FINANCIAL MONITORING & REPORTING

Process Management

Process Owner	Chief executive officer
Department	Executive Management
Document level	Policy
Approval level	Board of Directors

Review History

Amendment	Reviewed by	Date	Approved by	Date	Version

Signature for Approval:

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Chief Executive officer (CEO) **Chairman of the Board**

1. Introduction

The financial monitoring and reporting policy for MaSP sets out some guidelines on financial monitoring and reporting. Financial monitoring will be based on the accounting system and records as well as budgets. One of the main reasons for keeping accounting records is that information about how the Organization 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 MaSP financial affairs. The policy will facilitate timely financial reporting, accuracy and relevance. Financial reports are needed primarily by those responsible for managing the Organization and by current and potential donor agencies; but those responsible for financial management of MaSP also need to 'give an account' of their stewardship to a wide range of stakeholders.

The Board of Directors need financial reports to oversee the finances of the Organization. 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. MaSP is sharing financial information with its members 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 organization 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 MaSP (such as unaccounted working advances) and owed by MaSP (e.g. to suppliers' / tax authorities).

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

2. Users of financial reports

- Board of Directors – To keep an eye on how resources are being used to achieve the Societies objectives.
- CEO and Senior Management Team – To keep an eye on how project funds are being used, especially compared to the original plans. To help plan for the future.
- Project staff – To know how much money and resources are available for their projects and what has been spent so far.
- Finance staff – To make sure that there is enough money in the bank to buy the items MaSP needs to run its programmes
- Donors (Scottish Government) – To make sure their grants are being used as agreed and that the project's objectives are fulfilled. To consider whether to support an organization in the future

- Governments departments – To make sure that MaSP pays any taxes due and that it does not abuse its status as a 'not for profit' organization.
- 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.
- General public – To know what MaSP raises and spends during the year and what the money is used for

3. Internal financial monitoring & reporting

At the beginning of each financial year the Finance and Administration Officer (FAO) will set deadlines for reconciliations and reporting. It is the responsibility of the relevant officer at respective level to ensure that the necessary reports are prepared. The relevant accountant/ administrator is responsible for producing the reports.

a. Monthly reports

Monthly reports are prepared for the office and the Finance officer communicates the cut-off dates for respective month-end process at the beginning of the fiscal year. The officer at respective level shall make sure that such cut off procedures are being followed and that all expenditure and income relating to the period for which the report is prepared are included. This facilitates budget vs. actual expenditure comparison both for projects and general office income statements.

b. Preparation of monthly accounts

It is imperative that all monthly reconciliations and month-end procedures are prepared and captured in QuickBooks before producing the final management accounts. This is in recognition of the fact the reconciliations have a major impact on account balances and income and expenditure. Reconciliations are performed as described in the section above for bank accounts, petty cash, major debtor and creditor accounts, payroll, statutory deductions, VAT, stock balances, prepayments such as deposits, accruals, fixed deposit accounts, control accounts and ledger accounts.

Once all reconciliations have been performed, the starting point for the monthly financial report should be the printing of the general ledger for each project. The GL shall be forwarded to the budget holder by the 7th working day of the following month. The GL is checked by the budget holder / manager or the relevant accountant/ administrator for unusual or material changes. The review is also to ensure that all entries have been posted with the correct Pastel codes.

c. Adjustments

All accounts that require correction and reconciliations should be done after the first GL print out. As part of the adjustment stage, all accruals and provisions should be captured. All adjusting journal vouchers need review by the relevant accountant/ administrator and approval by the budget holder / manager or CEO. Adherence to the Organization's authorization limits should be exercised for these approvals.

d. Production of accounts

After all corrections, adjustments and account reconciliations have been done; the relevant accountant/administrator should print a final trial balance and general ledger. The final trail balance shall be dated and signed by the relevant manager / budget holder.

Monthly management accounts consist of Income Statement, Balance Sheet, Cash Flow Statement and Budget Monitoring Reports (budgetary analysis).

The variance reports are an effective tool to monitor performance on a monthly basis. They allow the senior management and the Head of Structures / Departments to take corrective actions at an early stage prior to the fiscal year end or the end of the project implementation period. The variance report also serves to explain deviations from budget in MASP consolidated financial statements and assists the FM in his/her presentation to the Board.

Variance reports are produced monthly, at national level for each project for which a budget has been approved to ensure a full picture of actual expenditure against budgeted costs and activities. At provincial and branch level, it is the responsibility of respective manager, with the assistance from the finance officer(s), to produce variance reports. The manager shall seek explanations from the project managers for any significant deviations between budgeted and actual expenditure.

The level of significance is currently [+/- 10% Explanations will be forwarded to the National Office. For donor funded projects the [+/- 10% apply unless lower amounts have been agreed with the donor. The project budget holders will ensure that there is consistency between the project financial and narrative reports and reasons for budget deviations should also be included in the narrative reports.

e. Authorisation and review

FAO and the relevant accountant/ administrator review the financial reports and statements. Should errors be found at this review stage, adjustment will need to be done via journal entries. After all branch reports have been approved as correct, can the provincial office run a consolidated set of financial reports and statements. At national office, MASP consolidated reports and statements are produced once all provincial reports have been approved. The set of reports at each level are printed, dated and signed by the relevant manager. A copy of the monthly management reports is filed.

f. Quarterly reports

At the end of every quarter, quarterly financial reports shall be prepared within the deadlines communicate by the Finance Admin Officer at the start of each fiscal year. Quarterly financial reports consisting of Income Statement, Balance Sheet, Cash-flow Statement and Variance Report. These reports are prepared for each office at each level (national, provincial and branch)

After the draft financial statements have been extracted, copies shall be distributed to the CEO, within 30 days after the end of previous quarter. The CEO will check and agree with the finance department as to the correctness of the statements within one week following receipt of the drafts.

After agreement or in case of non-communication from the program manager and budget holders a final copy of the financial statement shall be produced and distributed to the same officers together with a variance analysis and report.

The final quarterly financial report shall be completed within 30 days after the end of previous quarter and the period shall be closed in the financial system.

In connection with the quarterly report, a statement of affairs is prepared for each programme, indicating opening balance for the period, funds received, total expenditures and the new closing balance, and a specification of the composition of the balance i.e. cash, bank balances, accruals, outstanding advances etc.

g. Budget Monitoring Reports

The report takes the budget for the reporting period (preferably the phased budget) and compares that with the actual income and expenditure for the same period. The difference between the budget and the actual result is known as the variance 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. The budget monitoring report also show variances as percentages.

How to Calculate Percentages:

The budget variance percentage can be calculated as follows:

$$\frac{\text{Budget variance \$}}{\text{Budget for period \$}} \times 100$$

Under-spends will result in a positive % and over-spends will produce a negative %

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.

Key areas to focus on when you pick up a Budget Monitoring Report include:

- What is the accounting basis of the report – is it compiled on the cash or accruals basis? Are there outstanding commitments? If so, how does that affect the results?
- What does the bottom line tell you? Overall, is the budget overspending or under-spending and is it significant at this time in the life of the project or programme? 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' (i.e. budget items in the same area, such as Staff costs or Admin costs)? 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 overspent.
- Do not just concentrate on over-spending – remember that under-spending is just as critical for MASP.
- Do linked budget line items (e.g. 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?

h. Variance analysis

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 described as favourable (i.e. generally good news) and negative ones as adverse (i.e. generally bad news). A positive variance happens when:

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

However, note that a budget under-spend is not always 'good news' for MASP as this could be because activities are not on target and this may be a cause for concern for the donor.

A negative 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 may be due to an error in the figures, for instance a mis-coding in the accounting records (which is effectively a change in quantity compared to the plan).

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 – e.g. 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
- Scottish Government rules and conditions.

Senior Management of MaSP must meet monthly to discuss all variances during the finance meetings and agree on the action to be taken.

i. Cash-flow monitoring

The cash-flow report is the cash-flow 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 cash-flow include:

- Exercise good credit control – chase debtors for prompt payment
- Review grant schedules – encourage payment in advance rather than in arrears
- Bank all money received daily
- Request special payment terms from major suppliers (and stick to them)
- Pay certain overheads by instalment – e.g. insurance premiums
- Prioritize major payments
- Defer action that will lead to additional expenditure – e.g. recruitment, taking on leases, purchasing equipment

j. Integrated reports

Every quarter a report shall be written for each structure within MaSP. The report together with the quarterly financial and variance reports form an Integrated Report. Such report shall identify programming achievements and constraints during the quarter under review and shall explain material deviations from planned activities and the financial impact of those variances. It is the responsibility of respective manager and budget holder to ensure that the narrative part is in line with the financial report and that there are no inconsistent/contradicting statements in the report.

Approved accounts are passed to the Audit Finance and HR Committee for review before submission to the Board of Directors for approval.

These Integrated Reports are shared with the relevant structures in MaSP and sent to donors (as agreed between MaSP and the donor). They form the main channel of regular reporting within the MaSP structures and with the donors and other interested parties.

k. Year End reports

Well in advance of the fiscal year end, the Finance and Admin Officer will circulate a timetable and checklist to all officers detailing the year-end tasks to be performed at the different structures and deadlines for completing each task.

The monthly management accounts reports produced over the period "year-to-date" should be an approximation of the year-end accounts.

l. External financial reporting

i. Donor reporting

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.

ii. 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 – i.e. 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.

iii. The donor report

Donors require that MaSP 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.

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.

iv. 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 MaSP.

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.

v. Audit

MaSP has migrated from cash basis to hybrid method which includes cash and accrual basis. This method will result in the production of the financial statements. The two main reports relevant to MaSP are:

- The Income and Expenditure report
- The Balance Sheet.

I. The Income and Expenditure report

The Income and Expenditure report shows the financial performance of MaSP over a period of one year.

It records as a summary:

- all categories of income received and expenditure paid in that year;
- all income not yet received but relating to that financial year; and
- all expenditure not yet paid but incurred in 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:

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

This excess figure is then included on the Balance Sheet under the heading Accumulated Funds. The accompanying Balance Sheet must be prepared as at the closing date of the period for which the Income and Expenditure Account is prepared.

II. The Balance Sheet

The purpose of a Balance Sheet is to disclose the financial position – or 'net worth' – of MaSP at a given date.

If the organization 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 organization was 'worth'.

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 the organization.

The Balance Sheet is in two parts.

- one part records all balances on asset accounts,
- the other records all balances on liabilities accounts plus the income and expenditure account balance.

Assets are classified into two parts:

- Non-current assets (fixed assets) – tangible and intangible long-term assets such as buildings, equipment, software 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.
- Current assets - 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.

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 considered to be very liquid, while money tied up in a building or a vehicle is clearly not liquid at all.

Liabilities are also divided into short and long-term liabilities:

- Current or short term liabilities – including outstanding payments, and short-term borrowings – i.e. those having to be paid within 12 months.
- Long-term liabilities – such as loans that need to be paid after 12 months.

III. What are the Annual Accounts?

These annual financial statements show in summarized 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 – and made ready for the external audit.

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

NB. The reporting templates could be added as appendices e.g. budget monitoring reports.