

1. Practical financial monitoring - your responsibilities

Trustees' responsibilities: Financial management is the responsibility of the board of trustees. The responsibility for appointing people to manage your money (the treasurer, the bookkeeper, the finance manager, your accountant) also rests with the board. The trustees are responsible for the information and the instructions these people are given to carry out their work. If things go wrong, the committee will have to carry the can. Most trustees know this, but it can be extraordinarily difficult to translate concern into suitably responsible practice.

Financial monitoring: Above all, the trustees are responsible for ensuring that:

- the organisation's money is secure
- all movements of money are properly recorded
- the organisation has and will continue to have the resources it needs to do its job.

Monitoring is a systematic means of achieving this. It is not a dead-end bureaucratic process, because the reports which are used by the trustees to monitor the *effectiveness of your financial systems and controls* are also essential for making *informed financial decisions* at policy and operational levels. You cannot control your organisation if you do not understand how it works.

Where monitoring fits in: A number of people have important roles in different parts of your arrangements for managing your money:

- day-to-day records will be kept by at least one employee or volunteer, the administrator or bookkeeper, who
 - keeps the basic financial records of money received, money spent, bills received,
 - looks after the banking of money and withdrawals from the bank
 - administers the petty cash system, if you have one
 - pays the staff's salaries and wages and keeps payroll records
- financial reports and plans may be prepared by the chief executive or manager or treasurer, who will put the raw financial information into a meaningful and understandable format – ie into balance sheets, income and expenditure accounts, budgets and budget reports
- monitoring – the trustees and the chief executive/manager will use these reports to *understand* the organisation better, ie to
 - assess the financial position of the organisation
 - guide them when making policy and spending decisions
 - help them look for any danger signs
 - pinpoint any defects in the way the records are kept and money is looked after.

The same people who monitor the financial reports will also be responsible for physical monitoring checks, ie ensuring that:

- the record books system or computer programme is being used correctly
- security arrangements to protect cash, cheques, purchasing etc are running correctly.

Understandable language: A key part of understanding your organisation is the accounting language which you use. This will vary greatly according to the experience and interests of the trustees. But there can be little doubt that very many boards of trustees cannot, and have no serious wish to, speak “accountantese”, the obscure language used by accountants.

So boards need a version of accounting language which they feel comfortable with and which does not turn half of them off when they pick up the monthly financial report. This requires support and training for trustees. But it also means that you should encourage your financial advisors to speak to you in language which most of you can easily understand, if they do not do so already.

2. Practical financial monitoring - how *NOT* to do it

Financial monitoring can produce a variety of negative attitudes among trustees and staff alike. It is as well to be aware of these before you start because lack of co-operation or understanding can wreck even the best system.

“Why bother with financial monitoring?” Some trustees see financial monitoring as a necessary chore, rather than a real job with a point. For the cynical, here are a few practical reasons for being serious about monitoring:

- if your organisation fails because the trustees did not keep proper control of its financial affairs you can be held personally liable for the losses. If you don't monitor regularly you cannot possibly be keeping proper control
- a busy but poorly monitored organisation can slump from apparent viability to insolvency in just a few months; this means that you can kill off your organisation with perhaps just a couple of board meetings where the chief executive or the treasurer present excuses rather than financial reports
- most chief executive officers and treasurers are scrupulously honest and competent enough at financial management for their charities to be 100 per cent safe in their hands without the board of trustees ever coming near them; but how do you know that this is the case in your organisation without monitoring?
- why would you all work so hard to set up and run your organisation, only to turn your back on it when it might need you most?

“If we don't have it, we can raise it”: Some committee members may be completely uninterested in good financial management. They are easy to recognise because, when you are considering the loss of a major grant cut, they suggest running a jumble sale. They are usually well-meaning and may be immeasurably valuable to the organisation in other capacities – which is their real danger, because it seems unkind to shut them up. You need to organise a training session without delay.

“Don't bother us”: There are many understandable reasons why individual trustees, or the board as a whole, may fail to monitor a project's finances properly. It helps to recognise them:

- “no one showed us how” – which is a training issue
- “we are too busy with other things” – a question of your group's priorities
- “we don't want to”, ie we are prepared to work hard as a volunteer on almost anything, as long as it is interesting, and finances are not – an issue of recruiting additional trustees perhaps
- “we can't” – it is realistic to work on the assumption that perhaps as many as half the members of any group can never be trained, cajoled or bullied into taking a serious and active role in monitoring the monthly financial reports.

“I have my reasons”:

- hiding a lack of skills: volunteers and paid staff are sometimes unwilling to admit they do not have the necessary skills, and they cover up by making excuses; you need to be aware of this and explain to people that it's nothing to be ashamed of; regular appraisals of paid staff should be geared to detect whether this is a problem
- hiding the truth: another much less common reason for producing inadequate financial reports is dishonesty; the merest suspicion of dishonesty can be so severely damaging to an organisation, whether or not it is justified, that *the board of trustees must remove any grounds for suspicion by insisting that full and open reports are presented to them every month.*

“We’re committed to monitoring, but we’re not very good at it” Here are some of the commoner mistakes made by groups which know they should monitor, but still can’t get it right.

- no financial report is produced this month because
 - you cannot find a reliable treasurer (you have not given the issue the right priority)
 - your manager or treasurer were too busy (they probably got their priorities wrong)
 - you are all too polite to ask
- the wrong information – small voluntary groups often have a fixation with monthly income and expenditure accounts, with the result that they never look at a balance sheet to check the health of their organisation
- irrelevant information – if you *tell* the committee the cost of the office toilet rolls rather than the costs of providing a your services then that’s exactly what they will discuss
- too much information – it is extremely common for an eager (or manipulative) managers to provide so much information that the trustees cannot sift out what is relevant and important, so you need to decide clearly what you need to know.

3. Practical financial monitoring - the basics

What financial information do you need?

The very basics: The following items aren't optional:

- a bank account
- accounts books or a computer programme for recording all financial transactions, income and expenditure and monthly totals
- someone to keep the cash book up to date and to prepare financial reports
- a realistic budget which shows you have sufficient income to cover expected spending
- a monthly meeting (the full board of trustees or a finance subcommittee or both)
- the "Financial Report" as an obligatory agenda item at that meeting
- a written financial report available to all members present in advance.

Ask the right questions: Information is no use if you don't know what you want to use it for. Here are the main issues you should be looking at when you discuss the financial report:

- What is your organisation's current position?
 - how much money have you got which is immediately available for you to use?
 - how solvent are you? ie if you stopped operating today would the organisation be able to pay all its debts
 - is your organisation getting richer or poorer?
 - what do you owe that you must pay soon (eg PAYE, National Insurance, VAT, your staff and your suppliers)?
 - do you need to reserve any of the money you have for any special purposes?
- Are you in control?
 - what money is owed to you, who owes it?
 - are you expecting grant payments?
 - how are you going to ensure you receive what you are owed?
 - will you be able to continue operating in the coming weeks and months?
 - what efforts are you making to attract or sustain new and existing sources of income?
- How well are you managing your finances?
 - are you viable? ie are you paying out more or less than you are spending each month?
 - are you keeping within your agreed budget?
 - are you spending money wisely?

Financial reports

The aim: Committees need financial information which:

- contains things they need to know
- they can read quickly
- they can learn to understand
- they can question.

The approach: The following recommended model for a basic monthly financial report is designed to meet the needs of a wide range of small and medium-sized organisations. It does not pretend to follow formal accounting practices. Instead it is designed to meet the known practical needs of trustees for basic information which is easy to understand and which leaves out unnecessary and distracting detail. Accountancy jargon is kept to a minimum, and issues which might cause confusion such as "fixed assets" and "depreciation" are ignored. This approach can be amended easily to include additional information needed by organisations as they grow.

The essential monthly financial report: The recommended financial report consists of three parts (or only 2 parts for small groups). Each one can usually fit on one side of A4 paper or less:

- a **“simplified balance sheet”** at the end of each month showing the “current assets” (it is not a true accounting balance sheet, but it is easy to prepare and understand)
- a **budget report** for the current month and the year to date, comparing your budget forecast with a summary of your actual income and expenditure (*small organisations which don’t have ongoing projects to monitor can probably monitor effectively without the budget report*)
- a **written report** to explain to members what the simplified balance sheet and the budget report mean for the organisation; in small organisations this can usually be a few lines unless there is anything particularly important to report.

The simplified balance sheet: The balance sheet is extremely easy to prepare (if you keep good financial records) and highly informative. In its simplest form any trustee can quickly learn to understand it.

The balance sheet is a snapshot of how much money you would have (your “net current assets”) on any particular day (usually the last day of the month) if you could pile up the cash from all your bank accounts and cash boxes, if people who owed you money paid up immediately, and if you then paid off all your debts to your suppliers, any outstanding VAT and Inland Revenue payments, and any bank loans.

The “net current assets” is not a real amount of money, so don’t get too excited by it. But it can be a valuable indicator of your financial state of health month to month. If the figure is minus rather than plus there may be an innocent explanation. But it could signify trouble.

The monthly budget report: The budget report brings together information from two places in your accounts system – your annual budget and the monthly “income and expenditure account” which summarises the organisations transactions each month. It tells you:

- what you originally expected to receive and to spend during the last month and during the financial year so far (summarised under standard headings)
- a summary of what you actually received
- a summary of what you actually spent.

Information you can don’t need in your reports:

- **full cash book records** – in small charities with small numbers of transaction each month, trustees frequently want to look at the cash book records of **every** payment in and out during the month; but this practice is not wise where there are larger numbers of transactions
- **the full budget** – it is quite common for trustees to receive the full budget report every month showing all 12 months of the year – and some trustees do not know where to start looking; so only provide the full report only if trustees ask for it and, if you do so, it is a good idea to highlight the current month’s figures so people can focus on the important detail.

4. Practical financial monitoring – a simplified “balance sheet”

The following notes explain how the Simplified Balance Sheet below works in practice.

Knowing you’re in safe hands: The information on balance sheet information is in itself powerful evidence that your accounts are being well managed. It suggests that person responsible for your accounts has:

- properly recorded all the month’s financial transactions
- reconciled the bank statement
- balanced the petty cash records
- checked the invoices which you have received but not yet paid
- looked at what your suppliers are owed, and, quite possibly, brought the Inland Revenue payments up to date
- maintained an ongoing VAT record
- counted (and hopefully banked) all the cash
- scouted around to ensure there are no outstanding problems
- checked for errors in the accounts.

(But do be a little cautious. It is not unknown for staff and volunteers under pressure, or just plain incompetent or dishonest, to invent information to cover up their failings. So other physical checks of your systems are also strongly advised, particularly when new people become involved in your systems. These are covered below.)

A balanced view of the bank balance: The amount of money in the bank is desperately misunderstood by some trustees. Don’t automatically get excited by big bank balances or depressed by small ones. A bank account boosted by a £20,000 grant cheque to cover your wage bill for six months may not actually be enough to ensure your survival. On the other hand, sending out an invoice for a £20,000 contract which you completed last month could make you feel extremely secure, even though there is very little in the bank.

The “bank balance” figure should be a “reconciled balance” at the date of the balance sheet (ie it should be based on the organisation’s latest bank statement with adjustments for additional recent income and expenditure). Get advice if you need help on this.

Cash in hand: “Cash in hand” is money you are holding on your premises, usually cash you have received from users or customers which is waiting to be banked. You should take note if large sums are reported since it suggests a possible problem with your banking arrangements and a security risk.

“Debtors” (money owed to the organisation): You should issue an invoice promptly when anyone receives goods or services from you but does not pay at the time they receive them (these are called “credit transactions”). Keep the debtors figure as low as possible. If it grows or won’t decrease, this may mean that your arrangements for credit control are not good enough, eg that you are not being firm or diligent enough in chasing people who owe you money. If there are only a few, you could list the creditors on the balance sheet under the “debtors”.

Taking stock: If you run a café or shop or carry on some other trading as part of your activities, the “value of stock” figure can point you to many important issues:

- whether you are buying the right amount of materials
- whether you are losing goods and materials through damage or waste (particularly items such as food and drink which have a limited life)
- whether you are suffering from theft.

A monthly stock check to calculate the value of the unsold goods and materials every month can be highly informative, and is strongly recommended. In many community businesses it is imperative.

VAT repayments: This only applies if you are registered for VAT and you are able to reclaim your VAT payments.

Loans to other bodies: If you make loans to another body (eg to help fund a subsidiary trading company) it is important that you check that repayments are being made, and ensure the rate of interest you charge is comparable with market rates.

“Creditors” (money you owe to suppliers etc): Creditors are people and organisations you owe money to. Normally you will have received an invoice from them showing the amount. But it is sensible to include any other big bill you have incurred in your creditors total on the monthly balance sheet, even if you have not yet received an invoice. You should keep all invoices you receive together and transfer them to another file as soon as you pay them. This way you can keep track of creditors each month. If the number is small you could list the creditors with amounts under the “creditors” heading on the balance sheet.

Inland Revenue: Include all PAYE tax and National Insurance payments you owe on wages and salaries which have been paid or are due to be paid up to the date of the balance sheet. Monitor the figure closely. It is extremely important that you do not get behind with these payments.

VAT: If you are registered for VAT and prepare your returns quarterly it may not be efficient to calculate the VAT you owe every month (though some computer systems will keep track for you). Don’t worry about this unless you know that you will have to make an exceptionally large VAT payment to Customs and Excise in the next one or two months.

“Restricted funds”: If you are holding money in your bank account which is earmarked by a funder to be spent on a *specific project or purchase* at some future date, you should show it here as a liability. This is because the money is not technically freely yours to spend at present, so you cannot truly regard it as an asset.

This can become a little complicated. For instance, if you receive a grant payment covering three months project expenditure on the day the balance sheet is prepared, and your funder has sent it one month after you actually started spending the grant, the “restricted funds” figure will now be equivalent to two months grant expenditure. Next month the “restricted funds” will be the equivalent of one month’s grant spending.

If presenting restricted funds on the balance sheet gets too difficult, you must explain the situation in the written part of the financial report so that trustees are not misled about the organisation’s financial position.

Advance payments: You may occasionally receive other payments in advance which are not strictly “restricted funds” under charity law, eg for contract work which you have not completed. Advance payments should be treated on the balance sheet in the same way as restricted funds.

Liabilities you are liable to overlook: Make sure you understand everything which is covered by “other liabilities. Are there any special payments which you will have to make for staff wages, holidays, or redundancies?

Understand your “net current assets”: Finally, although meaningless on its own, the “net current assets figure” is the ultimate indicator of whether your financial position is developing or declining over a period of time. Compare the “net current assets figures” each month for the past year, and you will see the pattern. Variations over one or two months may be blips, but anything beyond that may be a trend. A simple graph can help to show up trends visually for those who do not enjoy figures. If the trend is consistently downward it is time to take remedial action.

ANYTOWN COMMUNITY TRUST

Simplified Balance Sheet at (end of month)

ASSETS

Current account bank balance	£
Deposit account bank balance	£
Petty cash	£
Cash in hand	£
Owed to the Trust by debtors	
debtor 1	£
debtor 2	£
debtor 3 etc	£
Grant payments overdue	£
VAT repayment due	£
Other assets	£

Total assets

£A

LIABILITIES

Owed by the Trust to creditors	
creditor 1	£
creditor 2	£
creditor 3 etc	£
Inland Revenue payment due	£
VAT payment due	£
Advance payments received	£
Loans to be repaid	£
Other liabilities	£

Total

£B

Net Current Assets

£A-B

Example format for a simplified "balance sheet"

5. Practical financial monitoring – monitoring the budget

So you haven't got a budget. If you do not prepare a budget you won't have much of a clue where you are going. You won't be able to take decisions safely about fresh items of expenditure, new projects, staff pay rises, etc. You might survive for years in this condition. But that will be no more impressive than drifting in the Pacific Ocean in a rowing boat and avoiding Australia – in fact you could be drowned in a storm at any moment.

You must delegate someone in your organisation to draw up a budget, and keep it up to date. The budget should:

- cover a full 12 month period, preferably the 12 months of your financial year
- keep the headings for income and expenditure categories as close as possible to those you have used in previous budgets, grant applications etc
- be based as far as possible on your previous accounts records, or the experience of organisations doing similar work and/or using similar premises
- include a provision for “contingencies” – other unforeseen expenditure as a percentage (say three to 5 per cent) of the total – if this is likely to be relevant to your organisation
- show seasonal variations in items like gas and electricity charges as realistically as possible through the year (not the same average figure for every month or quarter)
- incorporate detailed notes on how you arrived at the figures it contains – otherwise they will not mean anything to other people in the organisation (eg the travel cost should relate to a total mileage at the standard mileage rate; and income figures should relate to something real such as a total number of users paying an average amount per head).

What you really need is a cash flow forecast: A cash flow forecast is very little more work to produce than a simple budget, and it will be much more useful for monitoring. The main distinguishing features are:

- income is shown in the month when you expect to receive bank the cash received, not necessarily when you issued the invoice or carried out the work
- expenditure is shown in the month when you expect to make the payment, not necessarily when you made the purchase or incurred the debt
- a “month-end balance” or “balance carried forward” figure is shown for each month (this is the bank balance at the start of the month plus expected income minus expected expenditure and is directly comparable with you actual bank balance).

The only budget you've got is the work of fiction in your Business Plan? Then redo it fast so that it matches the real world. Update any budget which has become so out of date or remote from your actual experience that it is no longer useful. Perhaps you think it's cheating to rewrite your financial forecasts whenever they prove to be wrong? But budget projections are to give you guidance, not to provide a test of your fortune telling abilities. The budget provides a model beside which you can assess your current performance. The more versions you produce, the closer you will get to understanding the way your finances are working, and the more control you will have over them.

Month by month monitoring: The budget report is designed so that you can easily compare your actual income and expenditure, heading by heading, against your original budget forecast. How you present and then use this information is up to the inventiveness and perception of your trustees and staff.:

- you will start to see which aspects of your activity need better control or closer examination – this can be crucially important if you are working on contracts where you know that margins are tight
- it can be useful to show major ongoing contracts and different types of sales income separately in your budget report

- larger organisation need a separate budget report for each substantial project which they operate so they can be monitored independently of one another.

Year-to-date comparisons: The comparison between the actual and the forecast finances for the past month is much less useful than the comparisons for the year to date (unless you happen to be in the second month of the financial year, of course). Also, it can often be instructive to see what happened at the same time in previous years, particularly if your activities are seasonal (such as running holidays for disadvantaged groups, or outdoor play facilities). Then you can plan to take advantage of recurrent peaks and troughs in demand for your service.

6. Practical financial monitoring - general guidance

Don't mention the toilet rolls: Many people who are in other respects coherent, intelligent and responsible human beings suddenly cannot cope when they see columns of figures! One common way which trustees use to disguise their inadequacy is to switch the conversation to something more tangible, such as the cost of toilet rolls. If you fail to bring this into the open you might *only* talk about the toilet rolls, or the stationery, or the coffee, and forget about important financial matters altogether.

Minimising the terror: The reporting system recommended here is intended to minimise your members' fear of figures. But you can go further by:

- highlighting relevant details very clearly
- attaching simple, brief explanatory notes which interpret the figures
- including the occasional graph to make the information more accessible (eg a line or bar graph of the "net current asset" figures for the past year)
- providing brief clear written reports to accompany the figures.

Don't be afraid to be dumb: Trustees have a right to ask dumb questions about the accounts. People are often afraid to ask the obvious, but the answers can be enlightening for everyone.

Ask difficult questions: This is monitoring after all, so any question which might help you and your colleagues to get closer to understanding the real performance of the organisation is entirely legitimate. If the information is not readily available or you are not satisfied with the answer you get, there are plenty of ways forward – a private discussion later with the manager or treasurer, a report to the next meeting, or a look at the financial records yourself. It's your right as a trustee. (But you shouldn't deliberately try to trip up your officers.)

Be open-minded and supportive: This is your opportunity to support, not to undermine your officers. Most managers welcome any serious interest in the accounts by the trustees because it means they can share their concerns and their successes. You certainly need to get suspicious if you discover there is a reluctance to divulge information. But even then you should be extremely careful about indicating any distrust, and most particularly about any challenge to the integrity of an employee or volunteer. The relationship will never recover.

Don't take precipitous action: Large numbers of suggestions for improvements in the running of the organisation will stem from discussions of the financial reports. That is part of the value of the process. But you should be extremely careful about leaping, for instance, from discussing a problem highlighted by balance sheet to instructing your manager or chair directly on how to run the operation. The manager is probably much more familiar with the financial situation than the trustees are, and radical new policies may be inappropriate. If major changes seem to be needed you should make sure they are properly investigated and evaluated, or at another meeting, before you take irreversible action.

Set up a finance committee: The disadvantage of handing over monitoring to a finance subcommittee is that other members of the main board of trustees or board may never get a chance to contribute. It is also quite possible to end up with futile duplicate discussions in the two groups if the meetings are poorly chaired. But a small finance sub committee with properly defined terms of reference can be useful for supporting the staff, carrying out checks in a non-threatening way, and coping with the otherwise distracting minor details. The main board or committee can then receive abbreviated reports and reserve their detailed involvement for issues such as setting the annual budget and policy discussions with large spending implications.

7. Practical financial monitoring – internal financial regulations

Standards for good financial practice: It is vital that the trustees set standards for good financial practice, and ensure that there are clear directions and procedures for dealing with financial affairs. These “internal regulations” should be appropriate to the size of your organisation and should not be over bureaucratic. If you have appointed an independent examiner or auditor, they may be able to help you decide what measures are suitable for your organisation. In general, trustees should ensure that internal financial regulations include:

- details of who is responsible for each aspect of maintaining financial records and preparing reports
- the delegation of responsibilities for financial matters to paid staff, volunteers subcommittees and outsiders
- procedures for preparing and approving financial plans and budgets
- the banking arrangements
- the payment of staff
- policies and procedures for purchasing goods and services
- procedures for authorising expenditure on behalf of the organisation
- a detailed description of the duties and responsibilities of the treasurer
- procedures for controlling, opening, listing and distributing incoming post where money is received in this way
- procedures for authorising and controlling activities concerned with raising or generating funds by or on behalf of the organisation.

The board should review these regulations from time to time to ensure that they are in keeping with the changing needs of the organisation.

Safeguards: It is also important to clarify procedures to ensure the security of your funds and to protect individuals who handle them:

- a minimum of two people should be present whenever money is handled (eg when emptying collection tins, counting takings after a jumble sale)
- all money received should be banked gross
- never make payments out of money received
- keep a cash float for all small payments, replenishing this from the bank account not from cash receipts
- no one should have authority for both ordering goods and for authorising the purchase of those goods
- no one should be able to authorise any payments to be made to themselves, eg wages and expenses claims.