# Financial Administration and Accounting

*Guidelines*

*Step TWO – Financial Statements*

| Column journal for the "Project" Year: 20XX | | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | Cash | | Bank | | From PMU | | Salaries | | Taxes | | Material | | Transport. | |
| Date | Text | Ver | Deb | Cre | Deb | Cre | Deb | Cre | Deb | Cre | Deb | Cre | Deb | Cre | Deb | Cre |
| 01-01 | From PMU | 1 | | | 40 000 | | | 40 000 | | | | | | | | |
| 01-01 | Bank withdrawal | 2 | 5 000 | | | 5 000 | | | | | | | | | | |
| 01-01 | Cement | 3 | | | | 3 300 | | | | | | | 3 300 | | | |
| 01-01 | Petrol | 4 | | 430 | | | | | | | | | | | 430 | |
| 02-01 | Educational material | 5 | | | | 553 | | | | | | | 553 | | | |
| 02-01 | Salary Oct –xx | 6 | | 4 000 | | | | | 3 000 | | 1 000 | | | | | |
| 04-01 | Bank withdrawal | 7 | 4 000 | | | 4 000 | | | | | | | | | | |
| 04-01 | Tires for the car | 8 | | | | 2 000 | | | | | | | | | 2 000 | |
| 05-01 | Books | 9 | | 87 | | | | | | | | | 87 | | | |
| 07-01 | Copies | 10 | | 112 | | | | | | | | | 112 | | | |
| 07-01 | Pens | 11 | | 58 | | | | | | | | | 58 | | | |
| | | 12 | | | | | | | | | | | | | | |
| | | 13 | | | | | | | | | | | | | | |

*Ex. Column journal*

Document information

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## Foreword

This document represents the second step in the Human Rights and Science and Action10 guidelines on Financial Administration and Accounting. The Guideline Step TWO was developed by Dr Cecilia Öman in February 2013, and was refined by Mr Anders Kinding, in August 2013. Some of the examples are provided by Mr Alexis K. Akotchaye, Account Manager with IDH in Togo.

The FAA procedures presented in Guideline Step TWO focuses on the bookkeeping performed by the end of the year including International Finance Reporting Standards, Balances Sheet, Income Statement, Auditing and Archiving. The Financial Administration and Accounting (FAA) procedures presented in guideline ONE includes the Financial Year, Basics of Bookkeeping, to Book an Activity and Supporting Documents.

## Purpose

The purpose with the guidelines is to support Human Rights and Science and Action10 and their partners with the Financial Administration and Accounting.  Proper Financial Administration and Accounting is required to ensure project quality and transparency. The bookkeeping shows that the financial resources invested in a project were used in an efficient way. Thus, the bookkeeping is important means of communication between partners. The information is also used for monitoring and evaluation planning. Proper bookkeeping is one main tool for transparency and accountability.

## Short summary of the Guidelines Step ONE

The financial year must be decided on for each organisation. It is often relevant to use 1 January to 31 December as the financial year.

A separate bookkeeping is set up for each project. The bookkeeping shall be developed in the form of “the double entry bookkeeping system“ as described in the table below. All financial activities have to be accompanied by supporting documents.

**Bookkeeping journal for the "Project" Year 20XX**

| | | | | 4 | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| 1 | 2 | 3 | Cash account | | Bank account | | Funding ACTION10 | | Transport | |
| Date | Text | Ver. | Debet 5 | Credit | Debet | Credit | Debet | Credit | Debet | Credit |
| 07-jan-12 | Petrol for transportation to schools in the villages | 1 | | 200 | | | | | 200 | |

The book-keeping must be audited at the end of the financial year. The auditing must be performed by an external and professional auditor. It is the responsibility of the auditor to control each supporting document and verify its correctness in relation to the bookkeeping. The bookkeeping documents including the supporting documents must be safely archived and be kept until ten years after the project has closed.

## International Standards

International Financial Reporting Standards (IFRS) are designed as a common global language for business affairs so that company and organization's accounts are understandable and comparable across international boundaries. They are progressively replacing the many different national accounting standards. The rules to be followed by accountants to maintain books of accounts which is comparable, understandable, reliable and relevant as per the users internal or external.

## Financial statements

### Objective of financial statements

A financial statement should reflect true and fair view of the business affairs of the organization. As statements are used by various constituents of the society / regulators, they need to reflect true view of the financial position of the organization and it is very helpful to check the financial position of the business for a specific period.

### Four basic Financial Statements

IFRS financial statements consist of a;

1. Balance sheet (Statement of Financial Position )
2. Income Statement (Statement of Comprehensive Income)
3. Statement of Changes in Equity (SOCE)
4. Cash Flow Statement or Statement of Cash Flows

The statements come together with notes, including a summary of the significant accounting policies.

In these guidelines we will only address the Balance sheet and the Income statement at this time.

## Balance Sheet

In financial accounting, a balance sheet or statement of financial position is a summary of the financial balances. The financial balance is listed as of a specific date, such as the end of its financial year. A balance sheet is often described as a "snapshot of a company's or an organization's financial condition". Of the four basic financial statements, the balance sheet is the only statement which applies to a single point in time of a business' calendar year.

| **Assets** | |
|---|---|
| Cash | $6,600 |
| Accounts Receivable | $6,200 |
| Tools and equipment | $25,000 |
| Total Assets | $37,800 |

However, many transactions of an organisation are not paid immediately; they build up inventories of goods and they acquire buildings and equipment. In other words: organisations have assets and so they cannot, even if they want to, immediately turn these into cash at the end of each period. Often, these organisations owe money to suppliers and to tax authorities, and the proprietors do not withdraw all their original capital and profits at the end of each period. In other words organisations also have liabilities.

The "capital" is the difference between Assets and Liabilities. It is a measure of what is left when all liabilities has been paid for.

| **Balance Sheet** | | | | |
|---|---|---|---|---|
| Assets ("Active") | | | Liabilities ("Passive") | |
| Land | 7 000 | | Capital | 60 500 |
| Car | 5 000 | | Debts | 6 000 |
| Office | 4 000 | | Net Income 2013 | 14 500 |
| School building | 40 000 | | | |
| Bank account | 24 500 | | | |
| Cash account | 500 | | | |
| | | | | |
| TOTAL | 81 000 | | | 81 000 |

## Income Statement or Statement of Activities

At the end of the financial year the income of the year is compared with the expenses ("costs"). The comparison will show if the financial year generated a surplus or a loss.

Income statement is an organisation's financial statement that indicates how the revenue (money received before expenses are taken out) is transformed into the net income (the result after all revenues and expenses have been accounted for). It displays the revenues recognized for a specific period, and the cost and expenses charged against these revenues, including taxes. The purpose of the income statement is to show whether the organisation made or lost money during the period being reported.

An income statement represents a period of time. This contrasts with the balance sheet, which represents a single moment in time.

Charitable organizations produce a similar statement that reflects funding sources compared against program expenses, administrative costs, and other operating commitments. This statement is commonly referred to as the statement of activities. Revenues and expenses are further categorized in the statement of activities by the donor restrictions on the funds received and expended.

The income statement can be prepared in one of two methods, depending on the size of the business or project. The Single Step income statement takes a simpler approach, totalling revenues and subtracting expenses to find the net income. The more complex Multi-Step income statement takes several steps to find the net income, starting with the gross profit. It then calculates operating expenses and, when deducted from the gross profit, yields income from operations. Adding to income from operations is the difference of other revenues and other expenses. When combined with income from operations, this yields income before taxes. The final step is to deduct taxes, which finally produces the net income for the period measured. See comparison below:

| | |
|---|---|
| + Total Revenues | + Total Revenues |
| - Total Costs | - Cost of Goods Sold |
| = Net Income | = Gross Profit |
| | - Operating Expenses |
| | = Income from Operations |
| | + Other Revenues |
| | - Other Expenses |
| | = Income before Taxes |
| | - Taxes |
| | = Net Income |

## Examples of Statement of Activity

**Statement of Activities**
for the One Month Ended January 31, 2013

| | Total |
|---|---|
| **Revenues**<br>Contributions | $10,000 |
| **Expenses**<br>Program expenses<br>Gen & admin expenses<br>Fundraising expenses | <br>–<br>–<br>– |
| **Change in net assets** | 10,000 |
| + Net assets-beginning | – |
| = Net assets-ending | $10,000 |

**Statement of Activities**
for the One Month Ended February 28, 2013

| | Total |
|---|---|
| **Revenues**<br>Contributions | $ 8,000 |
| **Expenses**<br>Program expenses<br>Gen & admin expenses<br>Fundraising expenses | <br>–<br>-1,350<br>– |
| **Change in net assets** | 6,650 |
| + Net assets-beginning | 10,000 |
| = Net assets-ending | $16,650 |

## Auditing

The book-keeping must be audited at the end of the financial year. It is the responsibility of the auditor to control each supporting document and verify its correctness in relation to the bookkeeping. The Auditor compiles her findings in a document which she signs. This document shall be sent to the Partners, together with the financial report, in the beginning of the coming year.

The auditing must be performed by an external and professional auditor. The selection of the auditor must be approved in advance by all partners. The cost of the auditor shall be in relation to the volume of the project costs and international auditing firms may not be required unless the project is large. A presentation of the auditor´s firm together with the auditor's CV shall be sent to all Partners in the beginning of the financial year.

## Archiving

The bookkeeping documents including the supporting documents must be safely archived. They shall be stored in the same format as when the books were developed and audited.  The documents must be kept for five years after the project has closed. Paper copied must be protected from fire, water and sunlight and electronic copies must have a back-up.

## Examples

Please find the following examples which have been compiled in order to show how the Financial Statements could look like for a school project. Please note that every project will have their unique set of accounts, depending on the purpose of the project.  Some accounts are though always needed, for example Cash account, Bank account, and Income (donations or sales) account.

# Examples

| Bookkeeping Journal | | | | | | |
|---|---|---|---|---|---|---|
| | | | Cash | | Bank | |
| Date | Text | Ver. | Debit | Credit | Debit | Credit |
| 2013-01-02 | Bought 25 books to 25 students | 1 | | 2 500 | | |
| 2013-02-15 | Purchase of 2 packets  of sheet metal for the roof | 2 | | | | 30 000 |
| 2013-03-01 | Received donation from Action10 | 3 | | | 80 000 | 1 000 |
| 2013-03-17 | Bought petrol at Shell | 4 | | 5 000 | | |
| 2013-03-31 | Donation from local association ABC | 5 | 8 000 | | | |
| 2013-04-05 | Salary for Marsh 2013 | 6 | | | | 10 000 |
| 2013-04-20 | Purchase of a vehicle tire | 7 | | | | 1 500 |
| 2013-04-25 | Purchas 30 reading books | 8 | | | | 3 000 |
| 2013-06-29 | Rent of conference venue | 6 | | | | 1 000 |
| 2013-07-07 | Salary for June 2013 | 10 | | | | 10 000 |
| | TOTAL | | 8 000 | 7 500 | 80 000 | 56 500 |
| | | | Debit Balance: 500 | | Debit Balance: 24 500 | |

| | Donations | | Salaries | | Taxes | | Construction Materials | | Transport | |
|---|---|---|---|---|---|---|---|---|---|---|
| Ver. | Debit | Credit | Debit | Credit | Debit | Credit | Debit | Credit | Debit | Credit |
| 1 | | | | | | | | | | |
| 2 | | | | | | | 30 000 | | | |
| 3 | | 80 000 | | | 1 000 | | | | | |
| 4 | | | | | | | | | | |
| 5 | | 8 000 | | | | | | | | |
| 6 | | | 10 000 | | 2 000 | | | | | |
| 7 | | | | | | | | | 7 000 | |
| 8 | | | | | | | | | | |
| 6 | | | | | | | | | | |
| 10 | | | 10 000 | | 2 000 | | | | | |
| TOTAL | 0 | 88 000 | 20 000 | 0 | 5 000 | 0 | 30 000 | 0 | 7 000 | 0 |
| | Credit Balance: 88 000 | | Debit Balance: 20 000 | | DB: 5 000 | | DB: 30 000 | | DB: 7 000 | |

| | School Materials | | Petrol | | Rent of location | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Ver. | Debit | Credit | Debit | Credit | Debit | Credit | Debit | Credit | Debit | Credit |
| 1 | 2 500 | | | | | | | | | |
| 2 | | | | | | | | | | |
| 3 | | | | | | | | | | |
| 4 | | | 5 000 | | | | | | | |
| 5 | | | | | | | | | | |
| 6 | | | | | | | | | | |
| 7 | | | | | | | | | | |
| 8 | 3 000 | | | | | | | | | |
| 9 | | | | | 1 000 | | | | | |
| 10 | | | | | | | | | | |
| TOTAL | 5 500 | 0 | 5 000 | 0 | 1 000 | 0 | | | | |
| | DB: 5 500 | | DB: 5 000 | | DB: 1 000 | | | | | |

The journal presented in this form allows us to know what we have received in total, what we have spent as a whole, and what is remaining at the end of the activity or year.

This allows us also a quick view of what is remaining in cash at end of period (500F), as well as in the bank account (24 500 F).

Next step in the journal is to calculate the total of each account. The balance (difference) between debit and credit is revealed. This balance can be either Debit or Credit.
A Debit Balance (“DB”) means that the total debit flow is greater than the total credit flow. The balance is the difference it takes to have equality:  Debit = Credit.
A Credit Balance (“CB”): the total credit flow is greater than the total debit flow and the balance represents the difference.

IMPORTANT NOTE
The account "Cash" could never be negative (Credit Balance). That means that expenditure paid can never exceed the amount of cash money in the cash box. So the Cash Debit must always be greater than Cash Credit.

The account "Bank" may be credit (negative), which means that the bank has given us the ability to use more money than we have in the account (“a bank loan or overdraft”).

| **Income Statement for the year 2013** | | | |
|---|---|---|---|
| | Account name | Balance from Bookkeeping Journal | |
| + Revenues | Donations | +88 000 | |
| - Cost of sold goods | | 0 | |
| *= Gross Profit* | | | *88 000* |
| | | | |
| - Operating Expenses | Salaries | -20 000 | |
| | Construction Materials | -30 000 | |
| | Transport | -7 000 | |
| | School Materials | -5 500 | |
| | Petrol | -5 000 | |
| | Rent of location | -1 000 | -68 500 |
| *= Income before taxes* | | | *=19 500* |
| | | | |
| - Taxes | Taxes | -5 000 | -5 000 |
| ***= Net Income*** | | | ***=14 500*** |

| **Balance Sheet, 31th December 2013** | | | | |
|---|---|---|---|---|
| Assets (”Active”) | | | Liabilities (”Passive”) | |
| Land | 7 000 | | Capital | 60 500 |
| Car | 5 000 | | Debts | 6 000 |
| Office | 4 000 | | Net Income 2013 | 14 500 |
| School building | 40 000 | | | |
| Bank account | 24 500 | | | |
| Cash account | 500 | | | |
| | | | | |
| TOTAL | 81 000 | | | 81 000 |

TOTAL ASSETS = TOTAL LIABILITIES (the Balance Sheet is always balanced)

ASSETS includes all goods or anything that belongs to the company or NGO

The LIABILITIES takes into account all debts and means that have enabled the company or NGO possess everything we have as assets.