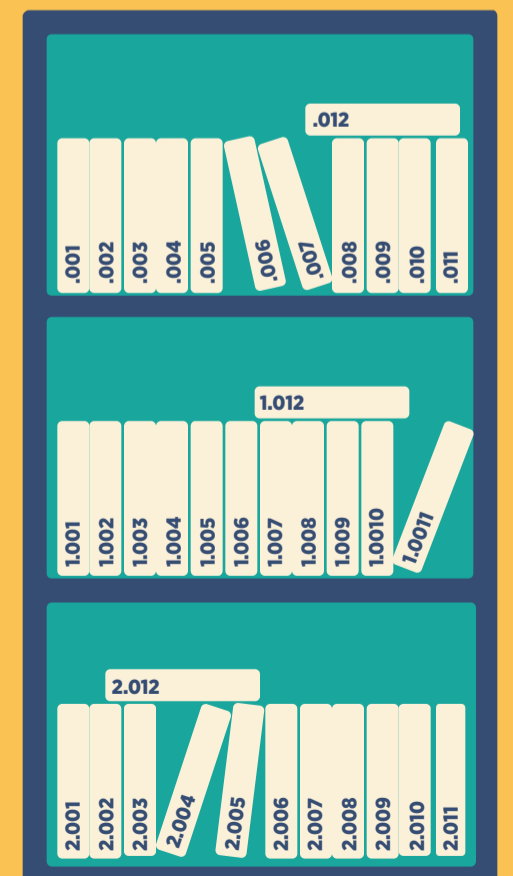


FINANCIAL MANAGEMENT FOR NON PROFIT ORGANIZATIONS

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GLOSSARY



Account	The basic element of the accounting system. It is used to record increases and decreases in assets, liabilities, fund balance, income and expense items.	Excess	The positive difference of revenue over expenses. It shows what you have left after you have paid for everything.
Accrual Basis	A recordkeeping method under which income is recorded when it is earned and expense recorded when incurred. Under the accrual basis method, goods and services purchased should be recorded as assets at the time the liability arises, which is normally when the title to the goods passes or when services have been received.	Fixed Assets	Capitalized costs (expenditures), the benefits of which exceed one year. NGOs should capitalize fixed assets purchased with unrestricted funds at cost. Donated fixed assets should be recorded at their fair value at the date of the gift.
Accrued	Expenses already incurred for which no transaction has yet been recorded.	Fixed Costs	Expenses that are not affected by the volume of revenue. Rent and utilities, for example, must be paid whether or not an activity is accomplished. Fixed expenses are the basic costs that every organization knows it will incur each month.
Accumulated	Depreciation account by which the balance of the Depreciation noncurrent assets is reduced.	Functional Expenses	A classification which groups the expenses of an organization based on their function, which might be: <ul style="list-style-type: none">• Program expenses• Management & general expenses• Fundraising expenses
Balance Sheet	A financial statement, which shows what an organization owns and owes at a certain date (the date it is prepared). The Balance Sheet is a list of assets on one side and liabilities on the other side, accompanied by the respective amounts. Correctly prepared, the balance sheet must balance, which means the total assets should equal the total liabilities.	Fund Balance	The difference between what an organization owns and what it owes. These funds may be restricted (if left over from a grant) or designated (if restricted by a decision of the board for specific purposes).
Cash	Money in hand or readily available.	Fundraising Expenses	Costs incurred for the purpose of inducing others to contribute money, securities, time, materials, or facilities for which the contributor will receive no direct economic benefit. Normally, these costs should include personnel, occupancy, printing & mailing and all direct and indirect costs of soliciting.
Cash Basis	A recordkeeping method under which income is recorded when it is earned and an expense recorded when incurred.	Liabilities	Debts or what is owed to third parties.
Contra Account	An account that has a balance opposite the normal balance. We would expect a contra-asset account to have a credit balance and a liability account to have a debit balance.	Operating Costs	Expenditures arising out of current operating activities. What it costs you to do business – salaries, rent, utilities etc.
Depreciation	An accounting method which aims to distribute the cost or other basic value of tangible assets over the estimated useful life of the assets in a systematic and rational manner. Depreciation for the year is the portion of the total charge that is allocated to the year.	Posting	Transferring figures to another book, usually from books of original entry to those of second entry.
Deferred Revenue	Revenue which is recorded before it is earned and which requires adjusting entries at the end of the period.	Restricted Funds	Income that has been restricted by donors or other outside parties for specific purposes.
		Statement of Revenue and Expenses	Lists the revenues less expenses of the period, with the difference representing excess or deficit.

WHY IS IT IMPORTANT TO KEEP FINANCIAL RECORDS?

INTERNAL ADMINISTRATION TOOL

Key financial decisions such as buying office furniture, hiring staff and defining the prices for services cannot be taken without having exact financial data. A good financial system provides useful financial information to help the NPO hire staff to administer and control its activities.



GIVING INFORMATION TO THIRD PARTIES

The NPO is not the only user of its financial information. In the case of a grant or a loan, the donor or the loaner need financial details to consider the capacity of the NPO to administer grants in the right way or to return the loan.

In order to provide right information, the NPO needs a financial system that can furnish all financial reports when needed such as the balance sheet, the statement of revenues and expenditures, the budget and money forecast.

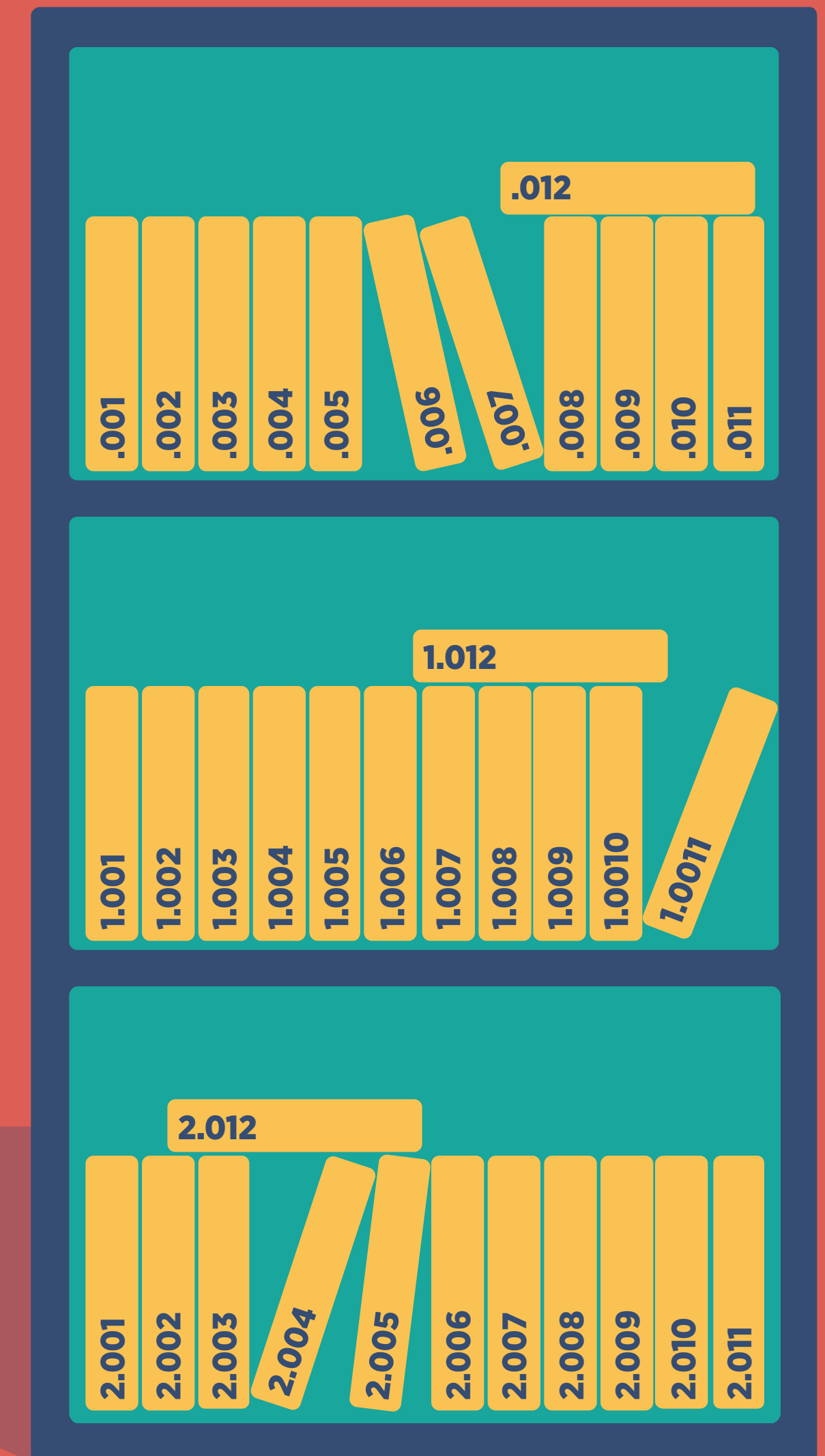


WHAT IS THE CHART OF ACCOUNTS?

The Chart of Accounts is a common language that is used throughout the NPO's entire record-keeping system. All the various elements that comprise the accounting system, including books of original and secondary entry, financial statements and budgets, should utilize the common language of the organization's Chart of Accounts.

The main purpose of this common language is to make possible the consolidation and interpretation of accounting information. The numbering system makes this possible.

To facilitate the record-keeping process of an economic entity, all accounts are numbered. The use of numbers to identify accounts in the organization is much easier and more efficient than using account titles.



GENERIC ACCOUNTING CATEGORIES

Independent of the unique characteristics of the organization reflected in the Chart of Accounts, there are five generic accounting categories common to all non-profit organizations:



REVENUES

These accounts represent earnings during the year. A revenue account is established for each source of revenue. The account titles generally should supply an adequate description of the nature of each revenue account. Many NPOs may utilize just one income account, calling it a grant, if this is the only source of revenues.

Depending on the type of the organization, other sources of revenues, and therefore other revenue accounts, might be:

CONTRACT INCOME:

Where the nature of the legal agreement is a contract rather than a grant.

CONTRIBUTIONS FROM INDIVIDUALS:

Funds raised from individual donors.

CONTRIBUTIONS FROM CORPORATIONS:

Funds raised from businesses.

INTEREST INCOME:

Money deriving from investments in the form of passive income.



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EXPENDITURES

The two main types of expenditures incurred by an NPO are Program Expenses and Management or General Expenses.

Establishing the Expense Accounts is a very delicate area when developing the Chart of Accounts. This will probably be the area where the most account titles are found. The NPO should be very careful in selecting its expenses accounts and should avoid having too many. For minor expenses like stationery and office supplies, where the total is not significant, the NPO may choose to have only one expense account, viz. Office Expenses.

Below is a list of some of the line item expense categories, which an NPO may choose to have in its expense accounts:

SALARIES:

The salaries of all employees of the organization.

RENT:

The rent of the office(s) of the organization.

TRAVEL EXPENSES:

All costs related to travel of the organization's staff, such as:

- Transportation expenses
- Accommodation expenses
- Food expenses

GENERAL OFFICE EXPENSES:

Stationery and other office supplies.

REPAIRS AND MAINTENANCE:

Under this line item, we can record all repair costs for the office and equipment.

PROFESSIONAL SERVICES:

When the organization needs the services of a professional, for instance, a computer engineer or a lawyer, you pay them a fee for the services provided. You may record this cost under this line item.

There will be other expenditures your organization incurs during its activities. Your Chart of Accounts should be built in such a way as to allow the entry of other expense accounts.

ASSETS

Assets are everything an NPO owns. Depending on the rate decided, the assets may be converted into cash. They are classified into two subcategories:

CURRENT ASSETS:

All those assets that are readily convertible to cash or its equivalent within one year, such as:

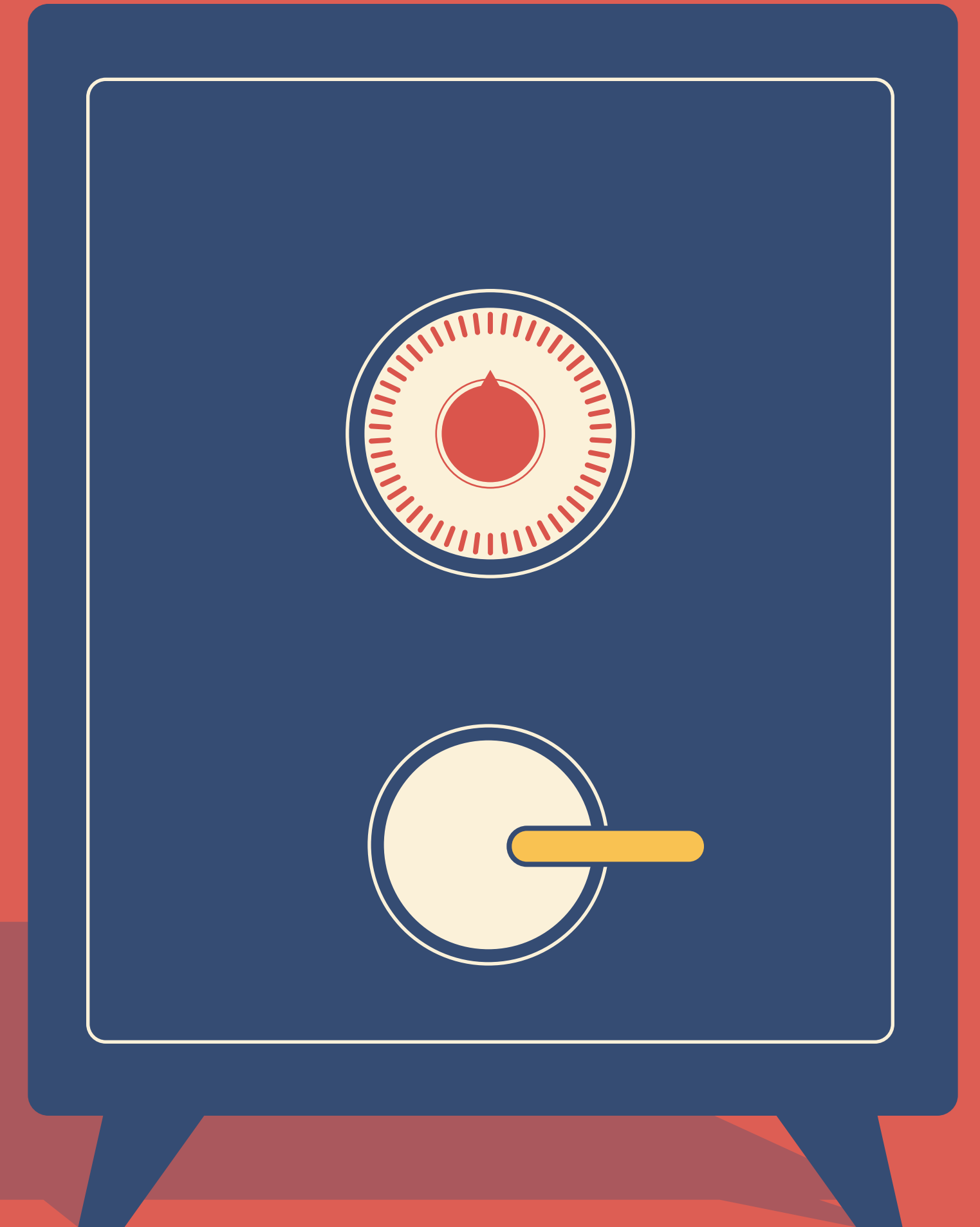
- Cash – in the Checking Account at the bank.
- Cash – in the office safe.
- Accounts receivable – grants or contracts signed which are an obligation for the donor or contractor, and payable to the NPO within the year. For example, a Reimbursement Grant.
- Advances – For instance, money advanced from the NPO to its employees for travel expenses, which are not considered expenses until the receipts from vendors are presented to the accountant.

FIXED ASSETS:

Those items purchased by the organization and from which it will benefit for more than one year.

Some Fixed Assets accounts are:

- Furniture and Equipment
- Savings Accounts (for more than a year)
- Accumulated Depreciation.



LIABILITIES

These accounts represent the obligations of the NPO toward third parties, or what it owes. As for the assets, we can group these into the following categories depending on when the NPO is supposed to pay them:

CURRENT LIABILITIES:

Those obligations that the NPO plans to pay within one year. Some Current Liability accounts are listed below:

- **Accounts Payable** – when, for example, you purchase goods or services on credit, the NPO will have an obligation toward the supplier. If this obligation is to be paid within the year, the NPO has a current liability.
- **Accrued Salaries** – if, for instance, the NPO pays the salaries for the past month in the first week of month, that is an accrued expense because the organization has an obligation to pay its employees for the work done during the month that was just completed.
- **Payroll Taxes & Social Insurance Withheld From Salaries** – the NPO may be required to withhold the taxes on personal income and social insurance from the salaries of its employees in order to pay them to the state on behalf of the employees. If these tax deductions are withheld and not paid to the state, this represents an obligation of the NPO to the state.

LONG TERM LIABILITIES:

The obligations that are due after a one-year period.

- **Long Term Debt** – This could be a loan the NPO takes to pay for its general or program expenditures.



FUND BALANCE

The Fund Balance deals with the basic value of the organization and it is calculated as follows:

$$\text{TOTAL ASSETS} - \text{TOTAL LIABILITIES} = \text{FUND BALANCE}$$

The five general categories of accounts may be presented in financial statements as in the table below:

ACCOUNTS	FINANCIAL DOCUMENTS
Income/Expenses	The Statement of Revenue and Expenditures (SRE)
Asset/ Liability/ Fund Balance	Balance Sheet

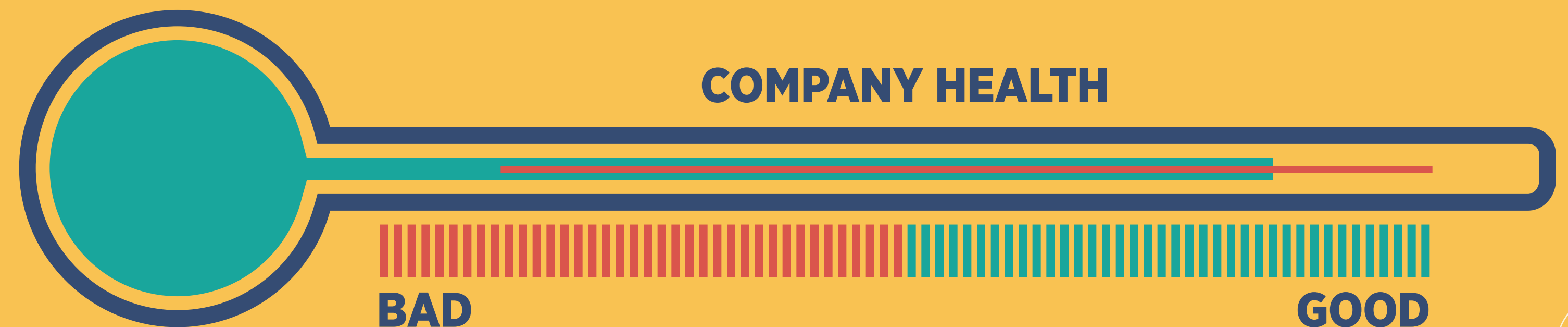
The Statement of Revenue and Expenditures (SRE)

Also referred to as the Income Statement, this document presents the financial activity of an organization over a certain period of time e.g. 3 months, 6 months or a year. It shows whether an organization is making, or losing, money. This statement can be prepared for each activity.

Let's see a simple SRE for ALBA Association:

ALBA NPO Statement of Revenues and Expenditures for the year ending December 31, 2002

Revenues:	
Grants	400
Contributions	90
Revenues from services rendered	100
Total Revenues	590
Expenditures:	
Personnel	220
Rent	50
Telephone & Utilities	20
Office Expenses	40
Total expenditures	330
Excess	260



The Statement of Assets, Liabilities and Fund Balance (Balance Sheet)

This statement is designed to show the financial position of the organization. The financial position is a dated statement of what the NPO owns and what it owes. By reviewing an organization's balance sheet, and comparing what it owns with what it owes, users can make judgments on the financial health, or solvency, of the organization.

The difference between assets and liabilities is the Fund Balance.

If this difference is positive (meaning total assets exceed total liabilities), the organization has a positive Fund Balance. Please note that the total of Assets should equal the combined total of Liabilities plus Fund Balance. This balancing of Assets to Liabilities plus Fund Balance is why the financial statement is called the Balance Sheet.

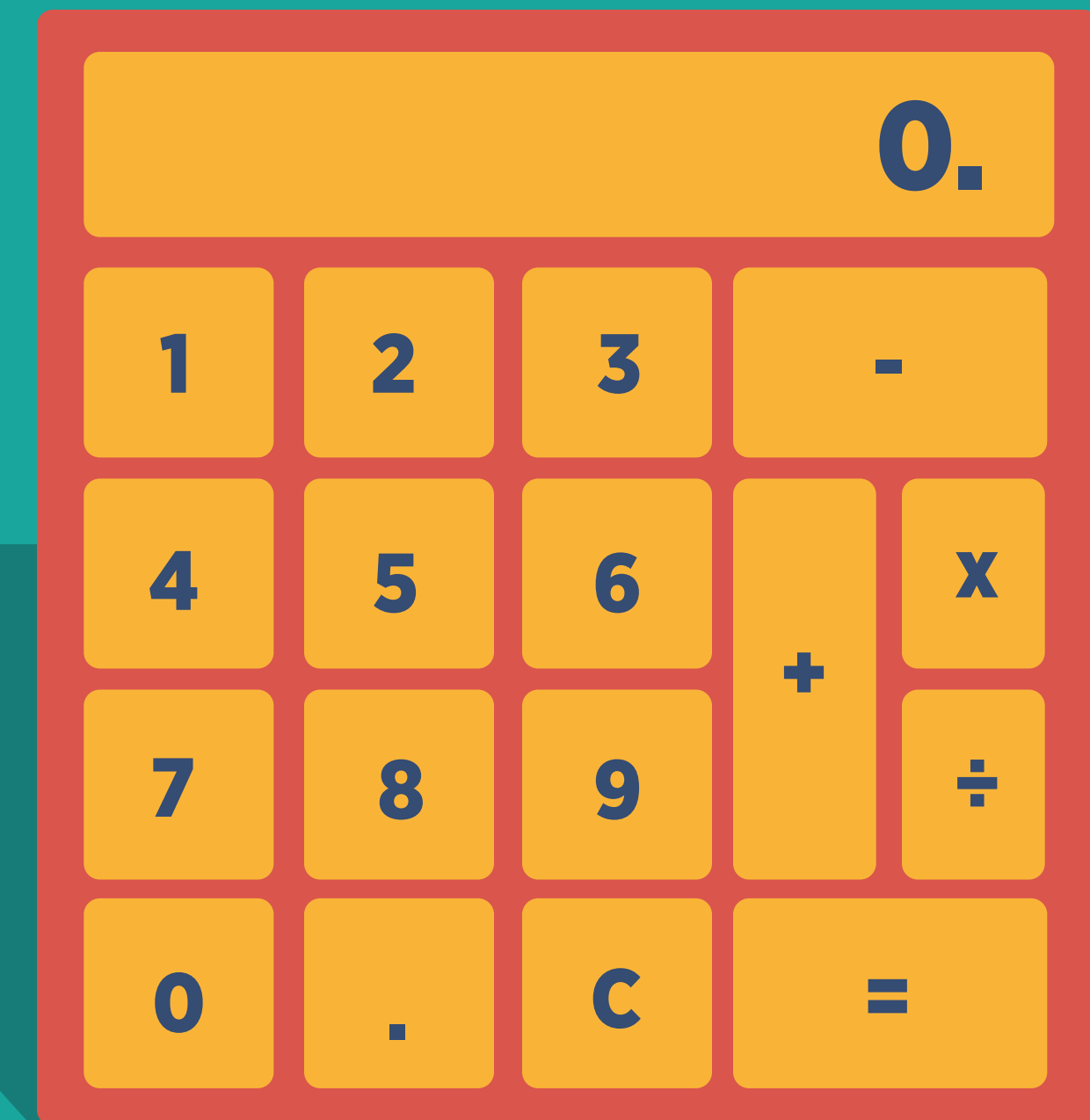
BUDGETING

The budget is a commitment to expend money for certain categories of goods and services.

Budgeting your money wisely is also a demonstration of your organization's management skills. An NPO needs both a good accounting system, as well as a budgeting system based on your Chart of Accounts. Donors are more likely to give funding to organizations with both good accounting systems, as well as good budgets.

BUDGETING PURPOSES

- To ensure the availability of necessary sources for the achievement of the project objectives, as defined in the project proposal.
- To define the amount needed for the implementation of the project.
- To ensure that available and restricted sources are used in the most efficient way.
- To be a monitoring instrument which is used to compare the estimated costs with the real ones.



MANAGERIAL FUNCTIONS OF BUDGETING

Planning element

- A financial plan covers a defined time period.

Cost estimation

- It gives a fair estimate of costs and services.

Control element

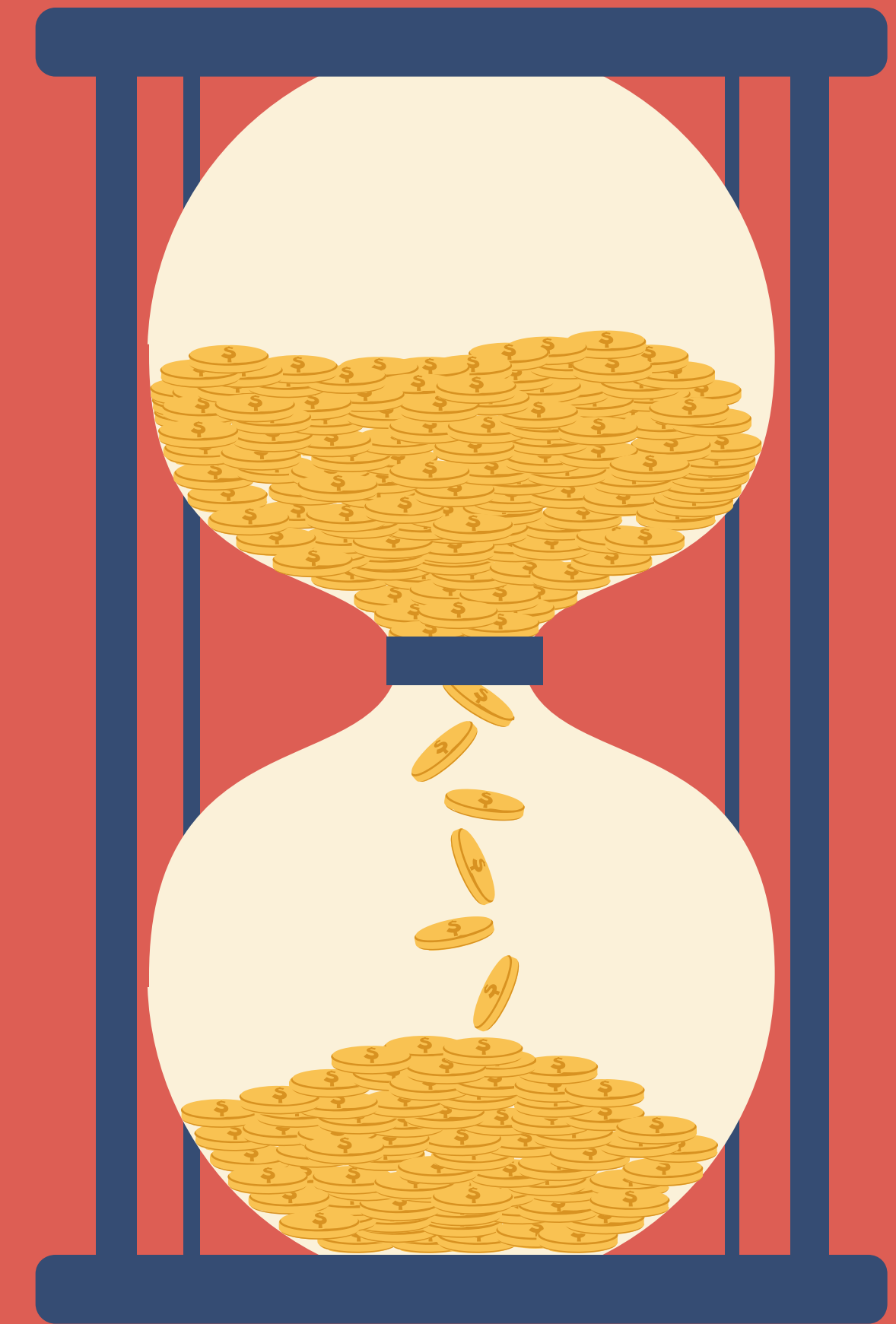
- It compares real and planned financial data in order to monitor the progress of project objectives.

NPOs, due to lack of experience, occasionally make mistakes in budgeting. Many of these mistakes can easily be avoided with some attention to the following points:

- It is important to identify all activities which are going to cost money. When permanent staff of the NPO is used in a donor-funded project, the cost to the organization of contributing the staff should be included in the budget.
- Another common mistake is forgetting, or ignoring, some of the expenses included in implementing activities. If you do not have the money when it is needed due to faulty budgeting or poor accounting, you may not be able to complete the project as promised to the donor or to the community.
- Some NPOs, in budgeting for their projects, neglect to shop around for the best prices for high-cost items such as vehicles or computers. If the quotation used in your budget is higher than the best price in the market for an item, the donor may reject the proposal.
- Sometimes, NPO budgets are too low for implementing the project. While this can be due to sudden increases in market prices, more often it is due to the NPO's unfamiliarity with the actual costs of implementing projects.

In order to overcome these obstacles, it is important to be acquainted with these three elements of budgeting:

- Programs/Activities
- Budget lines
- Chart of Accounts and Financial Sources



PROGRAMS / ACTIVITIES

Programs /Activities are a result of the vision, mission and strategies of the organization. The terminology program and activities are often used in different contexts e.g. programs for health, education etc. Activities are actions taken for the implementation of the program.

During the budgeting process, it is important to define the type of programs and activities, their number, the period when they will happen, and their duration.

It is also important to identify administrative costs (personnel and direct costs) necessary for their development, as well as the basic equipment needed for their realization.



GENERAL BUDGET LINE ITEMS

General budget line items:

I. Personnel (Salaries)

- Professional Staff
- Administrative/Assistant staff

II. Other benefits

(Percentage over the salary)

III. Direct Costs

- Office Rent
- Office equipment
- Phone/Internet/Mail
(Communication expenses)
- Printing
- Assisting costs
- Utilities (electricity, water bills)
- Other services

IV. Equipment

- Vehicle
- Computers
- Fax machine
- Copier

V. Training and training assistance

VI. Subproject costs

Costs of the activities that make the achievement of the project's aims possible.

E.g. An exhibition, conference, printing of leaflets, etc.

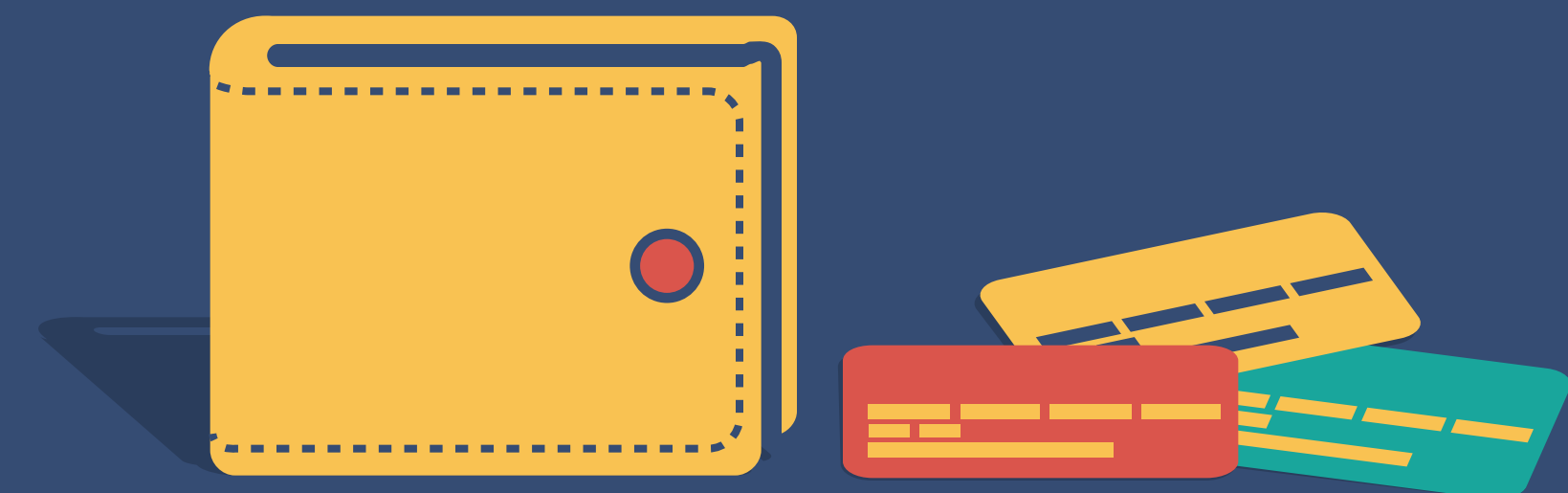


CHART OF ACCOUNTS

FINANCIAL SOURCES

These are the different types of funds and the institutions that offer them. While unrestricted funds (e.g. funds raised from private donations) are those that are at the disposal of the organization, restricted funds (e.g. grants) should be used for the specific programs and activities for which they were received.

BUDGET LINES, CHART OF ACCOUNTS NUMBERS, AND FINANCIAL SOURCES

After each number of your Chart of Accounts, you should have a Budget Line Item. The budget line item describes the item or service you are going to buy, says how many items you are going to buy, as well as when you are going to buy them. It also gives the total cost for each line item, and finally, the total cost for each budget category.

In preparing your budget, you will need two items:

- The project proposal, with detailed information on the activities which your organization proposes to carry out in order to accomplish the goals of the program or project
- A budget worksheet on which you can write down the items and activities along with their costs. The budget worksheet will also enable you to quickly estimate the total cost of the project. If your estimate of total cost is considerably higher than the funds you think will be available, you will need to make some adjustments to your project proposal.

BUDGET TIPS:

- The organization needs to have rules for when it will need to ask for bids for more expensive items.
- Your budget must indicate which donor is paying for what items. Your NPO's contribution, in cash or kind, should be listed in the budget.
- The budget must indicate the amount of money needed for each line item, for each quarter.





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