HOW TO BUILD A GOOD SMALL NGO

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SECTION D: **MONEY – BUDGETING, ACCOUNTING & FUND-RAISING**

This Section consists of parts of Chapters 9 & 10 and Annexes 4 & 5.
You should also download the two Excel Spreadsheets – 'budget.xls' and 'accounting.xls' (from http://www.networklearning.org/books/build-ngo.html).

Note: The original numbering is left in place so that extracts can be traced back.

Update, March 2006: This section was co-written by Mango, the NGO that helps other NGOs manage money better. Mango now have a "Financial Management Health Check" (in English, French, Spanish, Arabic and Russian). This will allow you to see how healthy the financial management is in your NGO: www.mango.org.uk/guide/section.aspx?ID=22
More financial resources are at www.mango.org.uk/guide/section.aspx?ID=5

9.3 Making Budgets

9.3.1 **The role of budgeting:**

Budgeting has a vital role to play throughout the cycle of every project. Money is the lifeblood of any project (or NGO), and it is controlled through budgets. So, budgeting is a fundamental element of all planning and monitoring. In the planning stages, it is necessary for the project's managers to have an accurate idea of the true cost of the project. This should have an impact on its design.

Without a realistic estimate of costs, there is no way of comparing the output of the project (perhaps in humanitarian terms) to the resources required – i.e. the project's cost-effectiveness. This prevents senior management from making strategic decisions about how best to use their limited resources. (For example, the cost of over-budgeting one project is paid in terms of lack of funding available for other projects. In other words, if project budgets are made too big, then they reduce the total results that an NGO can achieve.) The budget is also the basis of all financial negotiations with donors for external funding.

Once a project is under way, an accurate budget is essential as a financial control. The basis of financial management is comparing actual expenditure to budgeted expenditure. Without an accurate budget, this is impossible. Finally, the budget should form part of the evaluation of a project once it is finished.

> EXAMPLE: **WATER PROJECT IN ASIA**
> For a water project in Asia, the donor, a European Government, made a budget at their desks in their capital city. A lump sum was set down for the digging of 500 wells with pumps. Elsewhere in the Terms of Reference it mentioned that the wells should produce water, but the Project Manager was more concerned with digging. The project budget was never translated into exact field expenditures. Two-thirds of the way through, the project was on target and within budget – except that half the wells had no water. When an assessor pointed this out, the project had to re-dig all the dry wells, making them complete late and way over budget. When the project was evaluated, everyone blamed everyone else.

9.3.2 **Definition, and overall approach to budgeting:**

A budget describes the expected costs of one set of activities. So, budgets often have to be revised part way through a project. This happens when the activities that are actually carried out change from the activities originally planned. There is no point in comparing the actual cost of buying apples (or digging wells) to the projected cost of buying oranges (or drilling boreholes).

This means that it is important that the original budget was put together in a logical, simple way. Otherwise, it is impossible to understand how the original figures were calculated (or if they were calculated at all). And this makes it impossible to adapt the budget to changing circumstances.

So it is extremely important for budgets to be carefully thought through and well presented. Somebody else picking up your budget should always be able to understand it all (and adapt it, when necessary) with no additional explanation beyond what is written down. These notes suggest one way of doing this.

9.3.3 **Notes about accounts structure:**

A budget is drawn up using a specific accounts structure. An 'accounts structure' is the way in which costs are categorised. (For example, costs may be categorised as: local staff, international staff, travel, etc.) It is generally difficult to move from one accounts structure to another, once a project is under way.

The choice of accounts structure may be made by the NGO that you are working for – and if so, it must be used. However, some external donors have strict accounts structures that must also be accommodated. If you are receiving external funding for your project, then this must be looked into, as early as possible. You can save a lot of pain later on, by setting up an appropriate accounts structure. *See Chapter 10.*

ANNEX FOUR: **MORE ON BUDGETS – THE PRACTICALITIES**

To best learn from this section, print out the Excel spreadsheet "budget.xls" which accompanies this manual.

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An approach to drawing up a budget

EXAMPLE: **HARGEISA SCHOOLS DEVELOPMENT PROJECT**

First print out the Excel spreadsheet 'budget.xls'. The budget is a good one. It has the following characteristics which you should follow:

- The Budget details include basic information about the project, including the name; the period covered in the project; the currency used; clear labelling of the currency on each costs column; a "Code" column with accounts codes clearly marked;

- The “Description” column has a short description for each type of cost which should be as detailed as possible, and is unique for each item. For example, for staff, it has “ School Outreach Officer 1” and “School Outreach Officer 2” on different lines, rather than just one line ‘Outreach Officers’. A good rule of thumb is to go for more detail rather than less, if you are not sure how to describe a cost. Descriptions are as precise as possible. For example, ‘electricity for the office’ is much more useful than ‘power’.

- There are ‘other’ lines at the bottom of each section of the budget. This ensures that there are accounts codes for unforeseen expenditure. This means that the accounts codes do not have to be stretched when unexpected things happen – which they surely will.

- The units written in the “unit” column were chosen to correspond to how you will actually make payments for each item. This means that there will be different units for different items. You should not try to set units (e.g. the monthly cost) for the whole budget: this will only cause confusion for some items.

- The budget includes the time scale as well as the service. This means that it uses "composite units" – e.g. a ‘person-day’. For example, this would be the best unit to use for a consultant who will be working for ten days on a project.

Total Cost

The total cost column should be filled in with the ‘unit cost’ multiplied by the ‘quantity’. It is extremely important that all lines really do have this calculation made on them. If the numbers do not add up, then it is very hard to have any faith in the budget, or to adjust the budget.

(For example, suppose a budget showed 5 bags of cement, each with a unit cost of $20, having a total cost of $80. It is impossible to tell if this means that each bag could actually be bought for $16, or if only 4 bags were bought for $20 each. So, it is impossible to adjust the budget to changing circumstances. The total cost must be 5 x 20 = $100.)

Notes

Any notes about how a figure is arrived at (either the cost or quantity) should be written in the ‘notes’ column. This column is often not included in budgets. It always should be. Without it, it is impossible to know exactly why the quantity (or the unit cost) shown on the budget has been chosen. Every line should have a ‘note’ written alongside it. For example, if 5 air flights have been budgeted for, the note should explain why there are 5 flights, and not 4 or 6. Without a good record of the decisions taken in drawing up the budget, it is impossible to adjust the budget. This severely limits the use of the budget and the quality of financial management possible.

It is always useful to write more rather than less in the notes column. However, these notes do not have to be huge. They just have to be enough to explain the numbers given in the other columns of the budget. It cannot be stressed enough how important this information is.

EXERCISE FOR WOMEN WORKING IN NGOS:
Many women say "I'm bad with numbers" and " I can't do sums". Many of us were laughed at when we were small or told that nice girls were not good at maths. Forget about all that. Get a cheap pocket calculator, find a quiet corner or earplugs, and you will be able to do a budget or make a plan using numbers as well as anyone. Here is an example of a Focus Group Discussion from the Needs Assessment Annex (*Annex One*):

***"In three villages in Somalia, 19 women talked about their pregnancy history; between them they had had 136 known pregnancies leading to 79 living babies, some of whom died afterwards. The causes of the miscarriages suggested malnutrition and anaemia, malaria and sexually transmitted diseases. The women were still sad at their losses but glad to have had the chance to have their stories listened to"*.**

Now work out how many pregnancies on average the women had.

Then work out how many live births they had on average.

Now, try a percentage. What percentage of pregnancies led to a live baby?

<u>This is how to calculate it:</u> take the smaller of the two numbers, 79, and multiply it by 100. Then divide the result by the bigger number (79 x 100 = 7900. Divide by 136 = ?). It is not easy, but if you go slowly and do everything twice you can do it.

(Answers: 7; 4; 58%). *Well done!*

MANAGING THE MONEY

10.1 Managing the money

What is Financial Management?
Financial management involves planning, organising, controlling and reporting on the financial resources of an organisation to achieve organisational goals.

10.1.1 **Managing scarce resources**

NGOs must ensure donated funds and other resources are properly utilised to achieve the organisation's mission and objectives. Financial management equates to maintenance of a vehicle – if we don't put in the right fuel and oil and give it a regular service, the functioning of the vehicle suffers and it will not run efficiently. If neglected, the vehicle will eventually grind to a halt and fail to reach its intended destination.

Managing risk
All organisations face internal and external risks which can threaten operations and even

survival (e.g. funds being withdrawn, an office fire or a fraud). Risks must be managed in an organised way to limit the damage they can cause. This is done by establishing systems and procedures to bring about financial control.

Managing strategically
Financial management should not be seen as a separate activity left to finance department staff. It is of strategic importance and must be incorporated into all aspects of operational management.

10.1.2 **What is financial control?**

Financial control is a state of affairs which ensures that the finances of an organisation are being properly handled. The concept of financial control is at the heart of financial management. It is achieved by designing systems and procedures to suit the particular needs of an organisation. Without financial control:

- assets are put at risk,
- funds may not be spent in accordance with the organisation's objectives or donors' wishes, and
- the competence of managers and integrity of the organisation may be called into question.

10.1.3 **Why is financial management important for NGOs?**

In many NGOs, financial management takes a low priority. Financial planning and monitoring systems are often inadequate. But NGOs operate in a changing and competitive world. To survive in this challenging environment, managers need to develop the necessary understanding and confidence to make full use of financial information.

10.1.4 **Good practice in financial management can do the following:**

- help managers to be effective and efficient stewards of the resources to achieve objectives and fulfil commitments to stakeholders
- assist NGOs to be more accountable to donors and other stakeholders
- gain the respect and confidence of funding agencies, partners and those served
- give the NGO the advantage in competition for increasingly scarce resources
- help NGOs prepare themselves for long-term sustainability and the gradual increase of self-generated funds.

10.1.5 **Getting the basics right**

Good practice in financial management is achieved by designing systems and procedures around the four key "building blocks". These are:

1 **Accounting Records**
Every organisation must keep an accurate record of all financial transactions that take place so that, as a minimum, it can show how the funds have been used. This is referred to as the *Financial Accounting* function.

2 **Financial Planning**
to the organisation's strategic and operational plans, the budget is the cornerstone of any financial management system and plays an integral part in monitoring the use of funds.

3 **Financial Monitoring**
Management accounts are internal reports produced so that managers can compare the organisation's progress against the budget and then make decisions about the future. *Financial statements* are produced periodically for outside checkers to demonstrate how funds have been applied in the past.

4 **Internal Controls**
Controls, checks and balances – collectively referred to as internal controls – are put in place to safeguard an organisation's assets and manage risk. Their purpose is to deter opportunistic theft or fraud and to detect errors and omissions in the accounting records. An effective internal control system serves to value and protect those who are responsible for handling the financial affairs of the organisation.

Effective financial control will not be achieved by a partial implementation of the building blocks. For example, there is very little point in keeping detailed accounting records if they are not checked for errors and omissions. Inaccurate records will result in misleading information, which in turn could wrongly influence a financial management decision.

10.1.6 **Financial Accounting versus Management Accounting**

For the financial management process to take place effectively, financial systems and procedures need to cover two aspects of accounting, financial accounting and management accounting. This is the day-to-day work of an accounts section. It describes the systems and procedures used to keep track of financial and monetary transactions which take place inside an organisation – recording, classifying and summarising financial data for various purposes.

The building blocks
Financial accounting records can be maintained either using a manual or computerised system (or a combination of both methods). Although it is important to comply with certain accounting conventions and standards, the actual system adopted will depend on a variety of factors:

- expertise and resources available
- volume and type of transactions
- reporting requirements of managers
- obligations to donors

One output of financial accounting is the annual financial statements, which are backwards looking and used primarily for accountability to those external to the organisation. The routine output of financial accounting throughout the year must be accurate and up-to-date in order for management accounting to be undertaken effectively and with minimum effort.

Management Accounting
This takes the data gathered by the financial accounting process, compares the results with the budget and then analyses the information to help make decisions about the future management of the organisation. The reports produced by the management accounting process – most commonly the *Budget Compared to Actual Report* and the *Cash flow Forecast* – are therefore primarily for internal use and are forward looking.

Financial reports for management must be timely, accurate and relevant. They should be produced on a regular basis – usually monthly or quarterly depending on the needs of the organisation – and as soon as possible so that figures are relevant to managers' discussions.

10.1.7 **Why accounts are produced**
There are several compelling reasons to produce accounts, including:

- For project management: so that managers know how much money has been spent, on what;
- The law requires it: all charities are required to produce accounts detailing their income and expenditure;
- Donors require it: donors wish to see how their money has been spent;
- For control purposes: to check that money is not going missing;
- For budget monitoring and planning: to compare actual expenditure against the budget, so that managers can be sure that there are funds to complete all project activities.

10.1.8 **Financial controls**
A few basic financial controls can greatly reduce the chance of money going astray, or of funds running out. These are described below, and include areas like authorising expenditure. It may not always be possible to implement all the controls. But, the more that you are able to use, the stronger your system will be.

Remember that preparing accounts and comparing them against a budget is an extremely important financial control in itself. Another fundamental control is making sure that people with the appropriate skills and experience are recruited for financial work, and that their responsibilities are clearly defined. This should be the priority when it comes to finding new staff to take on the accounts: find someone who has the right qualifications and experience, and make sure that they know what is expected from them.

10.1.9 **Segregation of duties**
A standard financial control is to make sure that different members of staff have responsibility for different accounting duties. This introduces a series of checks on all accounting work, and greatly reduces the possibility of fraud. The basic jobs to try to split up are: authorising payments, handling cash and recording transactions.

10.1.10 **Accounting Golden Rules**

- ∆ Record everything that you do. You must preserve an 'audit trail'. That means that another person must be able to follow all of your accounts just from what you have recorded, with no additional explanation.
- ∆ Be organised. Make sure that all documents are properly filed, and all procedures properly followed.
- ∆ Be consistent. If you do things one way in one month, then do them the same way in the next month (unless there is a good reason for changing them).
- ∆ Keep on top of the books. Do not let them go for more than a week without making sure that they are up to date. Fill in all the proper books as the transactions happen: do not let a backlog build up.
- ∆ Do not get stuck on one point. If one thing is being very difficult, then make a simplifying assumption that will allow you to move on. Make a note of it, and discuss it with your manager or an accountant as soon as possible.

FUNDRAISING

10.2.1 **Planning the funding needs of the NGO, including training needs**

Idealism and motivation are not enough to set up a good NGO. You need money and you need to plan well ahead. In this planning it is wise to work out approximately how much funding will be needed for the first two to three years. Taking into account the following issues can be very helpful:

- If there is a possibility for voluntary participation by your members, it may be a good idea to first start looking for funds for small concrete activities, like the salary of a counsellor, money for visual aids, or money for a workshop.
- Donors often like to find out first what your NGO is able to handle, before getting fully involved. By starting with a small collaboration, you can show your sincerity and the quality of your work. Donors will be more generous when you apply for funds the second time around.
- Donors often prefer to support short-term projects with clear objectives, and which contribute to the independence of the NGO.
- In your planning, sources from within the project should be taken into account. e.g. insurance schemes and income generating activities. With health care activities, patient charges can be made for consultations and treatment (allowing for the financial capacity of the patients). Other projects can produce income from saleable articles like water,

handicrafts or agricultural products. Although these funds will never cover all project expenses, they are important in your planning and also in building the self-sustainability of your projects.

- Donors are in general more interested in project costs (implementation of activities) than in organisational costs (overhead costs e.g. costs for telephone/fax, e-mail, postage, electricity bill, etc.). For that reason, always include an item line for overhead costs when submitting a project proposal. UNICEF admits to 14%, but 10% is reasonable for a very small organisation. However some donors do not like paying much towards this line. In that case, find out the donor's policy on overheads and adjust the proposal accordingly.

* You also need to discuss a contingency line with the donor. This means allowing some money for the possibility of plans going wrong. A post-disaster project, for example, may face inflation, fluctuating exchange rates, hikes in the prices of essential raw materials etc. The project can soon be way over budget. An allowance of 'unforseen' of 5 to 6% is normal in every proposal.

NGOs should resist having donors give them money in tranches. If they get the entire grant they can put what is not immediately required on deposit and earn the interest. You can also encourage donors to set up endowment funds as a good way to become gradually more sustainable or at least independent of that donor.

Indirect Funding can take the form of substitution of resources, e.g. secondment of personnel. Examples are where government staff are allowed to work for your NGO for a certain period of time, or the government allows the project to use its visual aids materials.

***** Be very clear and honest about the amount of money you need for one particular activity, from one particular donor *****

Remember that the building of a relationship of trust with your donor is just as important as the amount of money you ask or receive.

EXAMPLE: **A WORKSHOP ON FUNDRAISING FOR A HUMAN RIGHTS NGO IN LESOTHO**

This NGO (CLRAC) organised a Workshop on Fund-raising for both staff and Board Members. Together, over three days, the participants worked through the following:

- a brief evaluation of fund raising by CLRAC in the past years: conclusions;
- how to plan the funding needs for CLRAC and set realistic objectives for the period 2000-2002;
- development of a fund-raising strategy, including: planning/timing of projects and CLRAC organisational costs in need of funding;
- capacity assessment in CLRAC to conduct fund-raising; how to build in fund-raising capacity: human resources development and organisational development;
- how to target donors, local and international – and what their requirements are;
- how to write a proposal for project funding;
- an outline for financial reporting;

- a plan to write a Strategic Planning document for implementation of fund-raising by CLRAC;
- meeting with a Maseru-based donor representative

Because the Board members and staff followed the Workshop together, a feeling of commitment and co-working also developed; the Strategic Planning Document got written and some money has been raised.

10.2.2 **Accepting the mind-set that will help you succeed**

Non-profit organisations in the South are steadily becoming more professional. For NGOs seeking grants, one of the most important steps is a mental one. It is accepting that there are no quick fixes, no magic shortcuts. The steady, regular work of your organisation - your board members, your staff responsible for funding – all this will develop an effective strategy through many small steps.

Par of the process is to be clear about what you are – each of you, each a very special NGO – and to make that clear in the documents that go to the possible funder. A *Mission Statement* that is enthusiastic, imaginative and creative will help a lot. Can you answer the following questions clearly and directly?

- What is the unique purpose of your organisation?
- What are the basic needs that this organisation fills?
  (the target group it serves and how this organisation meets the needs of the beneficiaries)

10.2.3 **Finding the agencies with funds**

Research on any funder's stated programme interests is essential. Do not attempt a scatter approach, sending requests to a wide group of organisations. It can damage your organisation's credibility. You are trying to identify the few funders that have interests that are in line with your organisational and project objectives. Here is a guide to research into funding: if you do not qualify, do not apply. Many funding agencies now have web-sites so look them up and see what they say.

Funder research is a two-step process. The first step aims to develop an initial 'prospect' list of some 10 to 15 funders who have general interests in the subject area of your organisation or project. The second step involves further research and refines this list to the 3 or 4 funders you may approach.

Sources for funding can be found within your country as well as abroad. Local funding has a number of advantages. The procedures are often easier to follow. And international donors want to know that local sources have been tried first. When applying for funds from abroad, the national registration of your NGO and formal approval of your project by your government, is often necessary.

Locally, the main institutions to apply to for funds are:

- *Local organisations*
  Think of Rotary or Lions clubs, churches, temples, mosques, hospitals, local business associations, the 'rich' in your community etc.

- *Government or District institutions*
  Funds are often available, especially if working in co-operation in the same field of interest. Think also of secondment of staff, use of their logistics etc.

Possible sources from abroad include:

- *Voluntary funding organisations*
  These include missions, aid agencies and other groups, both religious and secular. Most of them are based in the North, in Europe, North America and Australia. Such groups are often interested in supporting smaller-scale development and health projects. A list of names can be obtained from national and voluntary organisations and from embassies.

- *International Aid organisations.*
  These include the United Nations Agencies such as WHO, UNICEF, UNDP, FAO, the European Commission (EC), the World Bank (WB), Asian Development Bank (ADB). However, they do not often support small-scale projects directly. Funds from these sources are more likely to be available via national umbrella organisations. It is worth finding out what their contributions in your country are, to the government and to bigger NGOs. This information will be available from your government (ministry) or from local UN and EC delegations etc.

- *Foreign Embassies*.
  They often have funds available for small-scale projects. (For example, Dutch Embassies have special funding sources for so called KAP projects. From these sources they can give direct support to projects with sums up to $20,000. Special procedures/criteria need to be followed).

10.2.4 **How to apply for funds**

1. Select your funding source. Try to get as much information as possible about the ins and outs of that organisation, its procedures for application and so on. Find out which person to approach within the organisation, so you can address them personally. This works best via mutual contacts.

2. Write a letter using your personal title to the person dealing with funds. Introduce yourselves in the letter and give a brief explanation of your organisation, its objectives, your intentions with respect to funds. Ask for the procedures you need to follow. Always make a copy of your letter to keep. If your source is local, give the person you addressed a phone call about one week after you mailed the letter and ask if was received. This is not only to make sure that the post is working, but it is also an excuse for exchanging more

information. Personal relationships are very important in fundraising. By making a phone call, you get a chance to find out they kind of person they are and to show your own involvement and motivation.

If you are approaching an international donor, follow your letter up with an e-mail message if possible, just to make sure that your application has been received and again to show your own motivation.

3 While waiting to find out the procedures to follow, you can prepare the information the donor will likely want to know. Most will expect brief details of the following:

- Aims and objectives of your organisation.
- Details of the target population
- Number of people/villages you want to reach
- Social structure of the communities, including details of local employment, income levels, high risk groups etc.
- Details of the project area, its location, terrain and climate.
- Your relationship with other organisations e.g. other NGOs and the Government and your intended co-operation with them.
- Names and qualifications of your staff members
- General plan of the implementations of your activities.
- Budget:
  - Include a budget for the first year.
  - Estimate expected funds from other sources.
  - Be concrete about the funds you are asking for.
  - Include in your budget items that are essential, but do not ask for expensive or unnecessary equipment.

If you follow all the guidelines and still your organisation does not get the grant it needs, remember that the funding agency has a hundred applications for every slice of money. Citizens Associations are increasingly turning to the independent funding community to assist their work and consequently the numbers and quality of projects – and their accompanying grant proposals – are increasing. So do not take the rejection personally. The percentage of proposals being failed is 90%, so do not be put off; you can learn from failure. Write a brief letter or email to the funder asking the reasons for the rejection. The answer may suggest how to improve the proposal, or even request an improved resubmission.

EXAMPLE:

I (FA) am a black woman from the South, living presently in the Netherlands. I am the founder of an NGO based both in the Netherlands and in Somaliland. In 1995 I came to the Netherlands as a refugee. The civil war had left me unable to stay in my homeland, a bankrupt, my house and small factory burnt to the ground.

During the months I waited in Europe to be either granted residential status or rejected, success in business no longer seemed important. Instead I decided to focus on making a difference. I began talking to other Somalis who shared my passion. The concept of our NGO gradually took shape with the purpose of advocacy for the internally displaced in Somaliland. On 7 November 1997, Doses of Hope was formed.

Finding the money, though was a major problem We were newcomers. We had set up an NGO in the heart of Europe. We started knocking on doors and encountered every obstacle and rejection - one reply said "we have received your letter and understood its contents but unfortunately we think neither our organisation nor any other organisation in the Netherlands would support your initiative". But we succeeded in finding partners – highly respected partners.

So remember the three Ps: Persistence, Patience and Pursuing.

10.2.5 **Co-operating with funding organisations**

Building a good trusted relationship with your donor is very important. Often, co-operation is not easy. The donor asks for long and complex reports, and transfers of funds are often delayed. Communication problems are common because of misunderstandings from both sides and because of postal delays. Don't forget that donors are dependent on their own supporters, who in turn will expect reassurance that their money is being well spent.

Ways to improve co-operation are:

- After receiving funds, write a letter of acknowledgement and thanks.
- Send regular reports as requested by the donor.
- Prepare accurate budgets, and keep costs as low as possible.
- If two or more donors are supporting your project, than the area of support should be clearly defined and communicated.
- Encourage the donors to share a single global report and accept each others' tour reports to reduce the amount of time you spend on their requirements.
- Always give feed-back to the donor on how the money was spent.
- Always stick clearly to the objectives of your NGO.
- If there are any major changes of plan, inform your donor.
- Welcome visitors from your donor agencies.
- Try to reply promptly to letters from your donor.

10.2.6 **Building fundraising capacity**

∆ Develop a fundraising policy and regulations for your NGO.

∆ Set up a fundraising committee, with clear job descriptions (responsibilities, tasks).

∆ Monitor these fundraising activities periodically

∆ Look again at the outline of the funding workshop in Chapter 10.2.1.

ANNEX FIVE: **MORE ON THE PRACTICALITIES OF ACCOUNTING**

To best learn from this section, print out the Excel Workbook "accounting.xls" which accompanies this manual. The workbook contains 8 spreadsheets which are good examples of the accounting records discussed here.

Remind yourself why accounts are produced:

- For project management: so that managers know how much money has been spent, on what;
- The law requires it: all charities are required to produce accounts detailing their income and expenditure;
- Donors require it: donors wish to see how their money has been spent;
- For control purposes: to check that money is not going missing;
- For budget monitoring and planning: to compare actual expenditure against the budget, so that managers can be sure that there are funds to complete all project activities.

Recording transactions

Cashbook:
Payments and receipts are referred to as transactions. All transactions must be properly recorded in a cashbook. The cashbook is the most important single accounting book. If you do not keep any other accounting records (apart from the receipts), then you should keep a cashbook. It sets down the basic information used to build up a complete set of accounts.

The following details must be entered in the cashbook for each transaction: the date, a description, the reference number (see later), and the amount.

The sheet “Cashbook” shows the cashbook for a new field project. It is important to note that this is just one example of how a cashbook can be laid out. Cashbooks can be set out differently, for instance with receipts and payments laid out in adjacent columns, in the same table. However, they always contain the same basic information.

The first entry recorded in the January sheet (1st Jan 2000) is the $20,000 cash, which the Office Manager brought from the UK Head Office in order to set up the field office. From the point of view of the field office, this is income. (Previously there was no money in the office cash account. Now there is $20,000.) So, this is recorded on the left hand side, in the receipt section.

In January a donation of $2,000 was also received. This means that total receipts for the month were $22,000. In the same month, a total of $7,000 was spent, as payments on rent, materials, electricity and salaries. Deducting the total payments from the total receipts gives the amount remaining at the end of the month (i.e. $22,000 - $7,000 = $15,000). The $15,000 is called the *‘balance carried forward’*. This is because it is the balance of money carried forward to the next month, February.

This 'balance carried forward' should be the same as the amount of money in the safe at the end of the month. If it is not the same, then either a payment or a receipt has been made but not recorded in the cashbook, or money has been taken or added to the safe.

(This exercise of comparing the amount of money in the safe to the balance in the cashbook is known as a *'cash reconciliation'*, and should be carried out at the end of every month. Record the findings of any cash reconciliations that you perform on a cash count form (see example on sheet "Cashcount"). Include an explanation for any differences between the balance on the cashbook and the amount of money in the safe.)

Moving down the example to the February accounts, the first entry is the 'balance brought forward' from January (i.e. $15,000). This is the starting position for the month. It is extremely important that the balance brought forward in one month is exactly the same as the balance carried forward from the previous month.

(There was no balance brought forward for January, because the office did not exist before January. It did not have any funds to 'bring forward'.)

During February, $300 of additional income is received, and a total of $14,250 payments is made. So, the balance carried forward at the end of February is $1,050, and this should be the amount in the safe on the 28th February.

Bankbook:
In the example, the new field office starts up holding all its money in cash. However, in February the Office Manager decides to open an account at a local bank. She is then able to make payments using a cheque book as well as by using cash, and to hold the office's funds in the bank.

So, the Office Manager has to keep a separate accounting book to record the details of bank transactions. An example of this is shown in the sheet "Bankbook". (There has to be a separate accounting book for each 'pot' of money used by the office: the cashbooks, and the bankbooks, should described exactly what is happening in the cash accounts and the bank accounts.)

The 'bankbook' has almost exactly the same format as the cashbook. The only difference is an extra column used to record the cheque numbers of all payments made. In fact, the term cashbook is used loosely. It can refer to a book detailing either cash transactions or bank transactions. The term 'bankbook' is used here to distinguish it from the cashbook.

The office's bank account was opened with a deposit of $10,000, taken from the cash account. It is important to see how this is shown in the cash and bank books. In the cashbook it is recorded as a payment. This makes sense, because the cash account is $10,000 worse off. (Without this entry, the balance carried forward in the cashbook would be $10,000 higher than the amount in the safe.) In the bank book, the amount is recorded as a receipt. This also makes sense. Previously there was no money in the bank account, and now there is $10,000.

It is important to remember that transfers made between cash and bank must be recorded in both account books. In the example, cash is deposited in the bank. But, it is also true for cash that is withdrawn from the bank and held in the cash account.

The bankbook is completed in exactly the same way as the cashbook. In the example, cheque payments totalling $5,225 are made during February. $15,000 of income was received by bank transfer from Head Office, in addition to local income of $1,200. Together with the $10,000 deposited from the cash account, this means that total income received in the bank account (during February) was $26,200. So the balance carried forward at the end of the month was $20,975 (=$26,200 - $5,225).

Bank reconciliation:
The cash reconciliation confirmed that all the cash transactions were properly recorded in the cashbook. A similar check can be carried out for the bank account. Instead of comparing the balance in the cashbook to the amount of cash in the safe, the balance in the bankbook is compared (reconciled) to the balance on the bank statement. This is known as a 'bank reconciliation'.

A bank statement is a list of transactions produced by a bank, showing all the payments and receipts on an account over a period of time, and the amount held at the end of that period. See the sheet "Statement" for the bank statement received by the field office at the end of February.

The balance in the bankbook may not be the same as the amount on the statement, even if transactions have been properly recorded. There will probably be a number of timing differences. For example, a cheque payment made in the last couple of days of the month will be recorded in the bankbook. But the cheque may not have been presented to the bank and processed by the bank. So it might not appear on the bank statement. Or, money paid into the bank during the last few days of the month may not appear on that month's statement. There may also be some transactions on the bank statement that have not been recorded in the accounts. A common example is bank charges, which are deducted directly from the bank account.

So, it is necessary to check whether each transaction appears on the bank statement and in the bankbook. This can be done by ticking transactions off the statement, and seeing if they appear in the bankbook, and then by ticking transactions off the bankbook and seeing if they appear on the statement. It should then be possible, using transactions which are only recorded in one place, to reconcile the balance in the bankbook to the balance on the statement. See the sheet "Reconciliation" for an example.

Multiple currencies:
As explained above, separate books must be used to record cash and bank transactions. Separate books must also be used for each currency that is used. This allows you to keep track of the balance of each fund of money that you are using. (For instance, suppose you have 4,000 dollars and 14,000 Kenyan Shillings. You cannot account for both the dollars and the shillings in one cashbook – otherwise you would be trying to add up different currencies, which soon becomes very complicated, or meaningless.)

Payment vouchers (reference numbers):
In a cashbook, each transaction is given a reference number. For payments, this is done using payment vouchers.

Every payment should be documented on a payment voucher. This voucher must state: its own unique number (they should be numbered sequentially), the date of the payment, the payee (the person receiving the payment), a description, the amount of the payment and the accounts code. It should be prepared before the payment is made, and it can also be used to authorise payments. However, it is better practice to use separate authorisation forms for this.

The basic purpose of payment vouchers is to assign a unique number to each payment. This number is the label that finance staff use to track the payment through the accounting system. It is often necessary to do this, especially when problems crop up. If no printed payment vouchers are available, then you can make do by assigning each payment a number. For instance, you might choose to use the sequence "Jan01, Jan02, etc". This fulfils the vouchers' basic function.

Payment vouchers should be produced in duplicate. The first copy should be filed in the accounts records, and the second copy should be left in the payment vouchers book. This means that there is an extra record of all payments made in the vouchers book, along with the record in the cashbook.

Every payment must also be supported by a receipt, and an invoice where available. The receipt is the proof that payment really happened, and that the goods or services were really bought. The invoice describes the goods or services that were actually received. When there is no invoice, the goods or services received should be described on the receipt. Receipts should be filed, as described in the following section, "Supporting Documents".

Receipt vouchers:
Any income received should be documented on a receipt voucher. This must state: its own unique number (numbered sequentially), the date of the receipt, the payer (the person giving the money), a description, the amount and the accounts code.
Receipt vouchers should be produced in triplicate. The payer should be given one copy, signed by the person who received the money. This is their proof that the money has gone to your specific organisation. The second copy should be left in the receipt vouchers book, and the third should be filed in the accounts records.

Books of receipt vouchers should be stored in a secure place. Otherwise, anybody could use them, apparently receiving money in your organisation's name.

Supporting documents

All transactions must be recorded in cashbooks or bankbooks (as described above). However, each transaction must also have supporting documents filed for it, as well. Supporting documents include receipts, payment vouchers and authorisation forms. These files of supporting documents are a crucial part of any set of accounts.

There should be a separate file of documents for every month, with dividers in it for each different currency (and for cash as opposed to bank accounts). The documents filed for each transaction should include: authorisation (which could be on the payment voucher), the payment voucher, and receipts or invoices, all stapled together. The documents should be filed in order of payment voucher.

It should be easy to find the supporting documents in the files for any entry in a cashbook or bankbook. So, any accounts office is likely to have monthly files of supporting documents along its book shelves.

Producing accounts

Recording transactions is the basis of book-keeping, and one of the most important parts of any accounting system. However, on their own cash and bank books only have limited value. They only give details of individual transactions. They do not provide any overall picture of how much money was spent on what, and where money was received from. To do this, the information contained in the cashbooks must be summarised.

The sheet “Summary” shows a summary of the receipts and payments made by the field office in January and February. The information has been drawn from both the cashbook and the bankbook, and the income and expenditure has been summarised, using categories. From this, it is easy to see how much has been spent and received. It provides a clear breakdown of how the money was spent, and where it came from. This is useful for the project manager, who can monitor the overall financial situation.

When transactions are made in a number of currencies, you have to convert them all in to one common currency before you produce accounts. As discussed before, it does not make much sense to add dollars to shillings, for example.

Accounts codes:
The categories used to summarise cashbooks are labelled with ‘accounts codes’. Any set of categories can be used to summarise a project’s income and expenditure. For NGOs, the expenditure codes are generally the most important ones. They can be set up according to geographical region (for instance, expenditure in the North, South, East or West), according to project (for instance, expenditure on health education or agricultural support), or according to type of expenditure (for instance, staff costs, transport or agricultural tools).

Often, codes will use a mixture of these different frameworks. (This can give rise to long codes.) Any codes at all can be set up and used. However, the same codes must be used on the budget as all subsequent accounts. So, accounts codes are defined when the budget is written.

You must always consider the needs of people who will use the accounts when you are setting up accounts codes. The codes define what information will be produced. Will that information be useful for the people who use the accounts? These people include the project management, the NGO head office accountants and any external donors.

Some of the users have fixed, inflexible requirements. So, their standard accounts codes must be used. This is likely to be the case for the NGO head office accounts systems, and for some external donors. This is discussed further in the '*Donor Reporting'* Mango Accounting Pack

It is important that every transaction recorded in the cash and bank books is properly coded. For this, an extra column is required on the cash and bank books. See the sheet "Codes" for an example, applying codes to the January and February cashbooks.

Accounts summary:
The cash and bank books can be summarised using the accounts codes. This allows accounts to be produced. An example of a simple accounts summary is given on the sheet 'accounts summary'. You can see how the information produced here is useful for managers, and how it could easily be compared against an overall budget.

Financial controls

A few basic financial controls can greatly reduce the chance of money going astray, or of funds running out. These are described below, and include areas like authorising expenditure. It may not always be possible to implement all the controls. But, the more that you are able to use, the stronger your system will be.

Remember that preparing accounts and comparing them against a budget is an extremely important financial control in itself. Another fundamental control is making sure that people with the appropriate skills and experience are recruited for financial work, and that their responsibilities are clearly defined. This should be the priority when it comes to finding new staff to take on the accounts: find someone who has the right qualifications and experience, and make sure that they know what is expected from them.

Authorisation:
Every item of expenditure must be authorised. This is necessary to ensure that those with responsibility for expenditure are able to maintain control. The Project Manager, for instance, is normally responsible for ensuring that expenditure remains within budget. This would be outside his control if any of the staff could authorise payments. (For instance, money could be spent inappropriately.)

There must be clearly stated procedures agreed by the Project Manager, who is responsible for the budget, setting out different authority levels. For instance, the Office Manager might be allowed to authorise cash payments of up to $500. Payments for more than $500 would have to be authorised by the Project Manager (or a designated deputy in the absence of the project manager). It is generally also necessary to have different forms to authorise different types of transactions. (For instance, there might be a specific 'float request form' used to request and authorise floats.)

Security:
It is clearly very important that any cash in the office is kept secure, usually in a safe, or at least in a strong cashbox. Access to this should be restricted to one person. Cash held in the office should be restricted to a minimum. Money should be withdrawn from the bank, or obtained from Head Office, only when it is required.

Cash and bank reconciliations:
If regular cash and bank reconciliations are carried out, then you know that the accounts are recording reality: that if the accounts say that you have $100 of cash, then you really have $100 of cash. This is a fundamental control, and must be carried out at least every month.

Segregation of duties:
A standard financial control is to make sure that different members of staff have responsibility for different accounting duties. This introduces a series of checks on all accounting work, and greatly reduces the possibility of fraud. The basic jobs to try to split up are: authorising payments, handling cash and recording transactions.

Accounting Golden Rules

- Record everything that you do. You must preserve an 'audit trail'. That means that another person must be able to follow all of your accounts just from what you have recorded, with no additional explanation.

- Be organised. Make sure that all documents are properly filed, and all procedures properly followed.

- Be consistent. If you do things one way in one month, then do them the same way in the next month (unless there is a good reason for changing them).

- Keep on top of the books. Do not let them go for more than a week without making sure that they are up to date. Fill in all the proper books as the transactions happen: do not let a backlog build up.

- Do not get stuck on one point. If one thing is being very difficult, then make a simplifying assumption that will allow you to move on. Make a note of it, and discuss it with your manager or an accountant as soon as possible.

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