controller;
AO; Accounts Officer; AC = Accounts Clerk; SO = Senior Officer; LM = Line Manager.

Appendix 3: Bank Book – Receipts Page

MILESTONE PROJECT – January 2009

1	2	3	4	5	6	7	8	9	10	11
					ANALYSIS OF RECEIPTS CATEGORY					
Date	Details of transaction	Recpt. No.	Cost Centre	Total UC	Grant DFID 1010	Grant SMILE 1020	Donations & fundr'g 1120	Sales 1130	Training Fees 1140	Other [add code]
03/01	*Cash received for sales goods*	*46m*	*03*	*250.00*				*250.00*		
10/01	*Donation from Mrs Dlamini*	*21c*	*01*	*100.00*			*100.00*			
21/01	*Course fees*	*03b*	*02*	*2,000.00*					*2,000.00*	
23/01	*Misc. sales*	*04b*	*02*	*500.00*				*500.00*		
28/01	*Course fees*	*47m*	*03-01*	*1,500.00*				`	*1,500.00*	
30/01	*4th qtr SMILE grant*	*05b*	*01*	*10,000.00*		*10,000.00*				
			PAGE TOTAL	*14,350.00*	-	*10,000.00*	*100.00*	*750.00*	*3,500.00*	
			Plus: Balance brought forward from last month:	*7,894.76*						
			Less: Total Payments for the month:	*(11,692.08)*						
			Balance carried forward to next month	*10,552.68*						

UC = Unit of currency

Appendix 4: Bank Book – Payments Page

MILESTONE PROJECT – January 2009

1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
					ANALYSIS OF PAYMENTS CATEGORY									
Date	Payee/ details of transaction	Cheque Or ref. no.	Cost Centre	Amount Paid UC *	Postage & Stat'y 3050	Rent, Ins & Utilities 3070	Reprs/ Ren 3080	Teleph. Fax 3090	Salary & Ben. 4030	Travel & Subs 4040	Fuel 5010	Food & Accom. 6020	Training Materials 6030	Other [add code]
03/01	SPM Lettings	13571	01	400.00		400.00								
03/01	Petty cash reimbursement	13572	02	176.54	14.00					15.00	30.00	73.00	44.54	
03/01	Safeway Insurance Co. – office	13573	01	789..00		789.00								
04/01	Newman's Garage – Dec .a/c	13574	03	1362.00							1362.00			
04/01	NGO Assembly – room hire	13575	01	50.00								50.00		
04/01	Pat's Restaurant – food deposit	13576	01	150.00								150.00		
04/01	H. Brown – Dec. expenses	13577	02	65.35						65.35				
10/01	JS Supplies - Dec. a/c	13578	02	672.34	75.75		288.70						307.89	
10/01	SEB – Electricity Dec.	13579	01	375.21		375.21								
11/01	Pat's Restaurant – food (final)	13580	01	675.00								675.00		
11/01	D&J Timber Supplies – stocks	13581	02	1,085.19									1,085.19	
12/01	Office Supplies Ltd, desk/ chair	13582	01	1,000.00										1,000.00 [0110]
13/01	Petty cash reimbursement	13583	01&02	199.15	65.44		20.56			7.50	86.15		19.50	
21/01	Jo Joshi - Nov/Dec. expenses	13584	03	135.00						135.00				
25/01	Telecoms – Phone bill	13585	01	657.30				657.30						
29/01	J. Joshi - Jan. salary	13586	03	2,300.00					2,300.00					
29/01	H. Brown – volunteer allowance	13587	01	800.00					800.00					
29/01	P. Khan - volunteer allowance	13588	03-02	800.00					800.00					
			PAGE TOTAL:	11,692.08	155.19	1564.21	309.26	657.3	3900	222.85	1478.15	948	1457.12	1,000.00

* UC = Unit of currency

Appendix 5: Petty Cash Book

MILESTONE PROJECT

Period covered: *1 to 12 January 2009*

						ANALYSIS OF PAYMENTS						
Date	PCV No.	Details of transaction or cheque reference	Cash In UC	Cash Out UC	Cash Balance UC	Postage & stat'y 3050	Repairs & Ren. 3080	Travel & subs 4040	Fuel 5010	Food/ Accom 6020	Training Mats. 6030	Other
3/1		Cash balance brought forward:	23.46	-	23.46	-	-	-	-	-	-	-
3/1	-	Top up cheque no. 013572	176.54	-	200.00							
3/1	1	Milk & coffee for office	-	10.57	189.43		10.57					
3/1	2	Calculator batteries	-	9.99	179.44		9.99					
5/1	3	Stamps	-	7.00	172.44	7.00						
6/1	4	Petrol – Jo's van. Bldg dept	-	45.00	127.44				45.00			
7/1	5	Fax paper	-	13.49	113.95	13.49						
10/1	6	OHP materials, pads & pens	-	29.45	84.50	9.95					19.50	
10/1	7	Petrol for Hari's car	-	35.65	48.85				35.65			
11/1	8	Oil	-	5.50	43.35				5.50			
12/1	9	DHL to New York	-	35.00	8.35	35.00						
12/1	10	Lunch/bus fare, Treasurer	-	7.50	0.85			7.50				
		PAGE TOTAL:	200.00 A	199.15 B	0.85 C	65.44	20.56	7.50	86.15	-	19.50	

UC = Unit of currency

Total A must = B + C

Appendix 6: Sample Bank Reconciliation Form

Milestone Project January 2009

Bank account details: *RNU Bank, Current account no. 00067891*		
Bank statement date:		*31/01/2009*
Bank statement sheet number:		*37*

A. Balance as on bank statement:		*12,024.98*

Less payments in cashbook, not on statement		
04/01 chq no. 13575 NGO Assembly		*(50.00)*
25/01 chq no. 13585 Telecomms Co.		*(657.30)*
29/01 chq no. 13586 J. Joshi		*(2,300.00)*
B. Total deduction		*(3,007.30)*
Plus receipts in cashbook, not on statement		
28/01 Course fees		*1,500.00*
C. Total addition		*1,500.00*
Less receipts on statement, not in cashbook		
None		
D. Total deduction		*0.00*
Plus payments on statement, not in cashbook		
Bank charges		*35.00*
E. Total addition		*35.00*
F. Balance in Bank Book [A-B+C-D+E]		*10,552.68*

Reconciliation performed by: *A.D.Ministrator*

Signed: *ADM* Date: *7/02/09*

Reconciliation checked by: *A. Treasurer*

Signed: *AT* Date: *9/02/09*

Appendix 7: Sample Receipts & Payments Account

Receipts and Payments Account for the Milestone Project

1 January to 31 December 2008

		UC	UC
Opening balance cash and bank			**2,880**
Receipts			
	Donor grants Received:		
	– DFID	48,000	
	– SMILE Trust	43,000	
	Donations & fundraising	750	
	Training fees	13,540	
	Sales	11,406	
	Bank interest	832	
	Total receipts		**117,528**
Payments			
	Personnel costs	46,580	
	Training expenses	20,588	
	Vehicle running expenses	14,886	
	Audit/accountancy	510	
	Bank charges	455	
	Board meetings	2,156	
	Postage & stationery	4,768	
	Publicity	396	
	Rent, insurance & utilities	9,985	
	Repairs & renewals	689	
	Telephones & fax	9,450	
	Office Equipment	1,850	
	Total payments		**(112,313)**
Closing balance cash and bank			**8,095**

UC = Unit of Currency

Appendix 8: Sample Income & Expenditure Account

MILESTONE PROJECT

Statement of Income & Expenditure for the year ended 31 December 2008

	UC	UC	2007 UC
INCOME:			
Donor Income:			
– DFID	48,000		45,000
– SMILE Trust	48,000	96,000	45,000
Other Income:			
– Donations & Fundraising	6,750		6,600
– Training Fees	14,640		12,250
– Sales	11,765		6,768
– Bank Interest	832	33,987	698
TOTAL INCOME		**129,987**	**116,316**
EXPENDITURE:			
Personnel Costs		52,580	48,780
Training Expenses		20,588	18,743
Vehicle Running Expenses		15,686	12,670
Depreciation		12,455	13,633
Administration:			
– Audit/Accountancy	587		500
– Bank Charges	455		387
– Board Meetings	2,057		1,480
– Postage & Stationery	4,838		6,776
– Publicity	396		325
– Rent, Insurance & Utilities	9,994		6,524
– Repairs & Renewals	539		324
– Telephones & Fax	9,341	28,207	6,803
TOTAL EXPENDITURE		**129,516**	**116,945**
EXCESS OF INCOME /(EXPENDITURE) FOR THE YEAR:		**471**	**(629)**

UC = Unit of Currency

Appendix 9: Sample Balance Sheet

Milestone Project

Balance Sheet as at 31 December 2008

	2008 UC	2007 UC
FIXED ASSETS		
Vehicles & Equipment:		
- Value at 1 January	122,696	130,329
- Plus: Additions during the year	1,850	6,000
- Less: Depreciation for wear & tear	(12,455)	(13,633)
	112,091	122,696
CURRENT ASSETS		
Cash at bank and in hand	8,095	2,880
Grants Receivable	10,000	5,000
Debtors & Prepayments	2,459	1,000
	20,554	8,880
Less: CURRENT LIABILITIES payable within one year		
Creditors and accruals	(3,262)	(2,664)
Net Current Assets	17,292	6,216
Net Assets	**129,383**	**128,912**
ACCUMULATED FUNDS		
Balance at beginning of the year	128,912	129,541
Plus surplus/(less deficit) for period	471	(629)
Balance at the end of the year	**129,383**	**128,912**
Represented by:		
General Purposes Fund	6,292	5,216
Designated Fund	11,000	1,000
Capital Fund	112,091	122,696
	129,383	**128,912**

UC = Unit of Currency

Appendix 10: Schedule of Creditors & Debtors

Schedule of Creditors as at 31 December 2008

Invoice Date	Payee	Description	Amount	Date paid	Account Name
31/12/08	Electricity Supply Co.	December 08 electricity bill	375.21	10 Jan 09	Rent/utilities/insurance
31/12/08	Telecomms Ltd	December 08 telephone a/c	657.30	25 Jan 09	Telephones & fax
21/12/08	City Stationers Ltd	Photocopying paper	145.25	05 Feb 09	Postage & stationery
31/12/08	Newman's Garage	Dec 08 petrol a/c, new tyres	1,362.00	4 Jan 09	Vehicle running/Travel
31/12/08	J. Joshi	Travel expenses for December 08	135.00	21 Jan 09	Vehicle running/Travel
-	PWC	Audit fee for 2008 audit (estimate)	587.00		Audit/Accountancy
		TOTAL CREDITORS	**3,261.76**		

Schedule of Debtors as at 31 December 2008

Due Date	Payee	Description	Amount	Date recvd.	Account Name
31/12/08	SMILE Trust	Final instalment of grant due	10,000.00	30 Jan 09	Grant - Smile Trust
31/12/08	Trainees	Training fees due for 2008 courses	2,100.00	Jan/Feb 09	Training Fees
31/12/08	Various	December 08 sales invoices	359.00	Jan/Feb 09	Sales
		TOTAL DEBTORS	**12,459.00**		

Appendix 11: Milestone Association Budget Summary

1 January to 31 December 2009

		Total Budget	Cost Centre Budgets		
			01 Co-ordination Dept	02 Building Dept	03 Metalwork Dept
INCOME		UC	UC	UC	UC
DONORS	DFID	90,000	20,000	35,000	35,000
	Smile Trust	90,000	18,000	36,000	36,000
	Vanguard Society	15,000	0	0	15,000
OTHER	Bank Interest	1,000	1,000	0	0
	Donations	8,000	2,000	3,000	3,000
	Sales	24,800	0	15,300	9,500
	Training Fees	42,500	500	21,000	21,000
	Total Income:	**271,300**	**41,500**	**110,300**	**119,500**
EXPENDITURE					
ADMINISTR-ATION	Audit/accountancy	4,500	1500	1500	1500
	Bank charges	600	200	200	200
	Board Meetings	1,200	400	400	400
	Depreciation	6,000	2,000	2,000	2,000
	Postage & stationery	7,500	2,500	2,500	2,500
	Publicity	1,500	500	500	500
	Rent, ins. & utilities	9,000	3,000	3,000	3,000
	Repairs & renewals	1,500	500	500	500
	Telephones/fax	6,300	2,100	2,100	2,100
STAFF	Salaries	47,700	0	23,850	23,850
	Housing costs	7,200	7,200	0	0
	Medical insurance	8,600	0	4,300	4,300
	In-service training	4,500	1,500	1,500	1,500
	Recruitment	0	0	0	0
	Travel & subsistence	3,000	1,700	650	650
VEHICLE RUNNING	Fuel	9,000	4,000	2,500	2,500
	Vehicle Insurance	18,000	6,000	6,000	6,000
	Vehicle maintenance	24,000	8,000	8,000	8,000
TRAINING	Fees & honoraria	3,000	0	1,500	1,500
	Food & accommodation	16,000	0	8,000	8,000
	Training Materials	92,200	0	41,500	50,700
	Total Expenditure:	**271,300**	**41,500**	**110,300**	**119,500**

UC = Unit of currency

Appendix 12: Milestone Project Budget Worksheet

Metalwork Dept. Direct Project Costs Budget Worksheet

Budget Period: 1 January to 31 December 2009
Budget Currency: UCs
Total Budget: 107,000 UCs

Ref	Budget Item	Unit	Quantity	Unit Cost UC	Total UC	Notes	Account Code
A	**Project Staff Costs**				**30,300**		
A1	Metalwork trainer salary	Month	12	1,775	21,300		4030
A2	Social Security/Employers' Taxes	Month	12	213	2,550	12% of salary	4030
A3	Medical Insurance	Lumpsum	1	4,300	4,300	20% of annual salary, rounded to nearest 100	4030
A4	In service training	Days	10	150	1,500	For team training and technical training in RSA	4010
A5	Per diem	Month	12	40	480		4040
A6	Field trip travel	Lumpsum	1	170	170	To RSA	4040
B	**Direct Project Costs**				**76,700**		
B1	Fuel	KM	5,000	0.50	2,500	Est. 425 km per month for 11 months, plus 325 in December	5010
B2	Insurance for project vehicle	Lumpsum	1	6,000	6,000	Insurance as per quotation	5020
B3	Vehicle maintenance	Quarter	4	2,000	8,000	Est. quarterly service / new tyres, based on previous year	5030
B4	Fees for guest tutors	Days	12	125	1,500	Fees for 2 guest tutors x 2 days at 3 out of 4 workshops	6010
B5	Food & accommodation	Participant	80	100	8,000	For 20 participants per workshop, based on previous year	6020
B6	Training Materials	Workshop	4	12,675	50,700	Raw materials and tools for trainees, based on previous year	6030
	Total Direct Costs				**107,000**		

NB: Central support costs are to be added.

Appendix 13: Milestone Project Summary Cash Flow Forecast

1 January to 31 December 2009

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Incoming cash												
DFID grant	18,000	0	0	24,000	0	0	24,000	0	0	24,000	0	0
Smile Trust grant	0	0	22,500	0	0	22,500	0	0	22,500	0	0	22,500
Vanguard Society grant	0	0	7,500	0	0	0	7,500	0	0	0	0	0
Bank Interest	40	5	0	0	71	0	0	74	0	26	96	0
Sales income	2,000	2,000	2,000	2,000	2,000	2,000	1,500	1,800	2,000	2,000	2,500	3,000
Donations	0	0	2,000	0	0	2,000	0	0	2,000	0	0	2,000
Training fees	3,500	7,000	0	7,000	3,500	0	0	7,000	3,500	0	7,500	3,500
A TOTAL CASH IN	**23,540**	**9,005**	**34,000**	**33,000**	**5,571**	**26,500**	**33,000**	**8,874**	**30,000**	**26,026**	**10,096**	**31,000**
Outgoing cash												
Administration costs	2,000	2,000	5,000	2,000	2,000	7,100	2,000	2,000	2,000	2,000	2,000	2,000
Staff costs	5,600	5,600	5,600	5,600	5,600	5,600	6,200	6,200	6,200	6,200	6,200	6,400
Vehicle Running costs	22,000	2,500	2,500	3,000	2,500	2,500	3,000	2,500	2,500	3,000	2,500	2,500
Training programme	1,000	25,000	2,000	2,000	25,000	1,000	2,000	25,000	2,000	1,000	25,000	200
B TOTAL CASH OUT	**30,600**	**35,100**	**15,100**	**12,600**	**35,100**	**16,200**	**13,200**	**35,700**	**12,700**	**12,200**	**35,700**	**11,100**
C Net cash flow [A - B]	(7,060)	(26,095)	18,900	20,400	(29,529)	10,300	19,800	(26,826)	17,300	13,826	(25,604)	19,900
D Cash balance at start of month	8,095	1,035	(25,060)	(6,160)	14,240	(15,289)	(4,989)	14,811	(12,015)	5,285	19,111	(6,493)
E Cash balance at end of month [C + D]	**1,035**	**(25,060)**	**(6,160)**	**14,240**	**(15,289)**	**(4,989)**	**14,811**	**(12,015)**	**5,285**	**19,111**	**(6,493)**	**13,407**

Appendix 14: Milestone Project – Budget Compared To Actual Report

1 January to 31 March 2009

		TOTAL BUDGET	*1 January to 31 March* BUDGET	ACTUAL	VARIANCE (adv)/fav	VARIANCE %	NOTES
Income (actual = receipts)		UC	UC	UC	UC	UC	
Donors	DFID	90,000	25,000	25,000	0	*0%*	
	Smile Trust	90,000	25,000	25,000	0	*0%*	
	Vanguard Society	15,000	3,750	6,350	2,600	*69%*	Project tools purchased/reimbursed early
Other	Bank Interest	1,000	250	205	(45)	*-18%*	
	Donations	8,000	2,000	350	(1,650)	*-83%*	Fundraising strategy to be reviewed
	Sales	24,800	6,200	5,462	(738)	*-12%*	
	Training Fees	42,500	14,167	14,500	333	*2%*	
	TOTAL	**271,300**	**76,367**	**76,867**	**500**	***0.7%***	
Expenditure (includes commitments)							
Administration	Audit fees	4,500	0	0	0	*0%*	
	Bank charges	600	150	105	45	*30%*	
	Board Meeting	1,200	150	127	23	*15%*	
	Depreciation	6,000	0	0	0	*0%*	Year end book adjustment
	Post & stationery	7,500	1,875	636	1,239	*66%*	Delay in printing the annual report
	Publicity	1,500	375	200	175	*47%*	
	Rent, ins. & utilities	9,000	2,250	2,100	150	*7%*	
	Repairs & renewals	1,500	375	327	48	*13%*	
	Telephones/fax	6,300	1,575	1,982	(407)	*-26%*	Aware of problem, making efforts to improve
Staff	Salaries & benefits	63,500	15,875	15,150	725	*5%*	
	In-service training	4,500	1,125	1,000	125	*11%*	
	Recruitment	0	0	0	0	-	
	Travel & subs.	3,000	750	835	(85)	*-11%*	
Vehicle Running	Fuel	9,000	2,250	3,675	(1,425)	*-63%*	Error on our original budget – request review
	Vehicle Insurance	18,000	17,500	17,500	0	*0%*	
	Vehicle maintenance	24,000	6,000	5,608	392	*7%*	
Training	Fees & honoraria	3,000	750	500	250	*33%*	
	Food & accomm.	16,000	4,000	4,930	(930)	*-23%*	Costs for April course incurred in this quarter
	Training Materials	92,200	23,050	26,450	(3,400)	*-15%*	Costs for April course incurred in this quarter
	TOTAL	***271,300***	***78,050***	***81,125***	***(3,075)***	***-4%***	
	SURPLUS/(DEFICIT)	0	(1,683)	(4,258)	(2,575)		

UC = Unit of currency

Appendix 15: Sample Donor Monitoring Report

DFID No.12345
STATEMENT OF ACTUAL EXPENDITURE FOR QUARTER ENDING: **30-Sep-07**
AND ESTIMATED EXPENDITURE FOR QUARTER ENDING: **31-Dec-07** ***Rate applied:*** ***3.75***

		1	2	3	4 [2 - 3]	5	6	7	8 [7 - 4]	
Budget items:		**Annual Budget GBP**	**Budget last Qtr GBP**	**Actual last Qtr GBP**	**Balance remaining GBP**	**Spent to date GBP**	**Spent to date %**	**Budget next Qtr GBP**	**Grant claim GBP**	**See Report note no.**
Administration	Audit fees	1,200	0	0	0	1,267	106%	0	0	
	Bank charges	160	40	29	11	91	57%	32	21	
	Board Meeting	320	27	23	4	303	95%	27	23	
	Depreciation	1,600	0	0	0	0	0%	1,600	1,600	
	Post & stationery	2,000	500	426	74	1,814	91%	187	113	1
	Publicity	400	100	43	57	189	47%	200	143	
	Rent, ins. & utilities	2,400	600	586	14	1,745	73%	573	560	
	Repairs & renewals	400	100	57	43	212	53%	187	143	
	Telephones/fax	1,680	420	572	(152)	1,548	92%	415	567	2
Staff	Salaries & benefits	16,933	4,233	4,280	(47)	12,411	73%	4,280	4,327	
	In-service training	1,200	300	859	(559)	1,170	98%	30	589	3
	Recruitment	0	0	0	0	36	-	0	0	
	Travel & subs.	800	200	210	(10)	585	73%	195	205	
Vehicle Running	Fuel	2,400	600	773	(173)	2,622	109%	874	1,047	4
	Vehicle Insurance	4,800	0	40	(40)	4,720	98%	0	40	
	Vehicle maintenance	6,400	1,600	1,297	303	5,087	79%	1,307	1,004	
Training	Fees & honoraria	800	200	400	(200)	653	82%	147	347	
	Food & accomm.	4,267	1,067	1,027	40	3,501	82%	1,040	1,000	
	Training Materials	24,587	6,147	6,157	(11)	18,455	75%	6,133	6,144	
TOTAL		**72,347**	**16,133**	**16,780**	**(647)**	**56,409**	**78%**	**17,226**	**17,873**	
Total apportioned to DFID:		24,000	5,324	5,537	(213)	18,615	78%	5,385	5,599	
% apportioned to DFID:		*33%*	*33%*	*33%*	*33%*	*33%*		*33%*	*31%*	

Schedule of DFID grants received/due:

	GBP
Qtr 1	6,667
Qtr 2	5,867
Qtr 3	5,867
Qtr 4	5,599
TOTAL	**24,000**

Appendix 16: Milestone Project – Budget Forecast to 31 December 2009

	TOTAL	Actual - 1 January to 30 September			TOTAL	Forecast	TOTAL	
	BUDGET	Quarter 1	Quarter 2	Quarter 3	To 30 Sept	Quarter 4	ANTICIPATED	
Income	UC	UC	UC	UC	UC	UC	UC	
DFID	90,000	25,000	22,000	22,000	69,000	21,000	90,000	
Smile Trust	90,000	25,000	25,000	25,000	75,000	15,000	90,000	
Vanguard Society	15,000	6,350	0	8,500	14,850	0	14,850	
Bank Interest	1,000	205	196	226	627	200	827	
Donations	8,000	350	895	3,250	4,495	800	5,295	
Sales	24,800	5,462	4,670	6,785	16,917	7,000	23,917	
Training Fees	42,500	14,500	6,900	11,200	32,600	9,500	42,100	
TOTAL	**271,300**	**76,867**	**59,661**	**76,961**	**213,489**	**53,500**	**266,989**	
Expenditure								
Audit fees	4,500	0	4,750	0	4,750	0	4,750	
Bank charges	600	105	125	110	340	120	460	
Board Meeting	1,200	127	924	85	1,136	100	1,236	
Depreciation	6,000	0	0	0	0	6,000	6,000	
Post & stationery	7,500	636	4,568	1,598	6,802	700	7,502	AGM costs were under estimated.
Publicity	1,500	200	350	160	710	750	1,460	Expect the major event in November
Rent, ins. & utilities	9,000	2,100	2,243	2,199	6,542	2,150	8,692	Expenditure levels are generally on track.
Repairs & renewals	1,500	327	256	213	796	700	1,496	Major repairs expected in the month of December
Telephones/fax	6,300	1,982	1,678	2,145	5,805	1,558	7,363	Phone rates were raised by phone company.
Salaries & benefits	63,500	15,150	15,340	16,050	46,540	16,050	62,590	On track
In-service training	4,500	1,000	167	3,222	4,389	111	4,500	Last Qtr will not be very busy.
Recruitment	0	0	135	0	135	0	135	
Travel & subsistence	3,000	835	569	789	2,193	731	2,924	Estimate based on activity plan
Fuel	9,000	3,675	3,257	2,900	9,832	3,277	13,109	Estimate based on activity plan
Vehicle Insurance	18,000	17,500	50	150	17,700	0	17,700	
Vehicle maintenance	24,000	5,608	8,603	4,865	19,076	4,900	23,976	Estimate based on activity plan
Fees & honoraria	3,000	500	450	1,500	2,450	550	3,000	On track
Food & accomm.	16,000	4,930	4,350	3,850	13,130	3,900	17,030	
Training Materials	92,200	26,450	19,667	23,090	69,207	23,000	92,207	
TOTAL	**271,300**	**81,125**	**67,482**	**62,926**	**211,533**	**64,597**	**276,130**	

Appendix 17: Sample Financial Management Work Plan

KEY: ------ = daily x = no. weeks			*JAN*	*FEB*	*MAR*	*APR*	*MAY*	*JUN*	*JUL*	*AUG*	*SEP*	*OCT*	*NOV*	*DEC*
FINANCIAL ACCOUNTING ROUTINES														
	Banking	Daily	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------
	Payroll	Monthly	x	x	X	x	x	x	X	X	x	x	x	x
	Prepare Payment vouchers/cheques	Daily	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------
	Prepare/check Purchase Orders	Daily	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------
	Reimburse/reconcile p.cash / advances	Weekly	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
	Update Cash Book	Weekly	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
	Bank reconciliation	Monthly	x	x	X	x	x	x	X	X	x	x	x	x
	Trial Balance	Monthly	x	x	X	x	x	x	X	X	x	x	x	x
	Filing	Daily	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------
	Update stock records	Weekly	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx	xxxx
	Reconcile stock records	Monthly	x	x	X	x	x	x	X	x	x	x	x	x
YEAR END														
	Year-end reconciliation	Annual	----------											
	Prepare financial statements	Annual		----------										
	Prepare year-end schedules	Annual	----------											
	Auditor's visit	Annual			X									
	Income Tax annual return	Annual							----------					
BUDGETING														
	Prepare first draft budgets	Annual								xxxx				
	Revise budgets	Annual									x	x		
	Budget to Board for approval	Annual											x	
REPORTS														
	Prepare Budget Monitoring Report	Quarterly	x			x			X			x		
	Prepare Cash Flow Report	Monthly	x	x	X	x	x	x	X	x	x	x	x	x
	Prepare Donor Reports													
	- DFID	Quarterly		x			x			x			x	
	- USAID	Quarterly	x			x			X			x		
REVIEWS														
	Assets Register	Quarterly	x			x			X			x		
	Insurance cover	Six months				x						x		
	Chart of Accounts	Annually												x
	Delegated Authorities	Six months						x						x
	Pay award	Annually			X									
	Update Finance Manual	Annually												x

Appendix 18: A Checklist for Good Practice

A. Minimum Requirements	
Standard	**Why**
☑ A valid supporting document for every transaction, (securely filed and stored for the minimum period required.)	Protection for staff, evidence and details of transaction.
☑ A cash book for every bank account, reconciled every month.	To organise and summarise transaction information; check for errors and omissions.
☑ A Chart of Accounts – used consistently in the accounting records and budgets	Principle of consistency; to facilitate production of financial reports.
☑ A budget detailing costs and anticipated income for all operations.	Planning, fundraising, control and reporting.
☑ Clear delegation of authority – from governing body through the line management structure.	To know who is responsible for what and within what limits.
☑ Separation of duties – sharing finance administration duties between at least two people	To prevent temptation to steal and reduce opportunity to commit fraud; to share the load.
☑ Annual financial statements – preferably audited by an independent person.	Accountability to stakeholders; transparency.

B. Good Practice	
Standard	**Why**
☑ Additional accounting records when staff employed (wages book) or assets owned (Assets Register).	To meet statutory and audit requirements; for control purposes.
☑ Budgets based on real activity plans, which include the full cost of running a project.	Realistic, more likely to meet targets.
☑ Budgets with clear calculations and notes.	Easy to read and make adjustments. Easy to justify calculations.
☑ Separate core costs budget.	Encourages active management and financing strategy for core costs
☑ Monthly cash flow forecast.	Helps to identify and take action to avoid short-term cash flow problems.
☑ Use of Cost Centres for multiple donors and/or projects.	To separate restricted funds and related transactions; to facilitate reporting to managers and donors.
☑ Funding grids for multiple donors situations.	To avoid double-funding situations and identify areas of shortfall.
☑ Budget monitoring reports each month.	To monitor progress; control purposes.
☑ Written policies and procedures	To prevent confusion about organisation rules and expected practice.
☑ Diversified funding base – mix of restricted and unrestricted funds.	Less vulnerable to financial shocks; helps to build up reserves.
☑ A reasonable level of reserves.	Less vulnerable to financial shocks; helps overcome cashflow problems

Appendix 19: Sample Standard Forms

Expenses/Cash Advance Claim Form

NAME: _____

POSITION: _____

Date	Details of journey and/or type of allowance being claimed:	Receipt attached ✓	Amount claimed
TOTAL CLAIMED :			

I confirm that the above expenses have been/will be* necessarily incurred by me during the course of my duties.

* Delete as appropriate

SIGNED: _____ DATE: _____

AUTHORISED: _____ DATE: _____

RECEIVED BY: _____ DATE: _____

Fixed Assets Register

REF:

Name of Asset:			
Description:			
Make/Model:		**Serial No.:**	
Date Of Purchase:		**Supplier:**	
Purchase Price:		**Invoice No:**	
Location Of Asset:			
Depreciation Period:		**Depreciation Method:**	

Depreciation/Repairs/Insurance Schedule:

Date	Details	Cost / Valuation

Payment Voucher

Date:		Amount:	
Supplier or payee details		Cheque No. or PCV Reference:	
Invoice No.:		Order No.:	
COST CENTRE Or DEPT. REFERENCE:		BUDGET CATEGORY / CODE:	
DETAILS OF PAYMENT OR REQUEST FOR FUNDS:			
HAVE ESTIMATES/QUOTATIONS BEEN OBTAINED? YES/NO If yes, please attach copies and indicate preferred supplier with reasons. If no, please state why not obtained.			
CHECKED BY:			
ORIGINATED BY: DATE:		AUTHORISED BY: DATE:	
ENTERED IN RECORDS BY:		DATE:	

Bank Reconciliation Form

Bank account details:		
Bank statement date:		
Bank statement sheet number:		

A. Balance as on statement:		
Less payments in cashbook, not on statement (e.g. un-presented cheques)		
B. Total deduction		
Plus receipts in cashbook, not on statement (e.g. unbanked income)		
C. Total addition		
Less receipts on statement, not in cashbook (e.g. income received directly into bank account)		
D. Total deduction		
Plus payments on statement, not in cashbook (e.g. direct debits & bank charges)		
E. Total addition		
F. Balance in Bank Book [A-B+C-D+E]		

Reconciliation performed by:
Signed: Date:
Reconciliation checked by:
Signed: Date:

Vehicle Log Sheet

Vehicle registration no:_____

DATE OF JOURNEY	DESTINATION/JOURNEY DETAILS	DEPT.	KM READING		FUEL PURCHASED		DRIVER SIGNATURE
			START	FINISH	COST	# LITRES	
	Total KMs run / petrol purchased this month						

Appendix 20: Mango's Health Check

Mango's Health Check

How healthy is financial management in your not-for-profit organisation?

Version 3

2009

Contents

About Mango

Mango is a UK based charity which exists to strengthen the financial management of not-for-profit organisations, including NGOs. Mango publishes freely available tools, like this one, as well as running training courses and providing finance staff to work with NGOs. See www.mango.org.uk for more details.

What can Mango's Health Check do?

Mango's Financial Health Check can help you assess the health of your organisation's financial management. It is designed as a self assessment tool so that you can identify the areas where you need to improve.

The Health Check is a set of statements of good practice. They cover all the key areas of NGO financial management. For each statement, you need to consider how well your own organisation is in line with good practice. By the end of the Health Check you will be able to tell if the financial management in your organisation is healthy or sick - and whether you need to call a doctor!

You may like to run the Health Check again after a year or two, to assess and monitor your progress.

What can Mango's Health Check NOT do?

Every organisation is different and financial management systems must reflect this. A 'one size fits all' approach cannot work. But the key aspects of good practice are the same for most organisations most of the time. The Health Check focuses on those key aspects. They are the foundation stones of good practice.

Mango's Financial Health Check only provides a general indication of the health of your organisation's financial management. It is not an exhaustive list of all aspects of financial

management. It is not an audit and it does not describe a standard set of procedures which are relevant in every situation.

It is not appropriate to set a score as a 'pass rate' for partner assessment. It is not appropriate to compare scores of two organisations and make conclusions about differences between them.

Who is Mango's Financial Health Check designed for?

It has been particularly designed for small and medium sized not-for-profit organisations (or field offices). This may include Non Governmental Organisations, schools, medical centres, churches etc. It is not designed for the head offices of international organisations.

How to use Mango's Health Check

The Health Check can be run by any member of staff or a trustee. You do not need specialist financial skills to complete it. It includes explanations of each section and a glossary of the financial terms used.

The most useful way to use this tool is to complete it in a 2-3 hour workshop meeting, with input from the Treasurer, Chief Executive Officer, Senior Managers, and a selection of budget holders, finance staff and field staff (ideally 5- 7 people).

Taking each statement of best practice in turn, discuss whether it is true, or is in place, or happens in your organisation. Agree on a score based on what actually happens, not what is supposed to happen, or what is documented in your finance manual. The scores available are 5,4,1 and 0 only.

Explanation	Score
Our practice is totally in accordance in with the statement	5
Close to 5, but not quite there	4
Close to 0, but not that poor	1
This is not in place, or is not true or does not happen	0

Clearly a degree of judgement is required to decide between '4' or '1', and it is not an exact science. If you cannot give yourselves a clear cut 5 or 0, you need to decide which one you are closer to.

Often the real value in this exercise is not the score itself so much as the conversations and the details of issues discussed.
Make good notes and keep a list of action points as they come up.

Ring the score for each statement. Add up the total for each section and transfer it to page 9 to get a total. Then interpret the score using the guidance given.

Comments

Mango welcomes comments on its tools. Please send any comments or suggestions you might have on the Health Check to Terry Lewis, tlewis@mango.org.uk. Thank you!

Section 1	Planning & budgeting

Budgeting is about working out how much your planned activities are likely to cost. Both programme and finance staff should be involved in setting budgets, to create a foundation for good cooperation and coordination during spending and budget monitoring.

Budgets have a crucial role to play in strong financial management. Budgets should be approved by the Board of Trustees, to check they reflect the planned strategic direction of the organisation. Project managers can use a budget to guide implementation and check on progress. Overhead costs that are shared by many projects also need to be carefully controlled by an assigned budget holder.

The codes used for your budget lines need to correspond to the codes used in your accounting system. Otherwise it will be difficult to track actual spending against expected spending in your budget monitoring reports.

A cash flow forecast is as important as a budget. It constantly looks 3-6 months into the future, starting with the actual cash available now. It helps you to prioritise the timing and scale of planned activities and to spot cash flow problems in good time.

Ref	Statement of best practice	Score			
1.1	Budgets are prepared in good time for all the costs of running the organisation	5	4	1	0
1.2	Both finance and programme staff are involved in setting budgets	5	4	1	0
1.3	Project budgets are based on the costs of planned activities	5	4	1	0
1.4	Budget worksheets include explanatory notes and clear calculations	5	4	1	0
1.5	A separate budget is prepared for core costs (overheads)	5	4	1	0
1.6	Organisational budgets are approved by the Board of Trustees	5	4	1	0
1.7	A named individual (budget holder) is responsible for implementing and managing each budget	5	4	1	0
1.8	Budget codes match (or correspond to) accounting codes	5	4	1	0
1.9	All planned operational costs are adequately funded	5	4	1	0
1.10	A cash flow forecast is prepared every month	5	4	1	0
Total score for planning & budgeting					

Section 2	Basic accounting systems

Every financial transaction should be backed up by a 'supporting document', e.g. a receipt, invoice or sign sheet (eg for many travel reimbursements). This is the evidence that a specific transaction has taken place.

Every transaction involving paying out or receiving money should be written down in a cashbook. It can be kept in a physical cashbook or petty cashbook, on an Excel spreadsheet or as part of a computerised accounting package. Every entry in the cashbooks should be referenced back to the relevant supporting document.

It is important to check the accuracy of the accounting books at the end of each month by carrying out two essential 'reconciliations'. The bank statement balance is compared to the bank cashbook closing balance. A physical cash count is done to check the closing balance in the petty cash book.

Accounting works by assigning codes to each transaction entered in the cashbooks. The unique list of accounting codes that an organisation uses is called its "Chart of Accounts". Another set of codes can be used to assign transactions to a specific project or donor. These are called 'cost centre' codes.

Ref	Statement of best practice	Score			
2.1	Every payment made has a supporting document providing evidence	5	4	1	0
2.2	All cash or cheques received are recorded on pre-numbered carbon copy receipts (*if NGO does not receive cash or cheques score 5*)	5	4	1	0
2.3	All payments and receipts are recorded in cashbooks (date, description, amount)	5	4	1	0
2.4	There is a separate cashbook for each bank and cash account	5	4	1	0
2.5	Every entry in the cashbooks is cross referenced to a supporting document	5	4	1	0
2.6	All cashbooks are updated at least once per month	5	4	1	0
2.7	All cashbooks are written neatly in permanent ink or on computer	5	4	1	0
2.8	A standard Chart of Accounts is used to code (or classify) each transaction in the cashbooks	5	4	1	0
2.9	Transactions are also classified by project or donor using a standard list of 'cost centres'	5	4	1	0
2.10	A bank reconciliation is done each month, for every bank account	5	4	1	0
2.11	A cash count reconciliation is witnessed and recorded each month	5	4	1	0
2.12	The organisation keeps track of amounts owed to others (eg suppliers) and owed by others (eg staff)	5	4	1	0
Total score for basic accounting systems					

Section 3	Financial reporting

The Board of Trustees need financial reports to oversee the finances of the organisation. Managers need up-to-date figures to monitor projects and make decisions. Donor agencies need reports to check the use of their money, and often as a condition for further funding. Increasingly, organisations are sharing financial information with beneficiaries to increase accountability and build confidence. An annual external audit verifies the accuracy of the financial statements.

The monthly financial reports should include an **Income and Expenditure** report showing money coming into the organisation and how it was spent. If the report compares the amount spent against budget, it is called a **Budget Monitoring Report.** The budget is supposed to be a tool not a straight jacket. Project managers should use financial reports to help make decisions so that the money is used efficiently and effectively to achieve desired outcomes.

It is also important to report on balances held at the end of each month or quarter. Balances includes the amount of money held (cash and bank), as well as amounts owed to the organisation (such as unaccounted working advances) and owed by the organisation (eg to suppliers / tax authorities).

Reports should be produced showing the relevant level of detail according to their use (eg for a single project or donor) or consolidated. Reports should also have the right format for their use, eg donor formats as per grant agreements, standard formats for annual audited accounts, accessible formats for beneficiaries, user friendly formats for managers.

NB: Donor reports are considered in **Section 5: Grant Management.**

Ref	Statement of best practice	Score			
3.1	The board reviews financial reports every quarter	5	4	1	0
3.2	Senior managers discuss financial reports at least once every three months	5	4	1	0
3.3	Reports include details of cash and bank balances, amounts due (eg from staff) and owed (eg to suppliers)	5	4	1	0
3.4	Budget holders receive budget monitoring reports every month	5	4	1	0
3.5	Budget monitoring reports include explanations and comments about differences	5	4	1	0
3.6	Financial reports are used to help make decisions	5	4	1	0
3.7	Financial information is shared with beneficiaries at least once per year, in an accessible way	5	4	1	0
3.8	Annual audits are up-to-date (signed within 6 months of the year end)	5	4	1	0
Total score for reporting					

Section 4	Internal controls

NGOs use a lot of different internal controls to make sure that:

- Assets are safeguarded
- Accounting records are accurate and up to date
- Fraud and errors are prevented and detected
- Staff are protected

Note: the other sections of the Health Check also include important controls. For instance cash and bank reconciliations are important for checking accuracy of accounting records and identifying fraud.

Ref	Statement of best practice	Score			
4.1	Cash is kept safely in a locked cashbox or safe, in the custody of one individual	5	4	1	0
4.2	All cash received is banked intact, ie without any being spent *(if no cash is received, score 5)*	5	4	1	0
4.3	All cheques are signed by at least two authorised signatories	5	4	1	0
4.4	Cheques are signed only when all the details have been properly filled in (ie no signatories ever sign blank cheques)	5	4	1	0
4.5	Bank reconciliations are checked by someone who did not prepare them	5	4	1	0
4.6	There is a written policy detailing who can authorise expenditure of different types or value	5	4	1	0
4.7	All transactions are properly authorised	5	4	1	0
4.8	Cash payments are authorised by someone other than the cashier	5	4	1	0
4.9	Different steps in the procurement process, (eg ordering, receiving and paying) are shared among different people.	5	4	1	0
4.10	Expenses claims for staff advances are checked by the same person who authorised the advance	5	4	1	0
4.11	Staff salaries (including advances and loans deductions) are checked each month by a senior manager	5	4	1	0
4.12	Statutory deductions (eg payroll taxes) are properly made and paid on time	5	4	1	0
4.13	All fixed assets (eg vehicles, computers, equipment) owned by the NGO are insured and controlled using a fixed assets register	5	4	1	0
4.14	There is an approved policies and procedures manual in place which is relevant to the organisation, and known by staff	5	4	1	0
4.15	A properly registered audit firm is selected by the trustees	5	4	1	0
Total score for internal controls					

Section 5	Grant management

Most NGOs get at least some of their funding as grants from donor partners. It is important to have a grant agreement in place that outlines the amounts and timings of funds to be transferred.

Donors tend to fund specific projects with specific budgets which form part of the agreement.

The grant agreement may also contain a number of grant conditions, including procurement rules and reporting requirements. Programme and Finance staff need to work together to ensure consistency between the narrative and financial reports about the same project.

Often NGOs work with several different donors at the same time. It is very important to keep track of which donor is funding which project (or part of a project). It is very bad practice to 'borrow' money received from a donor for a specific project for another purpose.

Ref	Statement of best practice	Score			
5.1	There is a signed grant agreement in place for each grant	5	4	1	0
5.2	Senior Managers check the grant conditions are reasonable before signing agreements	5	4	1	0
5.3	Grant conditions on procurement are known by finance staff, budget holders and procurement officer(s)	5	4	1	0
5.4	There is compliance with the terms and conditions in grant agreements	5	4	1	0
5.5	Donors receive financial reports in the right format and on time	5	4	1	0
5.6	Donor financial and narrative reports are consistent and clearly linked to each other	5	4	1	0
5.7	Donor funds are kept for the activities they are meant for and never 'borrowed' for other activities	5	4	1	0
Total score for grant management					

Section 6	Staffing

Good financial management is dependent on staff with the right skills, support, and attitude to carry out their responsibilities. All staff have a role to play in financial management. The accounting staff are part of a wider team including the Executive Director, Programme Managers and the Board. Integrating good financial management into programmes involves budget holders and finance staff working hand in hand through all the stages of the financial cycle (plan-do-review).

It may be difficult to assess the technical competence of accounting staff. Good indicators are the timeliness of reports, the neatness of files and records in the accounts office, and auditor's comments or recommendations.

Ref	Statement of best practice	Score			
6.1	The board includes someone with the skills needed to oversee all financial activities	5	4	1	0
6.2	The finance staff have the skills (and qualifications) needed to carry out all financial activities	5	4	1	0
6.3	Managers and programme staff have the financial skills they need to manage budgets and implement controls	5	4	1	0
6.4	Finance staff and budget holders work together well in payments processing and budget monitoring	5	4	1	0
6.5	Different roles within the finance function are clearly defined, known and followed	5	4	1	0
6.6	Senior staff lead by example in following control procedures	5	4	1	0
6.7	Finance staff are recruited freely and fairly on the basis of merit only	5	4	1	0
6.8	All staff receive the training and support they need to carry out their financial management responsibilities	5	4	1	0
Total score for staffing					

Interpreting your score

Record your score for each section in this table. Then compare it to the columns on the right and ring or shade the appropriate risk assessment for each section. Finally add up your total score and see the advice below.

Section	Your Score
1. Planning and budgeting	
2. Basic Accounting Systems	
3. Financial reporting	
4. Internal controls	
5. Grant management	
6. Staffing	
Total Score	

High Risk	Medium Risk	Low Risk
0 - 25	26 - 40	41 - 50
0 - 30	31 - 50	51 - 60
0 - 20	21 - 35	36 - 40
0 - 40	41 - 60	61 - 75
0 - 15	16 - 25	26 – 35
0 - 20	21 - 30	31 - 40
0 - 150	**151 - 240**	**241 - 300**

Your score is over 240

Well done! Your financial management is in good shape. The risks of not being able to complete your work because of financial problems are low. But do also consider the risk assessment in each section: effective financial management requires strength in all six areas. Use this opportunity to make improvements and further reduce your financial risk.

Your score is between 151 and 240

Not bad! There is clearly some good financial practice in place, but still plenty of room for improvement. There is a risk that financial problems will prevent you from doing your work. Low scoring sections require immediate attention from managers.

Your score is less than 150

Work to be done! You have serious problems. Your financial management is not in good health. There is a high risk that you will face financial problems in the near future: funds may be misused, or donors may withdraw their financial support. Managers and trustees should meet urgently to discuss how the situation can be improved. You should consider calling in assistance as soon as possible. This must be dealt with right now.

Account code	A code for a specific type of transaction. Transactions are given a code which describes what type of income or expenditure they are - e.g. 5050 Transport costs, 5600 Office rent etc.
Bank reconciliation	Comparing the month end balance on the bank statement to the month end balance in the cashbook and identifying any differences.
Budget	The best possible estimate of the cost of a set of activities over a given period of time, and of how you are going to pay for those activities
Cashbook	A book or spreadsheet that lists all of the receipts and payments made in to and out of a particular bank or cash account.
Cash reconciliation	Comparing the month end physical cash counted to the expected month end balance in the petty cashbook.
Cash flow forecast	A report that shows the expected timing of receipts and payments for the next 3-6 months (or longer).
Chart of accounts	A list of all account codes, including a description of each code.
Core costs	Costs shared by many projects. Also called overheads or indirect costs.
Cost centre	A label for a group of costs which are looked at together. For instance, different projects are often treated as different cost centres.
External audit	A review of the year-end financial statements carried out by a professionally qualified and legally registered auditor resulting in an opinion about whether they give a true and fair view.
Fixed asset	An item of high value owed by the organisation for use over a long period. Normally office equipment, vehicles and property.
Fixed asset register	A register (list) of the assets owned by the organisation, including details such as: reference number, date bought, purchase price, and location.
Payment voucher	An internal document raised for each payment. It provides a unique reference number and evidence of authorisation. Supporting documents are attached to it.
Petty cash records	The cashbook where cash transactions are recorded, and the supporting documents relating to each transaction.
Procurement	The process of purchasing goods and services. Steps in the process may include requesting, authorising, selecting suppliers, ordering, receiving and paying.
Receipt book register	A register (list) of receipt books as they come from the printers showing dates when each one is issued, finished and returned.
Reconciliation	The process of comparing information held in two sets of records that describe the same transactions.
Supporting document	The original documents that describe each transaction. These may include, receipts, invoices, delivery notes, sign sheets etc
Statutory deductions	Amounts which must be taken from an employee's pay before they receive it, such as income tax or national insurance contributions.
Transaction	Any exchange of goods, services or money in return for other goods, services or money. Most commonly receipts and payments.
Trustee	A member of an NGO's most senior governing body, who shares overall responsibility for the NGOs work.
Working advance	A sum of money entrusted to someone to spend on behalf of the organisation, which needs to be accounted for.