

Community Money Matters

Managing Community Money

Foreword

Acknowledgements

No publication with aspirations to set out good practice in the management of money by voluntary community organisations could ever be the work of one person, and this is no exception. Inevitably, in seeking to single out those who have consciously or unconsciously provided inspiration, teaching, and examples of practice, good and bad, there will be those whose contribution goes unacknowledged, for which I apologise in advance.

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I have also drawn on my own experience as trustee and treasurer of the Oval Community Association, and I am grateful to the trustees, staff and volunteers, past and present, of that association, who have tolerated my learning by experience, I hope to our mutual advantage.

Community Matters itself must take some of the credit, since it was attending their courses and conferences which started me down the road to becoming a community accountant, and it was from those I met at Community Matters Annual Conferences that I was able to set in the wider context my own, inevitably narrow, perspective. If I have stolen your ideas without acknowledgement, I beg your indulgence. There is a fine line between plagiarism and research, and I may sometimes have inadvertently stepped over it.

This publication can trace its ancestry back to two sources:

1. "How to Manage Your Money, If You Have Any", which was produced by the Community Accountancy Project in Hackney, now sadly out of print, and suggestions that this publication, which had become dated, should be revised.
2. "Accounting for Voluntary Groups", originally published by Ealing Voluntary Service Council in 1994, and re-written by me in 2001 (but never re-published).

For copyright reasons, I have carefully avoided recycling any of the material in the Hackney CAP publication, whilst acknowledging its inspiration.

Any errors of fact or interpretation are my responsibility alone. Where opinions are expressed, these do not necessarily reflect those of either Community Accountancy Self Help or Community Matters.

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CHAPTER 1

1. INTRODUCTION

Most community organisations are unincorporated associations, governed by a constitution, which sets out what the objects of the association are (i.e. what it is for) and the rules and regulations for the conduct of its members. Unincorporated associations are usually run by a management committee, elected annually by and from its members, which may be individuals (people living or working in its catchment area), groups (both the building's user-groups and associations sections) and outside organisations, both statutory and voluntary). Although treated as a separate entity for tax purposes, unincorporated associations are not in law separate entities, and can't in their own right enter into contracts. In addition, the management committee members are jointly and severally (that is both individually and collectively) responsible for any debts the association may incur. (i.e. they have unlimited liability).

Anybody can start an unincorporated association. There is no requirement to register with anyone, and regulations (other than the law of the land) are few and far between, with general and financial management, book-keeping and accounting largely left to the common sense of the management committee members, and to generally accepted accounting practice for such clubs and societies.

However, if your community organisation

- ❖ Has objects or carries out activities which are wholly charitable, or
- ❖ occupies community premises, and/or has adopted the model constitution prepared by Community Matters (the National Federation of Community Organisations)

then it should be registered with the Charity Commissioners for England and Wales

Unincorporated associations which have registered with the Charity Commissioners

- ❖ Become charitable unincorporated associations
- ❖ Their management committee members become the charity's trustees
- ❖ Are subject to charity law, which lays down the sort of financial records which the charity has to keep, and the rules and regulations which the management committee, as trustees, are to follow

Those community organisations who have a real need to enter into contracts in their own right, or where the management committee are concerned at their unlimited liability status usually become companies limited by guarantee, having registered with Companies House. Companies have a memorandum of association and a set of articles of association, which together serve the same function as the constitution of unincorporated associations. Companies, which are subject to Company Law, are legal entities and their directors, which is what the management committee members become, do have limited liability for the debts of the company. If such companies

- ❖ Have objects or carries out activities which are wholly charitable, or
- ❖ Occupy community premises, and/or have adopted a memorandum of association and articles of association provided through Community Matters

then they should also be registered with the Charity Commissioners for England and Wales.

Such Charitable Companies not only remain subject to company law but in addition also become subject to charity law.

Because these rules and regulations colour all that a charitable community organisation, whether unincorporated or a company, has to do, they are touched on in this introduction, and gone into in more depth, as an when appropriate, later.

1.1. Receipts and Payments, or Income and Expenditure?

There are two basic approaches to accounting. The simplest and easiest to understand is called Receipts and Payments Accounting. The other, more complex, is called Income and Expenditure Accounting. Which one you pick will influence

- ❖ Your way of budgeting and working out cash flow
- ❖ Your system of bookkeeping
- ❖ The way you prepare and present your end of year accounts

Receipts and Payments accounts, sometimes referred to as cash accounts, only recognise a transaction – money received, or paid out – when it takes place. That is, when a cheque or cash is received, and when a cheque or cash is handed over.

Income and Expenditure accounts, also and more properly called accruals accounting, on the other hand, recognise a transaction when it falls due. That is, when an invoice is received or sent out, not when the invoice is settled. Accruals accounting also makes a distinction between capital items, which have a life and a value spanning several years, and revenue items, which are used up or spent in the normal course of activities. Accountants and lawyers believe that only accruals accounting can show the true and fair view required by Company law.

If you are an unincorporated charitable association with a turn-over of less than £100,000 you are permitted to prepare your end of year accounts, and by implication, to keep your books, on a receipts and payments. You can opt for accruals accounting, if you wish.

If you are charitable company, whatever the size of your turn-over, or an unincorporated charitable association with a turn-over greater than £100,000 a year, you are required by charity law to prepare your end of year accounts on an accruals basis. Although this implies that you keep your books on an accruals basis, it is in fact common-place to keep your books on a receipts and payments basis, but draw up your end of year accounts on an accruals basis.

Whichever method or combination of methods you choose, your budgets must be compatible with them.

Which option you should pick depends on your circumstances and situation. For small charities (no paid staff, turn-over less than £10,000), receipts and payments accounts is always appropriate. For larger groups, it depends on

- ❖ How much money is owed by you and to you
- ❖ How much money is or has been spent on buying capital items
- ❖ How knowledgeable your treasurer, bookkeeper or finance worker are
- ❖ Whether you are prepared to pay an accountant

For example, if at the end of each year

- ❖ You owe and are owed very little
- ❖ What you owe and are owed doesn't change much from year to year
- ❖ You spend little on capital items

there will be very little difference between your receipts and payments and your income and expenditure accounts, and thus little reason to opt for accruals accounts, unless your treasurer, bookkeeper and finance worker are up for it.

If, however,

- ❖ You owe and/or are owed significant sums
- ❖ What you owe and are owed changes a lot from year to year

- ❖ You spend a lot on capital items

you really ought to consider accruals accounting, at least for your year end accounts, and to allow for the cost of paying an accountant to do this in your budget, unless your treasurer, bookkeeper or finance worker are up for it.

In this publication, primarily designed around the requirements of charitable unincorporated associations managing community buildings, it is assumed that your book-keeping is going to be on a receipts and payments basis, but your annual accounts are going to be presented on an accruals basis.

Whichever you choose, you will also have

- ❖ To keep a register of fixed assets
 - A list of the capital items you have purchased
 - What and where they are
 - What you paid for them
 - When you bought them
- ❖ To keep a register of debtors and creditors
 - Who they are
 - How much is owed
 - For what
 - Debtors owe you money
 - Creditors you owe money to
- ❖ To do fund accounting
 - To distinguish between unrestricted, restricted, and endowment funds
 - Unrestricted funds are those which come without strings attached, and can be spent as the managing trustees see fit
 - Restricted funds are those that come with strings attached
 - They can only be spent in accordance with the wishes of the donor
 - Most grants are restricted funds
 - Street collections for a specific project will also be restricted funds
 - Endowment funds are donated assets which the charity holds for its own use
 - Either permanent endowments, which cannot be converted into income
 - Or expendable endowments, which can

1.2. Single entry or double entry?

There are two types of book-keeping:

1. Single entry – each transaction is entered only once in each account book. The entries don't balance
2. Double entry – each transaction is entered twice in each account book, once as a debit and once as a credit. The entries balance

Double entry is in principle better, but needs at least some training – a year at evening classes, for example. Except as an academic exercise, little double entry book-keeping is now done manually. For those with double entry book-keeping skills, affordable computer software is available which takes the drudgery out, without devaluing the skills. However, for those without double-entry knowledge, the software, especially if intended for the small business sector, can be full of traps for the unwary, and the issues and options are discussed later.

Community organisations have traditionally kept single entry books in purpose-designed hard-backed accounts analysis books, still widely available from stationers and stationery suppliers. For the budget-conscious, there are soft backed analysis books (primarily aimed at students) available, or even pads of loose-leaved multi-

columnar accountancy paper. In general, the larger the book and the more columns it has, the better. However, there must now be few community organisations, especially those running community buildings which don't have access to a personal computer running a spread-sheet program, and since it is a straight-forward matter first to replicate in the software the layout of a multi-columnar analysis accounts book and then to use the software to add up the columns and rows automatically, this should now be the method of choice for associations keeping single entry books.

Accordingly, this book is written from the assumption that your community organisation will be keeping single entry books using a computer spread-sheet program. If your organisation hasn't yet got a computer, it is about time it got one. Second hand, but serviceable, machines are widely available at bargain-basement prices, and grants are readily available in most parts of the country to help community groups purchase computers. If you have a computer, but haven't yet got round to using a spread-sheet program, now is the time to get to grips with it. Spread-sheet programs were in fact the "killer" application which led to the explosive growth of personal computers in business, and are still amongst the most useful and versatile of applications. If your PC doesn't have a spread-sheet program, now is the time to purchase one. Although some well known spread-sheet programs are on the face of it expensive, charities can obtain substantial discounts. If lack of experience is the issue, courses at all levels from basic to very advanced are widely available – indeed, may be on offer in your local community building! Contact your local college of further education to find out what is on offer in your area. You may also find that your local voluntary sector training providers offer free/inexpensive courses locally.

The program used throughout this book is Microsoft Excel, because this is by far the commonest spread-sheet around. However, the principles apply equally to all such programs and the practices will translate from one to the other with only minor adaptation. The only requirement is that the software be capable of opening more than one page at a time. Accordingly, if you have an integrated application, such as Microsoft Works, which comes bundled with many new computers, it isn't designed to have more than one spread-sheet page open at a time, and you will have to either adapt the examples given to fit, or upgrade to a more capable application which can.

Accounting is concerned with all aspects of the work of a voluntary group which can be measured in money terms, especially

- ❖ Planning what money will be received and paid out in the future
 - We call this budgeting
- ❖ Recording
 - What money has been received and paid out by the group
 - What money is owed to the group and what money is owed by the group and by whom
 - What assets the group owns
- ❖ Classifying and summarising the recorded data so that it can be understood by and made use of by the group
- ❖ Communicating to the group and other interested people and organisations what has been learned by classifying and summarising the data

Bookkeeping is that part of accounting dealing with the recording.

This book aims to provide the essential information on how to manage your money for community organisations running community buildings. It generally assumes that you have several paid staff, income and/or expenditure in the range £50,000 to £150,000, and you (the community organisation, that is,) are a charitable unincorporated association, although it also touches on both charitable companies limited by guarantee and organisations which are not charities.

It aims both to set out the requirements, and to give good practice advice on how your group can meet these. The book tries to strike a balance between covering only the bare minimum essentials and going into too much depth across a wide range of topics. In practice, although it always starts with the basics, where this is required

to gain a proper grasp of good practice – wages and salaries, budgeting and book-keeping, for example – the topics are covered in some depth.

The book isn't intended to be read from cover to cover, but to be dipped into, section by section, as and when you need to know more or be reminded about a topic.

1.3. Accounting Year

Another fundamental choice which will have a profound affect on your accounting records is what is to be your accounting year. If your community organisation has been going for a year or two, the choice has been made for you, but was it the right choice? In principle, you can choose any 12 month period, and, if your organisation is a company limited by guarantee, Companies House will assume that your accounting year end will occur on the anniversary of your registration (actually, the end of the month immediately following the anniversary date of your registration). If your organisation is unincorporated, unless you take action to change it, your accounting year will be assumed to end on the anniversary of your adopting your constitution.

In practice, community organisations generally adopt one of three accounting years

1. Calendar years (i.e. January to December), which is what most private sector organisations and many charities not dependent on central and local government largesse adopt
2. Academic years (i.e. September to August), which is what most voluntary sector organisations whose primary object is the advancement of education adopt
3. Financial years (strictly, 6th. April to 5th. April, but in practice April to March), which is what the majority of the rest of the voluntary sector, especially those dependent on local authority grants, adopt

If you are likely to seek local authority or central government grants, and if you employ staff, it makes your life simpler if you adopt the financial year as your accounting year. The strange date for the start of the government's financial year is a result of two historical anomalies:

1. Prior to 1752, the United Kingdom used the Julian calendar, New Year's Day was on 25th. March, traditionally called Lady Day, and this was also one of the quarter days when accounts were settled. The government of the day used Lady Day, being both the start of the new year, and a quarter day as the start of its financial year.
2. In 1752, the United Kingdom adopted the Gregorian Calendar, with two consequences:-
 - i. New Years Day became 1st. January
 - ii. 11 days were removed from the calendar in September 1752, to re-synchronise the calendar with the solar year (fixing the spring equinox as 21st. March 1753), which resulted in the government financial year starting on 6th. April 1753 (i.e. 11 days later than under the old calendar, but on the same day, going by the solar year), which date it has remained ever since

If you are an existing organisation with a non-standard accounting year, and want to change it to a standard accounting year, this is possible. How you go about it, and its consequences depends on your organisation's legal status.

- ❖ If you are an unincorporated organisation not registered as a charity, you just do it. It is good practice to constrain your change year to be between 6 months and 18 months long, and to recast your previous year's accounts so that they cover the same timescale, but there are no legal requirements
- ❖ If you are an unincorporated organisation registered as a charity, you need to seek the Charity Commissioners permission, and your adjusted year must not be shorter than 6 calendar months nor longer than 18 calendar months. You are restricted to one change of date in any 5 year period, and can't change in successive years. You are also required to recast your previous end of year accounts to cover the revised timeframe
- ❖ If you are a charitable company, you will also need to apply to Companies House to change your Accounting Reference Date, using Companies House Form 225 You must apply well before your existing accounting year end. The restrictions are much the same as for unincorporated charities

If you are a new organisation, the rules are more or less the same as for existing organisations, in that you are permitted to have a first year which is between 6 and 18 months long, but you don't have to provide comparatives with a previous financial year. If you are unincorporated, you normally make the change before registering as a charity, so you don't need to involve the Charity Commissioners. However, if you are a company, you will have to formally change your accounting reference date (use Companies House Form 225).

Throughout this publication, it is assumed that your financial year runs from 1st. April one year to 31st. March the next. If your organisation uses a different financial year, you will have to make the necessary adjustments.

1.4. The Minimum Requirements

What you need, as a minimum is:

- ❖ A set of written procedures for handling money
 - These should set out clearly
 - What has to be done
 - How it has to be done
 - Who has to do it
 - They don't have to cover everything, just the important and the day-to-day
- ❖ A bank account, with instructions that at least two people must sign each cheque
 - This is essential
 - So that you can keep the group's money separate from your own
 - As your first line of defence against dishonesty and impropriety
- ❖ An annual budget, and cash flow
 - The budget is your plan showing
 - How you intend to spend the money over the year
 - Where this money is coming from
 - The cash flow is your plan showing
 - When the money comes in
 - When it goes out
 - so that you don't end up over-drawn
 - Larger projects may need a three year budget and cash flow
- ❖ A bookkeeping system which is written up in full at least monthly, with a bank reconciliation
 - The books
 - Record all monies you receive and pay out in the year
 - Analyse these under the headings you use for your budget
 - The bank reconciliation checks that your records and the banks agree, and if they don't, explains the differences
- ❖ Monthly finance reports that compare actual income and expenditure with the budgets
 - This is so that you
 - Know where you stand
 - Don't get any unpleasant surprises
 - Can work out whether you are winning or losing
 - Can cut your coat accordingly
- ❖ An independent examiner or auditor
 - An independent examiner is somebody outside your group who looks over your books at the year end to check that you are keeping to the rules

- An auditor
 - Is somebody independent of your group
 - Is a qualified accountant
 - Not only checks that you are keeping to the rules
 - Also checks that your books give a true and fair view of your finances

- ❖ Annual Accounts and Reports, comprising
 - Statement of Financial Activities for the year, and the previous year
 - A Balance Sheet at the year end, and the previous year end, broken down into
 1. Unrestricted Funds
 2. Restricted Funds
 3. Endowment Funds
 - A comprehensive set of Notes to the Accounts
 - Your Accounting Policies
 - The report of your Independent Examiner/Auditor
 - The Annual Report , covering
 - Reference and administrative information
 - Structure, governance and management
 - Objectives and Activities
 - Achievements and Performance
 - Financial Review

1.5. The Financial Cycle

All organisations, consciously or unconsciously, follow a “plan, do, review” cycle, in which the work to be done is planned, the plan is put into effect, and the results actually achieved are compared to those planned.

Community organisations are no exception, with the plan being represented by the budget and cash flow, the doing recorded in the books of account and the review being the comparison of actual monies received and paid with those budgeted for. The cycle is annual, with an annual budget and cash flow, the monthly records of monies received and paid forming the books of account, which are compared each month with the budget, and both being summarised in the annual accounts and reports. Accordingly, this book follows the annual financial cycle, starting with budgeting, via book-keeping and monthly management accounts and ending with the annual reports. Other topics are interspersed throughout the cycle, or follow it, as appropriate.

In practice, the yearly cycle is out of phase, since the budget for the following year has to be prepared well in advance, certainly well before the end of the current year, and the annual accounts and reports are prepared well after the current year ends, but the principle, figure 1, still applies.

Chapter 2

2. Writing a budget

A budget is an estimate of the expenditure you expect to incur by carrying out a plan of action and the income that you hope to generate to pay for this expenditure. It can be drawn up by any group of people to cover a particular activity or group of related activities – we call the resulting budgets project budgets - or a period of time, usually a year – we call such budgets annual budgets. In either case, the budget helps you to see exactly what things will cost so that you can make sure you have enough money to carry out your plan.

You need a budget for three reasons:

1. To work out what you can and can't afford to do
2. To set up your book-keeping system. You use the budget headings and sub-headings – we call these line items - as the column headers in your analysis books
3. To find out whether you are winning or losing in financial terms. By comparing your budget to what you actually spend (and raise), you can see any problem areas and take action to put things right by cutting your coat according to your cloth (i.e. adjust either the plan or your activities to suit) before you run into financial difficulties

A budget is often seen as a financial plan, but in reality it isn't the plan itself but an expression of the plan in money terms. We make our budgets to fit our plans, not our plans to fit our budgets. What we call the plan doesn't matter – it may be a work plan, or a business plan – but for an annual budget

- ❖ It must cover the correct time frame, always looking forward into the future. Many people get confused between budgets and accounts. The distinction is simple – budgets look forward (what we plan to do) and accounts look back (what we actually did)
- ❖ It must cover all the activities you want to undertake. If it isn't in your plan, you won't have either set aside any money for it or arranged to find the money to pay for it
- ❖ It must be compatible with your organization's vision, mission and aims and objectives, and, if you are a charity, all planned activities must be encompassed by the objects clause in your governing document
- ❖ It must not just be any old plan, but a cunning plan, with **SMART** objectives We must not only get the job done, but get it done well, and without waste. We live in a competitive world, and have to compete with our peers for grants and bookings, as much as with other voluntary and community groups. Our cunning plan is what helps to give us the edge and get the money in

SMART is an acronym made up from **S**pecific, **M**easurable, **A**chievable, **R**ealistic, **T**ime-bounded.

In order to put together a budget, you need to estimate your incomings and your outgoings – what you get in and what you pay out. You could estimate your income and then plan what you can do within this income. In fact, consciously or unconsciously, this is what we do, or perhaps ought to do, in our private lives. In practice, for community organisations, we estimate our annual expenditure, and then work out how we are going to raise the income to cover it.

One of the decisions around budgeting is when to do it. Ideally, this should be as near as possible to the start of the year to which it applies – February/March for a year starting April. You've then got up-to-date information from your accounts and firmed up plans to work with. In reality, you will not have this luxury. If you want a grant, and local authorities are no exception, the grant givers will want to see your budget as part of their grant-making process. They usually want the grant applications in no later than 6 months before the start of the relevant financial year. That means preparing a budget in September for the following April, when at best, you will have your accounts to August, which is only 5 months into the current year!

Producing a budget isn't rocket science. It involves common sense, the logical approach set out below and simple mathematical skills like addition and multiplication. A basic £5 calculator and some lined paper is all you

really need, though access to a computer spreadsheet program, such as Microsoft Excel, takes a lot of the drudgery out.

2.1. Five Steps to Producing a Successful Budget

1. Preparing the plan
2. Filling in the figures
3. Revising the figures
4. Options and contingency plans
5. Approval

2.1.1. Preparing the plan

Before you can estimate expenditure, you need in principle to express your plan as a list of the activities your group is going to do over the coming year, arranged in logical order, with details of how they are to be done, by whom, when, and with what resources, be they people - paid staff and volunteers – premises, equipment or expenses.

Alternatively, an easier approach which will yield satisfactory results is to start by making a list of all the expenditure headings (line items) you can think of that may be needed by your organisation in the year ahead, see [figure 2](#). If you are starting out, consider any one-off items like recruitment advertisements and any capital items (fixed assets), like furniture and computers, which will last for several years. Also think about running costs, which are expenses of a recurring nature such as rent, rates, salaries, electricity, postage, stationery, telephones, etc. Similar items like salaries and employer's national insurance should be grouped together under the same heading, and keep running cost headings separate from capital cost headings.

Now make a list of all likely income headings such as membership, subscriptions, grants, donations etc., [figure 3](#).

2.1.2. Filling in the Figures

This is the stage which can mean doing a lot of research and involving as many people as possible for their ideas, comments, suggestions and costings. No one person should be expected to produce the budget alone. The more people you involve (i.e. treasurer, other committee members, volunteers, workers, and others connected with the organisation), the better the chance that your budget will be soundly based. There is no magical formula to produce "the perfect budget" - no budget is ever 100% accurate!

If you have been going for years and expect things to go on next year much as they are this year and were last year, planning and estimating is easy - you can use the plan and the figures for this year and last year to project forward into next year, with a small increase to take account of inflation. If, however, your group is new or, as you should, you have plans either to do more, or to do things differently or better, this won't be enough, and you are going to have to start from scratch with the five step process.

In practice, the budget is going to be a mixture of the old and the new, so first, identify those items in your plan which won't change (unless you plan to move), such as office and premises costs and insurance, heat and light, and so on. Then, use the "next year is this year/last year plus inflation" technique. For the other items, you are going to have to do individual estimates.

Now that you have got your plan, estimate the cost of each activity or item of expenditure as realistically as you can. Look in shops and shop windows, and catalogues from stationers, office equipment suppliers, and companies like Argos. Search the internet. For purchased equipment or services, get quotes from suppliers.

For new paid staff posts, use

- ❖ Comparisons with existing staff

- ❖ What the going rate for the job is outside. Look in the jobs section of your local newspaper, for hourly paid staff. For salaried staff, especially if professionally qualified, look at the job adverts in The Guardian's Society supplement (published on Wednesdays)
- ❖ What other groups in the voluntary sector pay for similar positions
 - Many still tie their pay rates to local authority scales (the NJC scales), but this is often for convenience, you don't have to

Don't forget to allow for Employer's NI which is in addition to the salary, not part of it. Currently, employer's NI is 12.8% of the salary, less the first £4,895.

A widely used technique is to read across from a similar activity which either you or your organisation have done before, or more commonly, by talking to people in similar organisations who already do what you plan to, by reading across from them, on the principle that "If it looks like a duck, swims like a duck and quacks like a duck, it is a duck". The psychologists call this technique the "representativeness heuristic", and their research shows that this technique, whilst basically sound, has a catch, which is that we don't make sufficient allowances for the differences between what we did before, and what we plan to do now, or between our organisation and the similar organisation whose clothes we are stealing.

It can help to look at the items of income and expenditure in terms of their behaviour over time, categorising them as fixed, variable or mixed. Fixed items are things whose costs are likely to remain the same throughout the year i.e. rent and rates. Variable items are things likely to change depending on levels of activity i. e. income from hall lettings. Mixed are a bit of both. e.g. call charges on phones will vary with use, but the line rental remains the same regardless of the level of use.

This is crucial - make clear notes of why you included each item, how you arrived at each figure for the cost of an item, and on any items you are not sure about. When we plan and estimate, we make assumptions, consciously and unconsciously. Your plan and estimates are only as good as the assumptions you make, so write them down. Without the notes, you will look back at the figures and will not remember the assumptions you made, even if this was only a few days ago!

Now do the same with each item of income - estimate the likely amounts of income from each source. If estimating outgoings is relatively easy, largely a matter of doing the homework, estimating incomings is always more difficult. Start by talking to funders and other similar organisations, especially about what is realistic. Look into the possibility of charging for your services – there is nothing to stop a charity charging for the services it provides, the only condition is that the trading must be related to its charitable objects. For example, community organisations which are usually charitable, can charge for room hire because this is consistent with their charitable objects, and many charitable supplementary schools charge fees similarly.

Make notes on how each figure was arrived at, and any assumptions which were made, particularly about usage. If it is a guess or broad estimate say so. It is easier if you are carrying out "business as usual", since you can use past and current demand as a starting point. If, however, you are offering something new, it is easy to get it badly wrong. The problem with both the Millennium Dome and the Royal Armouries project in Leeds wasn't that they got their cost estimates wrong, but that they got their estimates of usage (visitor numbers) hopelessly wrong – they were far too optimistic.

2.1.3. Revising the figures

There are three kinds of budget:

1. A deficit budget, where you plan to spend more than you plan to receive. Deficit budgets are a bad idea, unless your reserves (that is, uncommitted cash in the bank) are large
2. A balanced budget, where you plan to spend the same as you plan to receive. Balanced budgets are usually, but wrongly, what voluntary groups aim for, since they assume there will be no mistakes

3. A surplus budget, where you plan to spend less than you plan to receive. Surplus budgets, which is what you should aim for, are often regarded as wrong for voluntary groups - wrong, because surplus is associated with profit. However, if your group is to grow, be able to survive sticky patches, or be able to do more than live hand-to-mouth it, needs to build up a reserve of cash in the bank. This reserve can only come from surpluses of receipts over payments

In setting your budget, in addition to aiming for a modest surplus, to build up the reserves, you should also have a contingency fund, shown as an item of expenditure. This is to take care of small errors and omissions in the budget, and to allow for the reality that you won't be able to be spot on with all your budget items, no matter how hard you try. Note that, by increasing the size of the contingency, a surplus budget can easily be turned in to a balanced budget, if your funders object to surplus budgets.

Having decided to budget for a modest surplus, and prepared a draft budget, show it to the people inside the organisation: workers, volunteers, and management committee members. Make sure you talk to those responsible, whether paid or volunteer, for delivering specific parts of the service.

Has anything been left out? Are extra headings needed? Missing out a heading is the same as giving that item a budget of £0. It is better to guess than leave something out altogether. At the same time, would the budget be simpler and easier to understand if several headings were grouped together?

Check on the items you were not sure about. Is more information needed to improve the accuracy of the estimated figures? On the question of accuracy, the figures in your budget may appear accurate to £1, but except for things like items equipment you intend to buy in the very near future, for which a recent quote is still valid, all the figures are estimates, and therefore approximate. On the other hand, if you round your figures to the nearest £1,000, or even £100 you can give the impression to potential funders that your budget is all guesswork. Rounding to the nearest £10 is a good compromise.

If your budget involves applying for grants, it takes months from application to decision, so when is the funding likely to be received and when are the activities likely to start? Check whether you are using current prices. If you are, and the work isn't going to start for many months, you will need to allow for inflation. Remember that different items will be affected differently.

You are very unlikely to get your budget to come out right first time. Usually, the first time round, planned spend exceeds the likely income. Also, the budget needs to get the backing of all your management committee and your paid staff and volunteers, after all, it is they who have to deliver the plan. For their comments to be taken seriously, there will have to be changes to the budget. Also, you may have to make changes to the budget for cash flow reasons. This shows one of the major complications when budgeting, and that is the need to iterate, that is, to go backwards and forwards through the calculations two or three times

- ❖ To take into account the comments of your staff, your volunteers and your management committee
- ❖ To fill in any gaps, where incomings and outgoings are linked
- ❖ To get incomings and outgoings to balance

Revise the notes. Make sure there is a note explaining how each figure was arrived at. People should understand where all the figures have come from, rather than just trust you with the finances. The notes are an important part of the democracy of your organisation. [Figure 4](#) is an example of part of a budget, together with its notes.

2.1.4. Options and contingency plans

You also need to look at options, that is, alternative courses of action, and contingency plans. You ask yourself “what if?” and then “what do we do if?”

If your budget still shows a shortfall of income over expenditure, what is your organisation going to do about it? Are you going to try and raise additional income, and if so, how? Or are you going to cut back on your plans, and if so, what?

What if your grant applications don't all come through, and you end up with a short fall of income? Can activities be scaled down? Would you cancel or postpone the project? Or would you split it into different phases and just start the first phase? What will happen if some income is late? Should you plan for other unexpected circumstances, and if so, what? Remember it may actually be better for all concerned not to start a project or activity, than to set it up on a shoestring budget which makes everyone panic!

What about the assumptions you made when you were putting the budget together, which should be clearly stated in the notes to the budget? What happens if we change these assumptions, particularly those concerning the number of users? What you should do is to look at how your incomings and outgoings change with changes in these assumptions. It is always better to be pessimistic.

The first year's budget is always the most difficult. A lot of guesses, have to be made because there is no historic information. It is sensible to ask similar organisations about their costs, but remember no two groups are the same. It's very important to include all the likely areas of expenditure, since missing something out is the same as budgeting no expenditure on that item. Be realistic about costs and do your homework and especially be realistic about your ability to fundraise.

There is a lot to be said in favour of community organisations having three year budgets, or even five year budgets, especially when part of a business plan. In any case, if you are seeking funding over three years it is likely that funders will want a budget covering three years. This isn't particularly difficult, but a computerised spreadsheet makes it much easier. You have to consider inflation for each year, changes in levels of activity, old projects finishing and new project starting each year. Either prepare a page for each year, or three columns next to each other - one for each year. Once you start on three year budgets, each year at budget time, you drop the year you are in and add a new year on to the end, revising your figures for the forthcoming year as you go. The additional advantage is that it forces your organisation always to take a longer view and to look at the bigger picture.

If you want to be extra thorough, once in every few years, use the technique called zero base budgeting. In this, every budget line item is set to zero initially, and has to justify its inclusion and any non-zero amount from scratch. “But we've always done it” isn't a good enough reason for including this item. That way, you won't become complacent.

Monthly budgets (or in extreme cases, weekly budgets) are what you need, as is suggested below, if you are to prepare (as you should) a cash flow forecast. I'm assuming throughout this publication that you have access to a computer spreadsheet program, such as Microsoft Excel. This makes preparing monthly budgets straightforward, especially if you have been going for some time and largely base your budgets on what happened in previous years, using the monthly actuals totals from your bookkeeping system. Even if you recalculate each budget item from scratch, you can still use the monthly pattern of income and expenditure to guide you in distributing the incomings or outgoings for each item over the months. If you don't already do so, you are strongly advised to adopt monthly budgeting at your earliest convenience. There is a steep learning curve, but the initial investment in time and effort required will be amply repaid. [Figure 5](#) is an example of such a monthly budget.

2.1.5. Approval

The budget should be presented to your management committee for their comments, alterations and approval. They should check

- ❖ That the budget fits your plans and priorities, both short-term and long-term
- ❖ The assumptions used in setting the budget, set out in the notes, both financial and non-financial
- ❖ That costs have been kept as low as possible

One decision you must involve your management committee in is what items to include in your forecasts of grant income. Typically, at the time for approval, some grant applications will have been granted (i.e. approved), some will be awaiting a decision and some planned applications are only due to be made during the year in question. The issue is as to whether to include grants not yet approved in the budget. Whether or not to include such a grant is a matter of judgement of the chances of the grant being approved, and getting it wrong can be very risky, giving your organisation a false sense of security. If you are not fairly certain that a grant will be approved, do not include it in the budget.

To recapitulate for a moment, making an accurate estimate of outgoings isn't difficult, provided we've done the work before (or know a man who has), we can break-down the tasks into its component parts, we have a way of estimating the cost of the component parts (e.g. for staff costs, by hours of work and rates of pay), we are realistic about how accurate is accurate (don't expect this to be the nearest pound - £5 per £100 is more like it), and importantly, the work is under our control, or at least (most of) the costs are under our control.

Making an accurate estimate of incomings is a different matter! We can only make assumptions about incomings, and only time will tell if these assumptions are realistic.

2.2. Budgeting for Projects

When community organisations apply for funding in the form of grants, what they are seeking is invariably funding for a specific project. This is not from choice, but a simple and inevitable reaction to funder's reluctance to fund the general work of the organisation, and, as a result, a lot of time and ingenuity goes into packaging on-going work into projects, which are essentially short-term.

Community organisations have always depended, to a greater or lesser extent, on donations and grants. Increasingly, these come with strings attached and there is a need to show that the donated or granted money was spent as intended. The justification for the donation or grant is usually a project – a specific task or tasks intended to achieve an objective – which doesn't cover the whole of the organisation's activities. Indeed, it is usual for community organisations to have several projects on the go at the same time, which may or may not add up to the total activities of the group.

Projects are seldom self-contained and free-standing. They normally draw on the group as a whole for administration and other indirect costs, like heat and light, rent and rates, telephones, cleaning and so on and so forth. The direct project costs are those things that relate solely and exclusively to the project, and wouldn't appear in your overall budget if the project didn't exist. Indirect project costs include those items, postage for example and staff time, which although shared, the proportion of which is due to the project can be readily identified and measured. It also includes those items, like heat and light, which are shared, but where it isn't practicable to identify and measure the project's share. How and why your project budget allows for these, thus ensuring that your projects pay their fair share of your organisations overheads is discussed in depth later in this publication under full cost recovery.

Budgets are usually prepared on a functional or organisational basis. That is, broken down either into the traditional elements of wages, heat and light, rent and rates and so on, or into departments or other sub-groups, such as lunch club, playgroup, adult education, and so on. Usually, there will be a bit of both. Unfortunately, when you come to apply for grants, it is unlikely that you will be able to fit your functional/organisational budget into the grant criteria (that is, the rules to be followed to get the grant), and you will have to prepare a

supplementary budget to support your grant application. This supplementary budget, which is a project budget, should be contained within your overall budget, but unless the need is taken into account when preparing the overall budget won't be easy to identify, being submerged within your budget line items.

You prepare a project budget in much the same way as you do an overall budget, by making a list of budget headings, or line items, all of which ought to be in your list of main budget headings or line items. If they aren't, because the project budget headings have been dictated by the grant application form, for example, you need to establish the relationship between your project budget headings/line items and your overall budget headings/line items. In many instances, you should be able to either fit your project budget headings into your overall budget headings, or either combine them into or split them out of your overall budget headings. If you can't, you need to consider recasting part of your overall budget to match the required project budget headings.

Both in principle and in practice, the same strictures about the need to plan, to fill in and revise the figures, to look at options and contingencies, to seek approval which apply to an overall annual budget apply equally to a project budget. There are additional provisos that projects don't fit neatly into one financial year, they often could carry over from one year to the next and always take longer than expected. Experience shows that projects take longer to get off the ground than planned, they hit unforeseen snags, they drag on longer than planned at the end.

It is often said that the last project completed successfully on time was Noah's Ark. The penalty clause for failure, death by drowning for all, clearly succeeded in concentrating minds wonderfully, but is a bit extreme for today's tastes!

Some projects will have only one source of funding, with only one budget and grant application. Others will have several funders, usually with a common budget but separate grant applications. As if this wasn't already complicated enough, many groups have several projects on the go at the same time, each with a budget, and perhaps several funders. Indeed, project budgets will form a major part of the group's overall budget. In such circumstances, it is worth considering turning all the group's activities into projects, doing all budgeting on a project basis, with the overall budget simply becoming the sum of the project budgets. Remember, although we tend to link projects to external funding, there is no absolute law which makes this so. Project can just as easily be internally funded, and many activities which groups undertake are projects, even though they aren't labelled or recognised as such. Even where all the group's activities fall under one project or another, there will still be common services and overheads which have to be shared out across projects, which again is a reference to full cost recovery.

As a reminder of the essential ingredients, here is the recipe:-

Cost your project idea

- ❖ Identify the inputs to your project, that is, the resources you need to put in
 - Money
 - Equipment
 - Buildings
 - People's time, energy and imagination
- ❖ All those you can't give or get for free can be expressed in money
- ❖ This expression in money is the budget

When costing, be realistic

- ❖ Price equipment carefully, don't just guess
- ❖ Get estimates for work you buy in
- ❖ Don't expect people to do the impossible
 - Don't expect to pay peanuts, unless you want monkeys

- ❖ Include a contingency to cover the errors and omissions

Write down your assumptions

- ❖ All plans and estimates depend on assumptions
 - We assume tomorrow will be like yesterday
- ❖ You need to write down how you arrived at the cost of each item in your budget
 - If things go right, you can use the estimate again
 - If things go wrong, what you wrote down will help you to work out why

Check your funder's requirements carefully

- ❖ You may need more than one budget
 - A budget for the whole project
 - A budget showing which part of the project you are asking the funder to pay for
 - A budget for your whole organisation
- ❖ Sometimes, these budgets will all be the same
- ❖ At others, all different

2.3. Further Information

CASH (Community Accountancy Self Help) has a factsheet on budgeting, available on-line at www.cash-online.org.uk/cashfacts which contains lists of typical budget headings, lots of useful tips, and a fully worked example, complete with the comprehensive notes to which your budget should aspire.

This factsheet has a six step process, the first 5 being more or less identical to the 5 steps set out above, and the sixth is monitoring revision, which is treated as a topic in its own right in this publication, rather than as a sub-topic within budgeting, of which it is a logical extension.

Funderfinder, better-known for their specialist software Groups in Need and People in Need, concerned with putting groups and individuals looking for funding in touch with potential funders, also provide, free, software called Budget Yourself, available to download from www.funderfinder.org.uk/freeware.php, whose purpose is to help voluntary groups write effective budgets. Its use is recommended, if you aren't experienced at budgeting, and still worth a look if you are.

Chapter 3

3. Preparing a cash flow forecast

3.1. When is a cash flow forecast not needed?

The short answer is never – all organisations should prepare a cash flow forecast. In practice, you may be able to get away without one, if

- ❖ Your organisation is small
- ❖ Your activities consist of a few one-off events each year, which are self-financing
- ❖ It has a lot of money (relative to your annual turn-over) readily available in a bank current account

3.2. When is a cash flow forecast needed?

The short answer is always, and especially if

- ❖ You don't have much money in the bank
- ❖ Your income and expenditure
 - Are uncertain
 - Are erratic
 - Are regular, but out of phase; that is, although your income and expenditure comes in at predictable times of the year, when you have to pay the money out isn't when you have the money coming in

In practice, few community organisations have a lot of spare cash in the bank and they don't (or shouldn't) generally have lots of large debtors and creditors whose accounts they can manipulate to free up funds, if needed. Accordingly, a cash flow forecast is essential, and monitoring your cash flow should be your primary financial management mechanism.

3.3. Forecasting Cash Flow

If you have done it properly, your budget will tell you what it costs to run your organisation and where the money is to come from to pay for it. What you now need to work out is when the money will be needed (to meet expenses and pay bills) and when it can be expected. This is called a cash flow forecast.

In principle, preparing a cash flow forecast is just a matter of turning your annual budget into a set of 12 monthly budgets, just a simple exercise with a calculator and accountancy paper (i.e. paper ruled into columns, available in any good stationers) or an even simpler exercise using a computer spread-sheet. In practice, there are two complications:

- ❖ Your income won't conveniently arrive in 12 equal instalments, and neither will your expenditure (though if all your staff are salaried, that is monthly paid, a large chunk of it will)
- ❖ Your budget may have been prepared on an income and expenditure basis, whereas what you want for turning it into cash flow is a budget on a receipts and payments basis.

The differences between income and expenditure and receipts and payments were explained in the introduction to this book. If you started your budget from scratch, with a blank sheet of paper, it is likely to be an income and expenditure budget, whereas if you started by using the previous year's actuals, your budget is likely to be a receipts and payments one.

To illustrate, let us consider a budget line item for a new organisation starting from scratch covering staff costs, which we have taken to mean not just salaries but also employer's NI. Assuming (unlikely for a new organisation) that all the staff are in post on day 1, we can break down each salary into net pay, which we pay over to each member of staff at the end of each month, and the employee's PAYE and NI which we have deducted and pay over to HM Revenue and Customs in the middle of the following month, together with the employer's NI. In the first year of operation, we make 12 payments of net salaries, but only 11 of PAYE and NI. Simply dividing our salary budget by 12 would give us an inaccurate forecast of cash flow.

Real life gets more complicated. If, rather than using the annual budget figures divided by 12, what we did, as a going concern, was to use our monthly actuals for the previous year, with an adjustment for inflation, we would show 12 net salary payments, but also 12 PAYE and NI payments, the 12th being the payment made in April this year of the liability incurred in March last year. This gives us a clue about what to do now we have got our annual budget into Excel and have divided each line item into 12 equal amounts, which is to look at each line in our budget and work out whether or not simply dividing the annual budget by 12 is realistic, and if it isn't, make some alternative assumptions. These are easy if you have historical monthly figures to look at, and what you plan to do isn't radically different from what you did then, because the monthly pattern of incomings and outgoings will be given to you. You will, however, have to take into account whether the historic figures are distorted, say by last year's decision to put off paying a bill until the last possible moment, or by a grant cheque being delayed by your funder, because you didn't get that monitoring report back on time.

When trying to be realistic in spreading our annual incomings and outgoings over the months of the year, you need to take into account both when you are likely to receive the bill, or send out the invoice, or receive the grant letter, and when you are likely to get the money, or pay it out. The usual assumption is that there will be a month's delay. If you are starting with a clean sheet of paper (or in our case a new Excel worksheet), there are patterns to incomings and outgoings you can recognise and use. Broadly, these are annual, quarterly and monthly, but you also need to take into account seasonal variations, such as lower use of your community buildings facilities in the summer, and a surge of social events increasing both incomings and outgoings in the run up to Christmas, or other religious festival, and those resulting from their being locked to a different annual cycle, like academic years, for playgroups and supplementary schools, and even holiday play schemes.

Here are some examples, based on a community organisation running a community building:-

- ❖ Salaried staff payments follow a regular monthly cycle, with little or no variation from month-to-month
- ❖ Hourly paid staff hours, and thus payments, are likely to wax and wane in phase with the academic year, being higher during term time and lower during holidays for some, and the reverse for others
- ❖ Hall hire for social events will be at a minimum during the summer holiday season and rise to a maximum in the run up to Christmas
- ❖ Insurances are usually paid annually, in advance, but you can opt to spread the payments over the year, but at an additional cost
- ❖ Heating and lighting costs will follow the seasons of the year, but billing may be quarterly, or even monthly. You can even arrange to pay in equal monthly instalments, but your suppliers will always arrange it such that you overpay
- ❖ Grant cheques from local authorities are often sent quarterly, if you are lucky, in advance, if not in arrears. However, some make one large payment up front, with the balance to come, usually when you have met some pre-condition, often the supply of last year's accounts, or the monitoring form covering the previous year's grants
- ❖ Other funders payment policies should be set out in their conditions of grant. What you want is for them to pay you in advance, so that you can use the grant to pay for the work. What they want to do is to pay you after you have done the work to their satisfaction, and submitted the paperwork to prove it
- ❖ If you supply services to or for large organisations, be they local authorities, other statutory agencies, other groups in the voluntary sector, or even in the private sector (for example, by hiring out your facilities for training), the general rule is the larger they are the slower they will be to pay their bills!
- ❖ Some items of expenditure are entirely under your control, like buying replacements for equipment which is still functioning, but well past its "best before" date. Others, like emergency repairs are by definition outside your control. Where the timing of the spend is entirely up to you, always take into account the cash flow implications when allocating the item in a monthly budget
- ❖ The bill from your accountant and/or independent examiner will always be for last year's work
- ❖ When looking at the previous year's actuals, some of the payments in the first month may be to settle the previous year's bills, and some in the last month to settle next year's, and similarly with receipts

Once you have sorted out your monthly budget and got it on a receipts and payments basis, the cash flow forecast is straightforward. At the beginning of each month, you add the balance from the previous month to the budgeted receipts for the month and subtract the budgeted payments. The monthly balance is the cash flow. An example of such a combined monthly budget and cash flow forecast are shown in [figure 6](#) .

Remember to add the bank and cash balances at the end of the old year to the first month's receipts for the new year. If you prepare your annual budget well in advance of the year, as well you might, you are going to have to forecast these. However, you should always check your forecasts against the true figures as soon as these are available, revising both the monthly budgets and the cash flow forecast as necessary.

If the monthly balances are always "in the black" (i.e. receipts plus balance brought forward is greater than payments) there is no need to worry. If, however, any are "in the red", ((i.e. receipts plus balance brought forward is less than payments) you have problem.

3.4. What if the cash flow forecast shows there will be a problem?

First, don't panic. To find such potential problems in plenty of time to do something about them is one reason for doing a cash flow forecast. The cash flow forecast is just that – a prediction of the future. It is not the future, unless you choose to ignore it. Second, look at your monthly budget:

- ❖ Are there any payments you can delay without upsetting your creditors?
- ❖ Can you put off making a major planned purchase?
- ❖ Is there any way you can bring forward a receipt?

If you can do any or all of these, you now have a revised monthly budget, and a cash flow which doesn't now result in a predicted deficit. If, however, this doesn't do the trick, you will have to consider the following:

- ❖ If the cash flow problem is short term (the end of the summer holidays is a difficult time for many groups, for example), running an overdraft is one solution:
 - Banks are in the business of lending money, and overdrafts are the standard way that many individuals and businesses fix their short term cash flow problems
 - You need to arrange the overdraft before you overdraw – unauthorised overdrafts always cost you more, and there is a risk of your cheques bouncing
 - Overdrafts are a costly way of borrowing longer term, and the bank can call in the overdraft, that is, require you to pay it off, at any time
- ❖ If the problem is medium term, say 2 or 3 months rather than 2 or 3 weeks, some of the options you will need to consider are:-
 - Asking your external funders for an advance
 - Borrowing money from your supporters, without interest, if possible, with interest, otherwise
 - Tackle your management committee members first, but remember, if they are also charity trustees, there needs to be a written loan agreement in place, specifying the repayment terms and the interest rates, and this is good practice whenever you accept a loan from an individual
 - Doing some fundraising to tide you over the sticky patch
 - Borrowing money from your bank in the form of a short term loan
 - If your group is unincorporated, your honorary officers (trustees, if you are a charity) may have to act as guarantors
 - Revising your budget, to cut down on your planned expenditure, or increase your planned income
 - Be realistic about your chances of getting extra income, and don't plan to make savings unless you mean them

If the problem is long term, with a significant overall deficit being carried forward into the next year, and no obvious way to cover it, you are in serious, possibly terminal, trouble. You need to seek professional advice as soon as you realise that you could be insolvent before the next year end, and may have to contemplate drastic action, such as making staff redundant (in itself, not without significant costs) if you or they can't come up with a realistic recovery plan.

Even if you are in the fortunate position to have money in the bank brought forward from previous years which can fill in any gaps between your monthly payments and your monthly receipts, it is still a good idea to look at ways in which you can adjust your monthly budgets to smooth the peaks and troughs in your cash flow. The ideal cash flow is one that is always positive – that is, monthly income always exceeds monthly expenditure. This ideal is seldom attainable for many voluntary organisations, especially those dependent on several project grants, which have a regular pattern of outgoings but irregular patterns of incomings.

What is important is that you have reserves, that is, money in the bank to tide you over any periods where your outgoings exceed your incomings and to cover rainy days – that is, unforeseen expenditure as a result of things not going to plan and, importantly, sources of income suddenly drying up. Reserves are another topic discussed in depth later in this publication.

Chapter 4

4. Bookkeeping

As explained in the introduction, bookkeeping is that part of accounting dealing with recording:

- ❖ What money has been received and paid out by the group
- ❖ What money is owed to the group and what money is owed by the group and by whom
- ❖ What assets the group owns

4.1. The Requirements

What community organisations require is a system of bookkeeping which displays the following characteristics:

- ❖ It should be simple
- ❖ It should require as few books as possible
- ❖ It should not take up too much time
- ❖ It should comply with the requirements, as appropriate and relevant, of the Charities Acts and the Companies Acts
- ❖ It should satisfy major funders and, as appropriate and relevant, inspectors from HM Revenue and Customs
- ❖ It should not involve major help from a professional accountant
- ❖ It should be easily understood by independent examiners or auditors
- ❖ Crucially, it should enable the group to judge, in financial terms, whether they are winning or losing

For community organisations which are charities, whether unincorporated or limited by guarantee, the overriding legal requirement, both books of account to be kept, and for what records are to be kept in those books, set out in Section 41 of the Charities Act 1993, which is reproduced here:-

Charities Act - Section 41

41.—(1) The charity trustees of a charity shall ensure that accounting records are kept in respect of the charity which are sufficient to show and explain all the charity's transactions, and which are such as to—

- (a) disclose at any time, with reasonable accuracy, the financial position of the charity at that time, and
- (b) enable the trustees to ensure that, where any statements of accounts are prepared by them under section 42(1) below, those statements of accounts comply with the requirements of regulations under that provision.

(2) The accounting records shall in particular contain—

- (a) entries showing from day to day all sums of money received and expended by the charity, and the matters in respect of which the receipt and expenditure takes place; and
- (b) a record of the assets and liabilities of the charity.

(3) The charity trustees of a charity shall preserve any accounting records made for the purposes of this section in respect of the charity for at least six years from the end of the financial year of the charity in which they are made.

For community organisations which are neither charities nor companies, there are no specific requirements, but compliance with Section 41 of the Charities Act is best practice, and will be assumed throughout this publication.

In order to comply with these requirements, it is not sufficient just to have a Day Book, figure 7, in which are recorded “entries showing from day to day all sums of money received and expended by the charity, and the matters in respect of which the receipt and expenditure takes place”, nor is it acceptable to put all receipts for moneys received into one shoe-box and the bills showing moneys paid into another, to be sorted out at the year end.

A Day Book - a cheap A4 desk diary, for example - is a useful aide memoir for organisations which can't make up the books on the day. The shoe boxes are useful repositories for the paperwork until it can be processed and filed, but they are no substitute for proper books of account. In this context this means analysis books in one

form or another, either traditional ledgers, in the form of a "Cash Received Analysis Book" for cash and cheques received and deposited in the bank account and a "Cash Paid Analysis Book" for all expenses paid by cheque. This publication assumes you are using a Microsoft Excel workbook, whose worksheets serve the same purpose, and are, in large measure, just electronic versions of the paper ledgers. We call them "Analysis Books" because each entry in these books, either physical or electronic, is analysed across into headed columns which relate directly to the headings used in preparing the budget. This is why we write the budget before we set up the book-keeping system, so that we now what our analysis column headings are.

Also, again, in order to comply with the requirements, we not only need to keep up the books and file away the supporting paperwork, but also to keep them up-to-date. This means that they need to be made up as you go along, not left to the end of the month, quarter or year. For a community organisation, by and large, this means that the books should be no more than a week behind i.e., that entries should be made in the books not later than a week after the transaction actually occurred.

The single entry book-keeping system, using Microsoft Excel Workbooks (or any similar computer spreadsheet program) will not only satisfy the legal requirements, but will also exhibit all the other desirable characteristics for a book-keeping system. The Workbooks will hold all the details of your group's income & expenditure in one place, and provide you with the information you need to manage your group's finances:

- ❖ How much money you have received in each month and year
- ❖ What it was given to you for and how you spent it
- ❖ And the totals of each type of income - fees, membership, donations - and expenditure - petty cash, wages, travel, hall hire - for each month and year

The information allows you to monitor what is happening with your group's finances:

- ❖ Are you spending too much on certain things
- ❖ Are you receiving as much money as you had hoped and expected, etc.

Having this information allows you to make choices:

- ❖ If the incoming money that you are receiving is less than expected you can change your groups' spending habits to ensure that you do not go overdrawn.

4.2. Filing

Most books on accounting will mention that you should be able to justify every entry in your accounts books (in our example, an Excel work-book) by having on file one or more pieces of paper relating to every entry. However, they often fail to stress that this is paramount, and never more so than when using computer software, such as Excel, where mistakes can be corrected and adjustments made without leaving any trace.

You know you have got the filing right when your account books can be recreated from scratch just by referring to the filed documents. We call these paper records justifying and explaining each entry 'vouchers'. Confusingly, sometimes when we talk about 'vouchers' we mean the supporting documentation, and sometimes we mean a form to which the documentation is attached on which we record details like the cheque number, the reference number we have allocated to the documentation, the analysis classification (the column heading in our books) and the project (if applicable), and so on and so forth. We may also use such a form to get a cheque prepared and to authorise payment. We may choose not to use such a form, either writing details like reference and cheque numbers on the bare documentation, or using a rubber stamp to print a blank voucher on to the documentation. Precisely what we do and how we do it isn't important. What is important is that we don't just rely on the form, but always (in so far as is reasonably practicable) support the form with other documentary evidence, ideally originating outside our group.

There are 3 cardinal rules when it comes to filing:

1. Get everything and keep everything – receipts, invoices, statements, wages records
2. Keep everything in order - keep one file for income vouchers and another for expenditure vouchers, keep

them in order – chronologically by date received or paid

3. Cross reference everything - things need to be linked together so that you can find, for example, the receipt that relates to a certain cheque, give each piece of paper you file away a unique reference number, and use this number as the reference in your accounts books

4.2.1. What should we use as the reference number?

Precisely what you use isn't important. What is important is that each number should be unique, with each entry line in the accounts having its own unique reference number.

For items of expenditure, it is customary to use cheque numbers. However, if you make payments by electronics funds transfers, credit or debit cards or cash, there won't be a cheque number to use, and you will either have to have one system for cheques and another for all the other payments, or to allocate each transaction a unique number. I prefer to do the latter, in the form xxoutyyy, where xx is the last 2 digits of the year, and yyy is the next number in the sequence which started at 001 with the first payment in this year. I am, and you should be, careful always also to write the cheque no. on any documentation covering a payment by cheque. Alternatively, you could photocopy each cheque, after it has been signed and countersigned and attach it to the payments voucher.

For items of income, what to use as the equivalent of the cheque number is not so obvious. You could use the paying in slip number, indeed you should write the paying in slip number on the income voucher, but there are two difficulties with this:

1. Some banks don't number their paying in slips
2. There may be several, sometimes many, income vouchers covered by one paying in slip

The first is an easy problem to solve. If your bank don't number your paying in slips, you must.

The second can't be solved, since it isn't possible to generate the required unique number for each voucher.

For money you receive by cheque, you could use the number on the cheque. However, this may not be unique – several people might be writing cheques payable to you over the course of the year with the same number, and you will have to add in the payer's account number and even the bank sort code number to be sure that the number will be unique in your records, making the number very long and complicated. In any event, you should, wherever possible, photocopy each cheque you receive and attach it to the income voucher.

For money you receive in cash you could use the number on the receipt (from a duplicate receipt book) you gave the payer to acknowledge the money. However, you will now have one complicated system for cheques, and another, albeit simpler system, for cash. As with payments, or I prefer to allocate each transaction a unique number, in the form xxinyyy, where xx is the last 2 digits of the year, and yyy is the next number in the sequence which started at 001 with the first receipt in this year. I am, and you should be, careful always also to write the paying in slip no. on the supporting documentation.

4.2.2. What documentation is acceptable to confirm that you received the money?

- ❖ For grants – a letter from your funder showing the amount of the grant, what it is for, and how it is to be paid to you (where the grant is restricted, you should attach a copy of the grant conditions)
- ❖ For room hire and lettings – a copy of your invoice, together with evidence (for cash, a signed receipt, for cheques a photocopy of the cheque) that the invoice has been paid
- ❖ For fees – for cash fees, a signed receipt annotated to show what the fees were for, for fees paid by cheque, a copy of the cheque annotated to show what the fees were for

Remember always to show on the documentation, or on the covering voucher, which of your budget headings each item of income comes under.

4.2.3. What documentation is acceptable to show how you spent the money?

- ❖ For equipment - an official supplier's invoice (showing their name, address, VAT number etc), clearly showing the goods supplied to you, receipted as having been paid by you, and/or supported by evidence that it was paid by you
- ❖ For smaller items - a store receipt (write on it what the item was, if it's not written clearly on the receipt)
- ❖ For food/refreshments - a store receipt (from the day of purchase/day before the event if they are perishables) showing the purchase of appropriate items; it is always best if the receipt contains only items for your community organisation - if it also has personal items on it, you need to cross them off and subtract them from the total
- ❖ For sessional fees/professional fees/childcare – either an invoice from the person you employed to provide the service showing their self-employed tax code, supported by evidence you have paid the invoice, or evidence that you have paid them through your PAYE system
- ❖ For volunteer expenses - proper paperwork (e.g. travel tickets, lunch receipts) that shows that the amount paid is a genuine reimbursement of actual expenditure, not just round sum payments (which would make the person liable to tax and also expose you/your organization to risk of prosecution)
- ❖ For travel expenses - clear evidence that the amount paid has been expended (e.g. tickets, petrol receipts for appropriate amounts that fit the journeys described, child fares as appropriate); if you are a local organisation in a big city, it is unlikely that you should be reimbursing multi-zone travel cards, so if you need to, you will need to explain why
- ❖ Stationery/postage - need proper receipts. If you buy a large number of stamps you should also explain what they were used for
- ❖ Room hire - an invoice (receipted as paid by you) from the venue specifying dates, times, and hire rates of facilities used or a cash payment receipt supported by the venue's booking form showing the dates, times, and facilities used

Remember always to show on the documentation, or on the covering voucher, which of your budget headings each expense comes under.

Note that petty cash vouchers, figure 8, on their own are generally not sufficient evidence of spend on their own - they can serve as evidence of cash payment if signed by the recipient, but will need to be supported by travel tickets, lunch receipts or invoices as appropriate.

4.2.4. What if there isn't any documentation?

The simple answer is that you will have to make some. For example, if you decide to pay expenses to one of your staff or volunteers who have lost the ticket or receipt, you need to put in a note explaining this, and what circumstantial evidence you took into account in making the decision to pay.

Note that, though a receipt is highly desirable, it isn't strictly required, provided that there is reasonable certainty that the expense was incurred. For example, if someone went out to get a plastic container of milk, and lost the receipt, you would have the container of milk, so there is reasonable certainty that the expense was incurred,

and with any luck it might have a price tag on it, providing evidence of the price paid. There will also be occasions where there will be no receipt, one of the most common being claims for vehicle mileage. In such circumstances, it falls to the person authorising the claim to apply the "reasonable certainty" test.

4.2.5. Filing Systems

Keeping the Cash Analysis Books up to date and properly reconciled is a large part of the accountability process, since this information tells you where the money has come from and who it has been paid to. However, the supporting documents are equally important as they provide the evidence of why the money has come in or gone out.

This means all the supporting documents need to be filed and referenced so that any queries can be easily answered by reference to the relevant documents. The following diagram shows how different parts of the filing system relate to each other, and combine to provide a "trail" for each receipt and payment. This trail should enable you to follow through any transaction from start to finish.

Lets take an example: you decide to order some goods from your stationery catalogue, and you receive an invoice which you file in the "unpaid invoices file". When you pay the invoice you write the details on the cheque stub and the cheque number on the invoice which you then file in the "paid invoices file" in cheque number order. The payment will be entered in the Cash Book using the details on the cheque stub and if any one queries the payment, you can produce the supporting documents from the file simply by reference to the cheque number.

You can develop whatever system suits the needs of your organisation, but here are some basic suggestions:

- 1 . Keep all documents in ring binder files - if they are just pushed into wallets they will invariably get muddled and out of sequence
2. The key to a good filing system is referencing everything in a logical order. For paid invoices, use the cheque number as your reference, and file in number order. For your income documents, start from 001 at the beginning of each year using the reference column in the Cash Received Analysis Book and filing in this number order
3. Keep income documents separate from expenditure documents
4. Keep a permanent record of all capital items (i.e. equipment, office furniture, vehicles etc.). This should include a brief description of each item, the serial number, its cost, the supplier and where it is kept. If you dispose of any item, make a note of the date and sale price (if any)
5. Keep copies of all committee meeting minutes, especially those about financial decisions
6. And lastly, do not throw all this evidence away once your auditor has agreed your accounts. To be safe, you should keep it for a minimum of six years

4.3. The Excel Workbook

We could just simply duplicate the three traditional paper ledgers in Excel, with one Workbook for each ledger, that is the Cash Received Analysis Book, the Cash Paid Analysis Book and the Petty Cash Analysis Book, with each sheet in our workbook representing a page in our ledger. We'd have the added flexibility of being able to make our pages longer or shorter, so that we could comfortably fit each month's transactions on a single page, and the cross-casting and down-casting (that is, adding up the row and column totals) could be made automatic. We'd also not be constrained by the number of columns in our paper ledger, and could easily arrange either for

page totals to be carried over onto the next page, or to be totalled onto a separate work-sheet. Indeed, there is a lot to be said for this approach, which has the added advantage of familiarity.

However, we can go further, and combine both the Cash Received Analysis Book and the Cash Paid Analysis Book into a single work-book, with each worksheet recording and analysing one month's receipts, whether in cash or by cheque and one month's payments by cheque. This has the added advantages that we can keep a running balance as we go along, and makes the bank reconciliation easier. How to do a bank reconciliation is the subject of a later chapter. On the 13th worksheet of our workbook we summarise each month's transactions, and provide yearly (and quarterly, if required) running totals.

4.3.1. Preparing the Workbook

An example of a receipts and payments analysis worksheet from a workbook freshly prepared for a new financial year is shown in [figure 9](#). Essentially, it is separated into three groups of columns, the left hand group of columns being the day book, the centre group the receipts analysis book and the right hand group the payments analysis.

The column headings in the daybook group, and the purpose of each column, are as follows:-

- ❖ Date – the date of the transaction
- ❖ Payer/Payee (note – not details) – who, by named individual or organisation, the transaction was with. Payer, for receipts, payee for payments. Often, this column is called “details” and tends to be just a narrative repeat of an analysis column heading, which is a waste of time, and a failure to comply with the Section 41 requirements
- ❖ Reference – the column in which you write down the unique reference number of the transaction. See the section on filing for further details
- ❖ Cheque/Paying In Slip No. – this column is optional – the number on the cheque, for payments, and the number on the paying in slip used to deposit the moneys in the bank. These should be written on the supporting paperwork, in any case.
- ❖ Project/fund Identifier – a column used to record which project or fund the transaction belongs to. Its use is explained in the section on Project and Fund Accounting
- ❖ Receipts – the amount of an incoming transaction (in £ and p)
- ❖ Payments – the amount of an outgoing transaction (in £ and p)
- ❖ Balance – the running balance, obtained by adding the receipt in the row to the previous row's balance and subtracting the current row's payment. In practice, an entry in a row will be either a receipt or a payment, never both.
- ❖ Reconciled – another optional column, but useful to record (I use a small r) that the entry in the row has been reconciled with the bank statement

In the Receipts group of column headings, the column headings should be the same as the line items in your budget. The final column in this group is a total column, which should be set to sum all the receipts column entries in each row. There may be more than one column entry in each row e.g. if a member pays their subscription and settles an invoice with a single cheque, but the amount in the total column must equal the amount in the corresponding row in the receipts column. There is one column heading which isn't a budget line item, and that is entitled Sundry Receipts (or Miscellaneous Receipts, or Other Receipts, or whatever). This is for those small and/or infrequent items of income which don't fit under your other headings, even broadly interpreted.

Similarly, in the Payments group of column headings, the column headings should be the same as the line items in your budget. The final column in this group is a total column, which should be set to sum all the payments column entries in each row. There may be more than one column entry in each row e.g. if you reimburse the Secretary by cheque for her expenses over the previous, there may be entries in several columns in the row, e.g. travel, stationery, postage, telephone, and so on, but the amount in the total column must equal the amount

in the corresponding row in the payments column. Here, there will be two column headings which aren't a budget line items. The first is the equivalent of that in the Receipts group, and is entitled Sundry Payments (or Miscellaneous Payments, or Other Payments, or whatever). This is for those small and/or infrequent items of expenditure which don't fit under your other headings, even broadly interpreted. The second is headed Petty Cash, and is used to record the transfers (by cheque made payable to cash) made from your bank account to your petty cash account.

Wherever possible, your analysis column headings should be the same as your budget headings. However, perhaps you have, for historic reasons, done it the other way round, and made your analysis headings your budget headings. Or, perhaps you use different headings in your analysis books from the ones you use for budgeting. In either case, you should consider changing you headings, because in neither case will the headings stand up to close inspection against a budget prepared from first principles. Sometimes, your management committee have got so used to the headings that you are effectively stuck with them. In this situation, it is up to the treasurer to embark on a re-education programme.

Only you can decide what your analysis column headings should be. They shouldn't just come out of a book, or be copied from some other group, they must suit your organisation's needs. There is nothing wrong with using text books or other group's accounts as a starting point, provided you change them to suit your needs, and don't just slavishly copy what somebody else has done. The headings in my example (figure 6 refers) are lifted from the analysis books of the Rhomboid Community Association, and suit their budgeting bookkeeping and management needs. They may not suit yours.

The temptation with an Excel –based set of books is to have a lot of analysis columns, because you don't have the limited number of column constraints of a paper ledger, and headings which used to be combined in your manual books, like say light and heat, suddenly have a column each. Don't fall into the trap of getting into too much detail, either in your budgeting or in your book-keeping. If you have only one or two entries in a column in a year, consider combining this column with another that also has only one or two entries. e.g. accountancy and insurance, where you may only make one payment for each in a year. You can still pick out individual items, if you need to. Also, if a column has only very low value entries, and the yearly total of these entries is small in proportion to your total expenditure, put these items into the Sundries column, don't keep a separate column.

If you have so many headings that the number of columns is getting unwieldy,

- ❖ Check that you don't have too many budget headings/line items – you shouldn't need more than 24 or so for receipts and 36 or so for payments
- ❖ Consider combining headings, as outlined above

If all else fails, you will have to resort to keeping your receipts on one worksheet and your payments on another. If you are in this situation, bow to the inevitable, and buy bookkeeping software (though even here, it pays not to have too many analysis headings).

Don't forget to identify on prominently on each worksheet

- ❖ The name of your group
- ❖ The name of your worksheet
 - That is, Receipts and Payments Analysis Book
- ❖ The calendar month and financial year to which the entries relate

4.3.2. Preparing the Filing System

Before you start using your Excel Workbook for the first time, you also need a lever arch file, or files, and a set of dividers, in which to file the supporting documentation. What supporting documentation you need and why you need it is explained at the beginning of this chapter under documentation. You prepare the lever arch files as follows:-

- ❖ Using the dividers, set up the following sections:-

- A section for receipts
- A section for payments
- A section for bank statements and bank reconciliations
- A section for creditors (people you owe money to).
 - When you get an invoice (a bill), you put it in this section until you get round to paying the bill, when you transfer it to the payments section, in the course of keeping the books
- A section for debtors (people who owe you money)
 - When you send out an invoice, you put a copy in this section, until you receive a cheque or cash to settle it, when you transfer it to the receipts section, in the course of keeping the books
- A section for capital items purchased. This will become your asset register
 - When you buy a capital item (something like a computer which
 - Costs a significant amount (£100s, rather than £10s)
 - Isn't consumed in the course of your group's activities,
 - Will be used for several years)
 you file a copy of the invoice showing
 - What the item is
 - When you bought it
 - What you paid for it.

4.3.3. Using the Workbooks

You use the books as follows:-

Consider first a payment made by cheque, say for a quarterly telephone bill.

- ❖ In the Receipts and Payment Analysis Book, you enter the date, the payer – the name of your telephone company (BT, or NTL, or whoever) the reference (in my system, the next number in the xxoutyyy sequence), (optionally) the cheque number, and the amount in the payments column, which should be automatically deducted from previous balance and put as the new balance in the final daybook column. You also enter the amount in the appropriate analysis column, e.g. telecoms (which could cover both phone line and broadband internet rentals and usage charges). Figure 10 shows the entry.
- ❖ In the Lever Arch File:-
 - You file the telephone bill in the payments section, either writing on it
 - The unique reference number
 - The cheque details (number, amount, date on cheque, who signed),
 or attaching a photocopy of the signed cheque. Alternatively, you attach to the bill a piece of paper (or a form) which records these details. We call such forms a cheque requisition.
 - If the payment isn't for something obvious, you'll need to provide an explanation, either on the bill, or the cheque requisition, or another piece of paper

Now look at money received, say a grant cheque:

(Note that, if you are following the rules, all receipts should be paid straight into the bank, so whether cash or cheque, the process is the same)

- ❖ In the Receipts and Payment Account Analysis Book, you enter the date, the payer – London Borough of Ealing, for example - the reference (in my system, the next number in the xxinyyy sequence) and the amount in the receipts column, which should be automatically added to the amount of the previous balance and put as the new balance in the final column in the daybook group. You also enter the amount in the appropriate analysis column. In our example, Restricted Grant. Figure 11 shows the entry
- ❖ In the Lever Arch File:-

- You file the remittance advice (the paperwork which came with the grant cheque) in the receipts section, either writing on it
 - The unique reference number
 - The cheque details (bank, branch, sort code, account number, cheque number, amount, date on cheque)
 or attaching a photocopy of the cheque as received
 - or
 - Attaching it to a piece of paper (or a form) which records these details
- If the receipt isn't for something obvious, you'll need to provide an explanation, either on the remittance advice, the covering letter, or another piece of paper

Most receipts and payments will be for an item falling under a single analysis column heading, but this won't always be the case. For example, a cheque may be received that might pay for fees, and membership subscriptions in one. This would be entered in one line: date, payer, reference, paying in slip number, total amount received, then the total amount split between the two relevant columns headings. In practice, the most common entry requiring analysis under several column headings will be payments made out of petty cash, which is covered in the section on petty cash under the Imprest system.

If you are keeping your books on a monthly basis, as is assumed, at the end of each month, check that the totals for each column have been added up correctly, by both cross-casting and down-casting, (adding up across the rows and down the columns, and vice versa) and that the totals from all the analysis columns onto have been correctly carried forward onto the summary work-sheet and entered in the appropriate row for the month in question. When you are calculating these check totals for a worksheet in your workbook, remember to total up the analysis columns both across the page and down the page, comparing the two answers you get with the answer you got by totalling up the Total column. All three answers should be the same. If they aren't there is a mistake in the formulae you have built into the worksheet. The commonest reason for this is your having added or deleted a row or column, by accident or design, and inadvertently excluded the row or column from the summation formula.

If you are a small community organisation, and have only a few transactions each month, it is acceptable to operate your workbook on a quarterly basis. That is, with each worksheet covering a 3 month period, and each row in the summary corresponding to a quarter, rather than a month. For very small groups, with only the occasional transaction, it is permissible to keep going on a single worksheet until either the number of rows becomes excessive (say over 240 rows), or the end of the year comes, whichever is sooner. If you fill much more than 240 rows in a year, you should consider keeping your accounts on a quarterly basis.

Don't get too concerned if all your entries aren't strictly in date sequence. If you overlook something or find out about an electronic funds transfer or bank charges only when you get a bank statement, add it in on the next available row. Don't be tempted to insert a row or sort your data by date order – you risk upsetting the formulae you have built in to your worksheets, and having to spend extra time and effort in finding and correcting the resulting errors.

Also, don't get too concerned if you make a mistake. Although the purists might insist that you reverse the original entry, (putting it in again as a minus amount) to cancel the mistake, before making the correct entry, it is acceptable these days just to correct the original entry.

There are a couple of circumstances when you really ought to reverse an entry, and these are

1. When a cheque you have received "bounces" (i.e. the issuing bank refuses to honour it, usually because the payer has insufficient money in their account)
2. When a cheque you have issued becomes time-expired (i.e. it was written out more than 6 months ago) before it is presented for payment

In the first instance, you repeat your original entry, but with an equivalent minus amount in both the receipts and appropriate receipts analysis columns, whereas in the second you repeat your original entry, but with an equivalent minus amount in both the payments and the appropriate payments analysis columns. Figure 12 illustrates these. Do not be tempted to enter the bounced cheque as a sundry payment, or the timed out cheque as a sundry receipt. If you do, you will overstate both your payments and your receipts.

At the beginning of the first month that you start to use your analysis workbook, you will need to put the balance of the bank account in the first row of the balance column in the first month's worksheet – a positive number if you are in credit, a negative number if you are overdrawn. This will ensure that the running balance from then on accurately shows the total amount of funds at your disposal, and can be directly compared with your cash flow projection. The date you use is the first day of the financial year, and in place of the payer/payee, you put Balance Brought Forward.

One other regular task you will have to carry out is to compare your analysis workbook with the bank statements. We call this, which is dealt with later, doing a bank reconciliation.

Figure 13 illustrates the relationship between the books of account, the cheque book and paying in book, the files of supporting paperwork and the bank statements.

You will also need

- ❖ To print out the spread-sheets regularly, ideally weekly, but at least once a month, filing the print-outs in a lever arch file
- ❖ To make and keep back-up copies of the computer file, in case the computer breaks down or the master file gets corrupted. You should do this every day you enter data.

4.4. Double Entry

Double entry book-keeping and keeping Books of Account using this technique are outside the scope of this publication. However, your bookkeeper, treasurer or somebody else in your organisation will need to have a good grasp of double entry book-keeping before you go down the accounting software route. If you want to learn double-entry book-keeping, the easiest way is to sign yourself up for a course of evening classes at your local College of Further Education. Basic courses, lasting a year, will be offered at GCSE and RSA/NVQ Level 1, some of which will be subsidised and therefore cheaper. Text-books are also available, in the local library, or in book-shops. Those in the Made Simple and Teach Yourself series are most appropriate for home study. You may also find suitable books in second-hand bookshops. The principles of double entry book-keeping were worked out by monks in the middle ages, and have changed only in detail since then, so old text books, although not matched to existing examination syllabuses, are still generally applicable.

4.5. Alternatives to Spread-sheets

4.5.1. Traditional Manual Books

If you aren't into computers, or can't cope with spreadsheet programs, or are used to manual books, traditional ledgers are perfectly satisfactory. Suitable hard-backed analysis books are widely available through stationers. Three books are usually required, designated the Cash Received Analysis Book, the Cash Paid Analysis Book, and the Petty Cash Book. In this instance, cash doesn't literally mean notes and coins, it means money. The purpose of each book is spelled out by their names,

- The Cash Received Analysis Book records all the income – notes, coins, cheques, electronics fund transfers – received by the group, and analyses this out under various column headings which should match your budget headings
- The Cash Paid Analysis Book does the same, but for all monies coming in
- The Petty Cash Analysis Book is a subsidiary book, recording and detailing all the minor purchases made using the money kept in your petty cash box

Normally, it is one page per month, though groups with lots of transactions may need to make it one page per fortnight, or even week, and groups with few transactions may be able to get away with one page per quarter.

When choosing the books to use, the golden rule is the more columns the better. Neatness and legibility are important, and, since good practice requires the entries to be in ink, correcting mistakes is an issue, since the use of correcting fluid is frowned upon. Ideally, mistakes should be corrected by striking through the original entry and writing in the correction as close as possible to the original entry in a different coloured ink. Unless you are a wiz at mental arithmetic, a calculator is an indispensable accessory.

As with a spreadsheet based system, all entries need to be explained and justified by a piece of paper neatly filed away, and one of the columns in each book must be assigned to the unique reference to be written both in the column and on the filed piece of paper.

Assuming that you have a just bank account and a petty cash account, you will need three account books. These are-

1. A bank account book
2. A receipts and payments account analysis book
3. A petty cash account analysis book

The account books used for single-entry book-keeping are made up of pages on which there are a number of columns and rows, with a wide column to the left for narrative, and narrow columns to the right for analysis. They can be purchased from most high street stationers. The hard-backed bound books usually have 96 pages, and can be expensive. In principle, you can use them for several years, but in practice, since they have to go off to your independent examiner or auditor each year, you may need a new set each year. However, if you shop around, you can find 32 page soft-backed stapled books which are just as suitable, and 1/5 the price.

Resist the temptation to buy combined income/debit and expenditure/credit analysis books, sold as 4/16 column analysis books, or similar. These are designed for small businesses, and you will soon find that they don't have nearly enough income analysis columns.

You are also going to need a large lever arch file and a set of file dividers. In this you will file the supporting paperwork.

- ❑ What you need for the bank account book is a three column analysis or treble cash account book
- ❑ What you need for the receipts and payments account analysis book is a sixteen or twenty (or more) column analysis book, either across two pages, or landscape ruled across single page.
- ❑ What you need for the petty cash account analysis book is a seven (or more) column analysis book

4.5.2. Off-the-shelf Manual Book-keeping Systems

For those groups who need additional help, there are a number of manual book-keeping systems on the market, which come with pre-prepared column headings and step by step instructions. These are also readily available at stationers. However, all but one are designed for commercial businesses, especially those who make lots of cash sales, and want weekly accounts, and all share one limitation when applied to voluntary groups, which is that they don't provide for analysis of income. Apart from being not for profit, the one other feature which differentiates voluntary group from businesses of equivalent turn-over is that they have several significant sources of income, not just or primarily the sale of goods or services.

The one exception is the Simplex T6 Accounts Book for Club and School-fund Treasurers, available by mail order from George Vyner Ltd., PO Box 1, Holmfirth, Huddersfield HD7 2RP (tel. 0484 685221) at around £10, plus post and packing. This comes complete with examples and instructions all set out ready for use. All you have to do is tailor the headings to your group's needs, and follow the instructions. However it is only really suitable for very small and small groups, especially those collecting subscriptions, who don't have lots of complicated transactions, and don't need anything more than basic receipts and payments accounts, such as for example, the sections within a community association. As with any system, all entries need to be justified by filed evidence.

Some national umbrella bodies also publish accounts books tailored specifically to the needs of their members. For example, the Pre-school Learning Alliance produces such books for Play-groups (which are free to their members).

For small groups needing something better than Simplex T6, but wanting something easier than the do-it-yourself system described above, the Simplex D Accounts book is one of the most widely available, and is well supported. A better alternative is The Best Small Business Accounts Book (Blue Book Version) published by Hingston Publishing Co., Honeymoon Lodge, Eaton Bishop, Hereford.HR2 9QT (tel. 01981 251621), available either by mail order or in Ryman's shops for ££10.50. However, neither provide for analysis of income.

4.6. Asset Register

Section 41 of the 1993 charities act requires the trustees to maintain a record of the assets and liabilities of their charity, yet this is one area where trustees commonly and consistently fail in their duty. Without such a record of assets and liabilities, even eligible charities opting for receipts and payments accounts cannot prepare the required Statement of Assets and Liabilities, which is after all just a summary of this record at the charity's year end.

In practice, it isn't all assets and liabilities which charities fail to track, since current assets, like invoices sent out but not paid, and the bank balance, and current liabilities, like bills awaiting payment, are or should be tracked

as part and parcel of maintaining the books of account, but fixed assets. Fixed assets are those items which last several years and aren't used up in the normal course of activities. Examples of fixed assets are

- ❖ Fixtures and fittings
- ❖ Office furniture
- ❖ Computers and office equipment

Fixed assets form part of an organisation's capital, and accountants talk about such items being capitalised, with their cost spread out over the life of the item. In principle, any item out of which we get several years service should be capitalised, even if they only cost a few £, like a hole punch or a stapler. In practice, we apply one of the accounting principles which will crop up from time to time in this publication and that is materiality, or significance. What this principle says is that we don't need to take account of items or amounts which are too small to bother about. In other words, whether you include them or not won't make a worthwhile difference to the totals. So, we realise this principle by adding another definition to long life and not being consumed, and that is cost a significant amount.

There is no hard and fast rule on what constitutes a significant amount - it depends on the relationship between the cost of the item and the size of your group, your annual turn-over and the life of the item, but a useful rule of thumb for community organisations is only to capitalise items which

- ❖ Have a life of 2 or more years
- ❖ Cost more than £100

This means that we don't capitalise our hole punch or stapler, but charge their entire cost – write them off, in accountants' parlance – as soon as we purchase them. As ever, there is an exception to that rule, and that is where you own or purchase a lot of low value items, which individually aren't of significant value, but collectively are. For example, if you have small hall which has 10 tables costing £50 each, and 60 chairs costing £10 each, the total cost of hall furniture is £1100, which is significant in anybody's books, and you should capitalise them, even though individually they cost less than the £100 limit.

We call the book, electronic spreadsheet, file or whatever in which we record and keep details of all the items we wish to capitalise our asset register. In principle, it should also record our current assets, but in practice they are already covered elsewhere in our books and records, so in practice our asset register will be a register of our fixed assets.

If you are a new organisation starting from scratch, the easiest way to build up an asset register is to put into a suitable loose-leaf file a copy of the purchase invoice for each item satisfying your capitalisation criteria. It is good practice to allocate a unique number to each invoice, and to mark this unique number on the item itself. When you dispose of a fixed asset you also need to make a note of this in the lever arch file, recording the price you got for it (or the cost of disposing of it). For an existing organisation, this is also the best way of maintaining an asset register, once you have got on top of it.

If you have been going for some years, and have so far failed to do your duty and maintain an asset register, you are going to have to start by taking an inventory of all the non-consumable items in your community building which would cost you significant money to replace. You could make this a paper exercise, by going through all your purchase invoices for previous years, lifting out the ones for capital items, but even if these are still in the boxes they came back from your independent examiner in, and tucked away in the cubby-hole under the stage, this is going to be a major task, and there is no guarantee that you still have the items, and what about all the stuff which you begged borrowed or stole, or didn't capitalise, not knowing any better? In the end, you are going to have to do a physical inventory of all the fixed assets in your building, recording what it is and where it is, and giving it a number, which you mark on it and on the paperwork.

Be prepared for a shock when you come to work out not only what it all cost you (which may be a problem with older items, especially those you have inherited from a previous regime but also what it will cost you to replace them. This figure is important for working out whether your insurance cover is adequate (it won't be!).

Whereas all your other accounting records are annual, to be filed away at the end of each financial year, the assets register is perpetual, being carried forward from one year to the next, with new items being added as they are purchased and old items removed as they are sold or thrown away. Once your register is up and running, it is good practice to carry out an inventory of all the items in the register at the end of each year, or the beginning of the next year to

- ❖ Check that you still have the item
 - If you don't, find out what has happened to it
 - Unexplained disappearances of fixed assets should be treated every bit as seriously as unexplained disappearances of money. For desirable items, like mobile phones, PDAs, laptops and the like, you should consider making these the personal responsibility of their principal users, with loss or damage without reasonable excuse a disciplinary matter.
- ❖ Check that you still have a use for it
 - If you don't, get rid of it, for money, if possible
- ❖ Check its condition – that it is safe and suitable
 - If it isn't, get it fixed or replaced

Such a register will satisfy the basic requirement, but you can save yourselves a lot of additional work at the year end if you supplement or supplant this paper record with an electronic record in the form of a worksheet in your accounts workbook in Excel, [figure 14](#). Not only can you record in a straight-forward table details of each item, what it cost you and when you bought it, you can set up the formulae using Excel's built-in functions to calculate the depreciation charge each year, and the net book value of each item, and also when you disposed of it, and what you got for it (or it cost you) when you did. Depreciation, which is discussed in detail in the chapter covering balance sheets, is the way in which the cost of capital items are spread over their useful lives.

4.7. Fund or Project Accounting

In principle, charities, and indeed any organisation receiving funds to which conditions are attached, need to keep a separate set of accounts for each fund received, including separate bank accounts and so on and so forth. In practice, some relaxation of these strict requirements is permitted, to the extent that charities can consolidate the accounts of each fund under class headings, the three classes being Restricted Funds, Unrestricted Funds and Endowment Funds, and there is no requirement to keep separate bank accounts. These classes are defined and explained elsewhere in this publication. So the minimum requirement for any charity is that its book-keeping and accounting systems must be capable of recording receipts and payments at the level of these three funds. In practice, the providers of restricted funds, such as local authorities making grants, will require you, as a condition of grant, to be able to demonstrate to their satisfaction that the funds they provided were properly spent only on those items agreed in the application for the grant.

In practice, therefore, we are nearly back where we started, needing to be able either to keep separate accounts for each project, but not separate bank accounts, or alternatively to extract the relevant information from the main accounts. The disadvantage of the former approach is that it implies an extra analysis book, with entries for each project duplicating those in the main analysis book, hardly single entry! The advantage is that you can, in principle at least, see at a glance the state of financial play of a project. The advantage of the latter approach is that it implies being able to tag or mark each entry in your main analysis books in such a way that the entries relating to a singled project can be easily extracted, thus avoiding the need to duplicate entries. The disadvantage is that, until all the relevant information is extracted you cannot see “at a glance” the state of play of a project’s finances. Use of the Excel spread-sheet program lends itself to either approach, but the one favoured here is the latter. That is, the tagging of each entry with a project identifier, though if you have only occasional or limited need for projects accounts, for example, if you just get the odd restricted grant to buy equipment, you may find it easier just to keep a separate project account.

This requires you to prepare a list of identifiers, short alpha-numeric sequences, one for each project, and to have an additional column in your analysis worksheets, into which you insert the relevant project identifier for each entry. At any time, you can copy the worksheet and order it using the built-in database functions to group all the items with the same project identifier together, when they can be summed and the current financial state of play of the project assessed.

Whether you can get away with a single set of accounts, albeit with the ability to extract project data, together with a single set of filed supporting paperwork will depend to some extent on what your funders require. If they need you to justify your project accounts by submitting receipts, you will clearly have either to file your paperwork by project, or file your paperwork centrally but have copies in a project file. Ideally, you should keep the originals of the supporting paperwork in your files, submitting copies to your funders, if this is what they want. However, as a result of fraud and other abuses, funders may well insist on the original documents. If they do, you must take copies, and be prepared to explain to your independent examiner why you can’t produce the originals.

If you find that most of your income and expenditure falls under one project or another you may find that it is best to bow to the inevitable, and treat all your income and expenditure as project-related. In this situation, you keep a separate account (as an Excel worksheet or sheets) for each project, and sum these individual project worksheets to give the overall picture. You may have difficulty in visualising your core or back office work as a project, but what is a project is largely a matter of semantics, so you can call whatever you want a project, within reason.

What you tag with your project identifier or put into your project worksheet depends on what you put into your project budget and agreed with your funder. If a funder or project is picking up the bill for a complete item of equipment or an entire salary, then things are straight-forward, and there will be a one-to-one relationship between each entry in your books and the supporting paperwork. However, for shared costs and indirect

expenditure, the process will be more complicated. For example, we may have direct project staff, all of whose time is chargeable to the project, and other staff who work only part-time on the project. They will need to keep time-sheets, and you will have to allocate a proportion of the costs of employing staff – monthly net wages and payments to the inland revenue of income tax and national insurance – to the project, in the ratio of project hours worked to overall hours worked, for each pay rate. In this case, in the selected method, we will have to split what would be just one entry in one row of our spreadsheet where we didn't need to bother about project accounts into however many rows we need so that it is one row, one entry, one project. with the supporting paper-work showing the workings. Where a cost borne by an organisation can be passed on to a project either directly, or in proportion to something measured, like hour worked, we call this process "allocation".

For those indirect costs, like heat and light, which we can't allocate, but of which the project needs to pay a share, we follow a similar process, with one row for each project sharing the expense, but with the project's share calculated using the same method as was used for the corresponding budget line item. We call this process "apportionment". For example, say you have decided to apportion 20% (1/5) of your heat and light costs to a project, because the project's worker takes up about 20% of the floor space in your office, when you pay an electricity bill you will annotate the bill, or attach paperwork, to show how and why the amount charged to the project was arrived at. What I'm writing about here is full cost recovery, and this is a topic discussed at length later in this publication.

Do not be tempted to put off tagging the project entries in your accounts spreadsheet, or writing up your project accounts, to the quarter end, or year end. Although it is possible to leave it till then, and even to produce only an end of quarter or year summary, and many organisations do just that, you are depriving yourselves of vital information you will need to manage the project. Managed projects don't always succeed, but projects that aren't managed seldom do.

Incidentally, if you are looking to computerise your accounts using commercial of-the-shelf software and you need now, or importantly, believe you may need in the foreseeable future to keep project accounts, make sure that any accounting software you are contemplating buying can provide project accounts.

Chapter 5

5. Cash and Petty Cash

One of the ways in which we make life difficult for ourselves is the way we use language, especially words like cash and money, whose meaning changes with context. Sometimes when we talk about cash we mean money and sometimes when we talk about money we mean cash. Commonly, we refer to the books of account as cash books, even though we record in them all forms of money, and they really ought to be called money books. Strictly, all cash is money, but all money isn't cash. Strictly, cash refers to notes and coins, whereas money encompasses cheques and other similar promissory notes and electronic funds transfers in addition to cash.

On the topic of cash, we need to distinguish between cash received and cash paid out. Cash received is money received in the form of coins and notes. Receiving cash from members, users of the group's services, and members of the public is something that community groups do often. Unfortunately, proper procedures are either not in place or not followed, and confusion can reign. Some groups will just put incoming cash in a tin, and later will pay it out to a volunteer to cover their travel expenses, with no record kept of either the cash coming in or being paid out. Before anyone knows what has happened the money has gone, without trace.

The golden rules are:-

- ❖ Always pay cash straight into the bank, and record it in the same way as for cheques, so that it appears both in your Analysis Book and on your bank statement
- ❖ Never, ever, make payments directly from cash received. Ideally, no cash payments should ever be made other than through Petty Cash

The basic guidelines for dealing with cash received are as follows:-

- ❖ Ensure that the cash that you have received is counted, and that both the giver and the receiver agree on the sum that is changing hands
- ❖ Make sure that both the giver and receiver are sure what the money is being received for - is it fees, membership subscriptions, a deposit or a donation?
- ❖ Always give a written receipt - from a numbered duplicate receipt book - immediately. The receipt should state:-
 1. The date
 2. The name of the person who has given the cash
 3. What the money was for
 4. How much money was received
 5. The signature of the person who received the cash
- ❖ The money should be paid into the group's bank account as soon as possible. The paying-in slip should have a description of what the money is for. If your group follows this procedure, it will have no problems responding to questions at a later date about whether such and such money was received and what it was for
- ❖ Don't be tempted to put money received in your Petty Cash box and then make payments from it. How will you distinguish between money received and money drawn from the bank for your Petty Cash float?

5.1. Petty Cash

"Petty cash" is the name given to systems and procedures for making small payments in cash. Common payments made out of petty cash are:-

- ❖ Reimbursement of small purchases made by members of the organisation on its behalf
- ❖ Payment of the out-of-pocket expenses of volunteers, committee members and staff
- ❖ Payment for small purchases, such as stamps, stationery, low value office supplies, tea, coffee and milk. These last are often made using a cash advance from the petty cash system.

The Petty Cash Book is where these payments are recorded.

In keeping with the aim of putting as many transactions through the bank as possible,

- ❖ You should only ever make small payments in cash,
- ❖ Cash payments should in total be only a small percentage of your total expenditure.

Remember, you should never put cash receipts into petty cash, however small, but pay them straight into the bank. Even if the bank account is used for all large transactions and petty cash only for some small transactions, managing the petty cash is still important, not least because there is more scope for muddle and dishonesty with cash. It is, therefore, essential to develop a secure and workable petty cash system.

In setting up and running your petty cash system,

- ❖ Be clear about who has the responsibility for running petty cash. One person alone should be in charge. This way mistakes will be limited, responsibilities will be clear, and any mistakes or problems can be rectified by that person, i.e., if money is short the responsibility lands with one person, rather than five people bickering over who is at fault. It is better to have more than one petty cash account, with a single person in charge of each, and each responsible for different activities, than to have more than one person in charge of a single petty cash account
- ❖ Have published rules covering what can be paid through petty cash, and what cannot. With a little effort and forethought, it is no more difficult for a small organisation to cut its cash payments to the bare minimum than for a large organisation. For example,
 - Where people have bank or building society accounts, always reimburse them by cheque, except for trivial amounts (less than £1)
 - where people don't have a bank account, reimburse them with a cheque made out to cash, except where there are no local facilities for cashing the cheque

5.1.1. Imprest system

The right way to manage petty cash is to use the imprest system. Here is a ten step guide to running an imprest system:-

1. Your management committee decide on the amount of the petty cash float. This may be any amount from £10 to £200, depending on the size of the organisation and its cash payments turnover. In principle, it should be the amount your organisation expects to pay out in petty cash in a week or month, depending on how long you expect the float to last. You then withdraw this amount, the imprest, for example, £100, from the bank by cashing a cheque, entering the amount in your Analysis Book in a column called "Petty Cash"
2. Put the £100 in cash in your Petty Cash box (a lockable metal cash box) and enter it in your Petty Cash Book on the receipts side. Only one person, the petty cashier, should operate the Petty Cash system at any one time, and they are the only person who should have access to the box, which should be kept locked when not actually in use. Have a sensible place to keep it; somewhere secure, like a locked filing cabinet or cupboard. When the Petty Cash box is handed over from one person to another, say because the original person is going on holiday or leaving, it should be done in front of a witness and the amount of cash and the amounts for vouchers should be written up in the Petty Cash Book
3. Any money paid out should be replaced with a Petty Cash voucher (pads of Petty Cash vouchers are available from stationers) made out to that amount and placed in the box. That way, there should then always be £100 (or whatever the amount of your imprest is) worth of cash and Petty Cash vouchers in the box – [figure 15](#) emphasises this point. Receipts should always be obtained for Petty Cash claims, and the receipts should be stapled to the Petty Cash vouchers. Occasionally, receipts will not be available. and in such circumstances, an explanation as to why a receipt isn't available should be written on or attached to the Petty Cash voucher. If they are not already numbered, number each voucher as it is used, ensuring that whatever numbering system is used,

each number is used only once. (If vouchers are pre-numbered, and you use more than one pad of vouchers per year, you will have to have some means of distinguishing between vouchers from different pads)

4. All Petty Cash vouchers should be signed by the claimant and then authorised by the petty cashier. If they are the person being reimbursed, they should get the petty cash voucher authorised by somebody else. The person making the claim should never be the person that authorises it!
5. If the petty cashier takes money out of petty cash to make a local purchase, or advances money to somebody else to do the same, they should ensure that a petty cash voucher and an I.O.U. are put into the cash box. When the purchase is made, a petty cash voucher, supported by a receipt, should be completed in the usual way, and any surplus cash returned to the petty cash box. At the same time, the advance voucher and I.O.U. should be removed from the box, and can be destroyed, unless there is a discrepancy (the amount of the purchase plus the cash returned being different to the amount of the advance), whereupon it should be kept until the discrepancy is resolved
6. The petty cashier should record the payments made in the payments side of the petty cash book as soon as possible, ideally daily, but never less than weekly. Unless you have a low value imprest, and replenish it weekly, do not leave it until the next time you draw more money from the bank for your Petty Cash fund. The larger the imprest, and the greater the number of and value of the transactions, the more frequently should the petty cash book be written up, and you should question whether you should be holding and paying out such large sums as Petty Cash
7. Top-up the float when you are near the point of exhausting your imprest. Since you should be recording details of all payments in the petty cash book, and keeping a running total, you will know when that is imminent. The total of these payments is the amount that you withdraw from the bank to restore your float to £100. If, for example, your payments come to £76.91, there should be £23.09 in your Petty Cash box. All you have to do is withdraw £76.91 to restore your float to £100
8. Petty Cash vouchers, with receipts, should be filed in date order. It helps to number the vouchers and put a corresponding number against that item of expenditure in the Petty Cash Book. It is important that vouchers are kept as they will be needed when you prepare your accounts
9. On a regular basis, ideally once a month, the petty cashier should
 - Check that all cash transactions have been recorded in the petty cash book
 - Reconciles the amount left in the petty cash box with the petty cash vouchers and the petty cash book
 - Present the Treasurer or bookkeeper with the petty cash book
 - For inspection
 - To enable the week's or month's petty cash expenses to be transferred to the expenditure analysis book
 - Hands over the petty cash vouchers and receipts for all the money paid out of petty cash, for filing
10. To provide the correct figure for the end of year accounts, on the last day of the financial year the Petty Cash should be counted in front of a witness and a signed certificate for that amount should be made out, or the Petty Cash Book should be signed

The only disadvantage to this system is that it needs the responsible person to be reasonably available and accessible, not always easy for very small groups without a fixed base or paid staff. However, these are just the sort of groups who least need a petty cash system.

5.1.2. Petty Cash is not compulsory

Don't run a Petty Cash system for its own sake. If you can make all your payments by cheque, do so. Many community organisations are accustomed to staff and volunteers saving up their claims for reimbursement, submitting them on an expenses claim form, an example of which is shown in figure 16 to which all the receipts justifying the claim are attached, once a month, with the reimbursement made by cheque. Some will, following

common practice in the private sector, make expenses payments and reimbursements to staff through payroll. In fact, the only reason many community organisations need to have a petty cash system at all is to avoid disadvantaging volunteers such as refugees and asylum seekers, as is discussed elsewhere.

5.2. Petty Cash Analysis Book

I am assuming that you will keep your Petty Cash Book as a worksheet or worksheets in an Excel (or similar spreadsheet program) workbook. However, the principles apply equally if you decide to stick with a manual book. An example of a petty cash analysis book set up in Excel is shown in [figure 17](#).

The payments side of the petty cash analysis book will in principle be identical to the payments side of the main analysis book, with the same number of columns and the same column headings. Although many of the columns won't be used to analyse out petty cash payments, it makes it much easier to prepare monthly, quarterly and annual accounts if unused columns are left in, rather than omitted, as is customary with manual books. Unused columns can be hidden when not required, and only unhidden when needed for "cutting and pasting", be that manual or automated. As far as the reference is concerned, there is no argument, since this should be the number on the petty cash voucher, and the date, the payee's name and the details are also taken from the vouchers. Remember, there may be more than one column entry per row, especially if volunteer's expenses are paid out of petty cash, with one payment covering say both travel (an entry in one column) and refreshments (or subsistence, or whatever you call it) (an entry in another column).

The receipts side is much simpler, since the only receipts will be transfers from the community organisation's bank account, so there is no need for any analysis columns, and the reference number should be the reference number of the cheque used to withdraw each imprest top-up from the bank, with date as on the cheque and payer shown as "Cash from Bank". You should have a running total column, so that you have due warning of your cash in hand running low (though it makes life easier to top up the imprest at the end of each month, even if it isn't actually fully depleted.)

5.3. Large Cash Payments

Occasionally you may have dealings with someone who insists on being paid in cash rather than by cheque. There is no need to put these payments through Petty Cash. It is simpler to cash a cheque at the bank and enter the payment in the main Cash Book in the normal way.

For example, a local builder carries out some repairs for you and wants to be paid in cash. You should make out a cheque for cash, withdraw the money from the bank and enter the details in the main Cash Book. Instead of entering the amount in the Petty Cash column put it under Repairs (or whatever) and file the builder's invoice with the vouchers for cheque payments. (The rights and wrongs of paying trades-people in cash are debated elsewhere in this publication.)

5.4. One off events

For one-off events, such as your annual fun day or fete, your Christmas party or your annual outing to the seaside, it is better to establish a special float and keep cash expenditure on the day completely separate from your regular Petty Cash system. Withdraw the special float money from the bank, recording the details in the Miscellaneous Expenses column of your Bank Analysis Book. During the day, you should make a note of all cash expenditure on Petty Cash vouchers, attaching receipts wherever possible, though it may in practice prove impossible to get receipts for all small items of expenditure. Don't put this off – the longer you leave it, the more difficult it becomes! Draw up an account for the day, putting the vouchers into a file and keeping them for your accounts. Unspent money should be paid back into the bank - not put into the Petty Cash box!

Some common examples of both one-off and regular events involving cash income or cash expenditure, or both, are discussed below.

5.5. Cash income and bingo

Bingo sessions are a common-place in community buildings, both as a source of income and as a social activity, especially for the elderly. Bingo in community buildings should normally be played under the rules and regulations set out in Section 41 of the Gaming Act, the most relevant points being:-

i) persons attending the entertainment must make only one payment in respect of bingo and that payment must not exceed £4.00. This single payment would include entrance or participation fee including whatever money is paid for the purchase of bingo tickets;

ii) the total value of prizes paid out must not exceed £400;

iii) it is not necessary to return all stake money taken from the purchase of bingo tickets to the players as prizes. The only stipulation is that all the proceeds from the bingo, after the deduction of reasonable expenses and the allocation of prizes, are applied to purposes other than private gain;

iv) bingo played under Section 41 may be advertised to members of the public (eg in a parish magazine or news sheet);

v) children and members of the public can take part in Section 41 bingo but would of course be precluded in cases where the provisions of the Liquor Licensing Act were appropriate.

The Act is policed by the gaming board of Great Britain, see Community Matters Information Sheet no. 26, Bingo, for further details. As a result, the games are small-scale, with all receipts taken in cash. In addition, refreshments are usually available, at modest prices, for cash purchases, and the cash prizes are taken from the receipts.

Any event where only the net proceeds are paid over to the community organisation has the potential for skimming. That is, for diversion of funds from the event into the pockets of those handling the cash. In addition, for community organisations which are charities, recording only the net takings of events in the accounts is not permitted, the requirement being to show both gross takings and expenses, so both for accounting reasons and to prevent fraud and theft, accurate records need to be kept of all monies received, whether for the combined entrance fee and bingo book charge or sale of refreshments.

The proceeds, gross and net, should also be checked against the number of people attending the session and the number of bingo books distributed, and any significant discrepancies investigated. The net takings, together with the accounts for the session, should be handed over to a responsible officer or employee of the community organisation, against signature, to be checked and then either banked, or if this is impracticable at the time, put in the safe to be banked later. Where the net proceeds can't be handed over after the session, the bingo organiser should be able to gain access to a safe in which to deposit the money, in front of a witness.

Only in exceptional circumstances should cash be removed from community premises, except in transit to be banked. Where security considerations dictate that money, such as the receipts from an evening bingo session, be taken home by an organiser for safe-keeping, this should be authorised in advance by the management committee, and a check made that the custodian is adequately covered by his or her household insurance policy for keeping cash at home.

5.6. Cash income and bars

This isn't the time or place to go into the ins and outs of bars in community buildings, but they can be both a useful source of unrestricted income and a serious head-ache for the management committee. I know of what I speak – I am one of the licensees of the bar in a community building which has a premises licence (and I have a personal licence). In the context of cash handling and accounting, bars present a serious opportunity for fraud and theft, and a serious cash management challenge.

Bars should never extend credit, so all their takings will be in cash. Depending on the day of the week and the time of the day, the amounts could run from £100s per day to £1,000s. All this cash should be put through a cash register, or registers, so the first safeguard is to check the amount in the cash register at the end of a session with the cash register record. At the start of the session, a cash float should be taken from a safe and

placed in the cash register (to provide change), and the physical count at the end of the session must take into account the amount of the float. In principle, the float should be counted into the till by 2 people and signed for, and the takings also counted by 2 people and signed for.

In principle, the amount in the till, less the float, should match exactly the amount shown on the till record. In practice, there will be discrepancies, and these need to be monitored and investigated, especially if significant. There should also be a correlation made between the till records and the stock sold. Many bars will have electronic tills which will record not only the amounts entered but also the actual drinks sold, and who made the sale. However, such tills are expensive, and significantly slow service, and many smaller and busier bars avoid them, trading off a reduced need for staff against reduced accuracy of till records, and an increased need for physical stock-taking. Even where all-singing and all-dancing tills are used, all stock should be physically checked either at the end of the session, or before the beginning of the next session and not just the ready-use store, again by 2 people. This will involve not just counting full bottles, but for example weighing part-used beer barrels and gauging part used spirit bottles. Since the relationship between the wholesale and retail price of the drinks is known (it should be determined by whoever is responsible for managing the bar, and reviewed regularly), what the stock physically sold should have fetched can be calculated and compared with the actual takings. Any discrepancies need to be monitored, and if significant, investigated. Bars are notorious for scams and fiddles, and strict comparison of actual takings with expected takings, based on movement of stock, is the first line of defence against them.

It is now the early hours of Sunday morning, and we have several £1,000s in assorted notes and change on our hands. What do we do now? Unfortunately, we can't put it into the night safe of our local bank, since it is now a Wetherspoon's pub, so we lock it, in front of a witness into a safe or safes, to be dealt with on Monday morning, when it will be drawn from the safe, recounted and banked intact. You need to control access to the safe keys, and the safe, and make sure that the safe and your insurance cover are adequate for the sums of money you are going to have in the safe. In addition, you need to think through who and how is to take the money to the bank, minimising the risk to whoever does it of being robbed on the way, and taking into account the fact that several £1000 in cash weighs many kilos!

5.7. Cash Income and Room/Hall Hire

A major source of income for community groups running community building is letting out rooms for meetings and halls for recreational and social activities. Dealing with halls first, it is good practice to require bookings in advance, secured by a refundable deposit, which is forfeit if the hirer cancels at short notice. The deposit is also usually forfeit if there is breakage or damage by the hirer, or if they don't clear up and leave the premises by an agreed time. The conditions of forfeit need to be written into the terms and conditions for hall hire. The amount of the deposit needs to strike a balance between covering your expenses if there is late cancellation, default or damage, and deterring hirers. You may have a scale of deposits, depending on your view of the risks involved, with your OAP bingo club at one end of the scale and 18th./21st. birthday parties at the other. If the bookings are taken sufficiently far forward, it doesn't matter whether the deposit is paid by cheque or cash. If a cheque bounces, the booking is void. However, with the hire fee itself, things can be more problematic, if you accept a cheque at the last minute and it bounces, the deposit may not be enough to cover your expenses. It is therefore reasonable to have one time limit for cheques, say 2 to 4 weeks in advance of the hire date, and another for cash, say 1 to 2 weeks before the hire date.

The foregoing primarily relates to the hire of halls on an occasional basis by members of the public for functions, such as family parties, wedding receptions and dances. You may also hire your community hall out on a regular basis to groups and your sections, for anything from badminton and carpet bowls through golden age club bingo sessions, scout/guide and religious groups, to children's dance, line dancing, aerobics and weight-watchers. Here, whether you should require a deposit and/or payment in advance depends on your relationship with the group, and your evaluation of the risk of them defaulting. Initially, where a group is new to you, you may require an initial deposit and payment in advance, but as time progresses you may roll the deposit over from one

booking to the next, and allow the group to pay against invoice. Indeed, established groups should be encouraged to pay the hire fees against invoice by cheque, either monthly or quarterly in advance.

With room hire, the amounts are much smaller, the consequences of default or cancellation less severe, and a deposit is not usually sought. How hire should be treated depends on whether the hire is a one-off, or a regular booking. For one-off, or occasional hire, whether you require payment in advance or on the day is a matter of your evaluation of the risks involved – payments in advance can usually be accepted by cheque, since if the cheque bounces, you have time to do something about it. Payments on the day should generally be in cash, unless the group are well known to you and you judge them to be credit-worthy. Regular hirers of rooms should be treated in the same way as regular hirers of your hall, paying by cheque against invoice.

Payments for hall and room hire, whether by cheque or cash, during your office hours shouldn't present a problem, even during holidays, being handled like any other transaction. Be sure always

- ❖ To provide a receipt, from a duplicate book, when accepting cash
- ❖ To relate the sum received to who paid it (which group it is on behalf of, that is – the receipt should tell you who) and what it was for (in this instance, hall or room hire), especially if there is no invoice or note of explanation proffered.

Where problems arise is when payments are tendered out of office hours, such as payments for room hire handed over on the night to a hall sitter or committee member in cash. You should have available

- ❖ A duplicate receipt book, from which to give a receipt in exchange for the money
- ❖ A note pad, or pro-forma on which who paid the money on behalf of what group and what it was for can be recorded
- ❖ An envelope into which the money, the note and any supporting paperwork can be placed
- ❖ A safe place where the envelope containing the money can be lodged

You could insist that all payments had to be made during office hours, but unless these hours are generous, this will be seen as unreasonable and a disincentive.

If you do allow hirers to pay after the event (effectively, allowing credit) you must keep tight control of arrears. It is in nobody's interest to allow a group to run up a large debt for room or hall hire - I came across a case not so long ago in which a group had been "allowed" to run up a debt amounting to 5 years rent! The group hadn't a cat in hell's chance of paying off the debt and the community association concerned couldn't really afford to write it off. No matter how worthy the group's cause and how disadvantaged, you must harden your hearts and bar the group from using hall or rooms until they pay up, insisting in the future on payment in cash in advance.

5.8. Cash Income and One-off Events

Community organisations often aim to hold both an annual community day and a bazaar, the former in the summer ideally out-of-doors and the latter as an adjunct to a religious/community festival indoors during the winter months, both as a means of raising funds and their profile. Summer fetes are typical and traditional (though you may call them something else, like "fun day"). Such events are characterised by many stalls and side-shows selling things, offering amusements and games of chance and/or skill for modest prizes. All transactions on the day will be in cash. Sometimes the items for sale and the prizes will be donated, and sometimes purchased.

If items are to be purchased, including refreshments, they should all be purchased, whenever possible, through the group's normal procedures, with payment made by cheque against invoices. Where cash purchases can't be avoided, the number of these needs to be minimised. Money should be drawn from the bank specifically for the purchases, with those charged with buying signing for the cash. All items purchased should be receipted, and all change should be accounted for, with this being paid back into the bank account. On the day, each stall or side-show will require a cash float, from which to provide change, and there should be a supplementary central float, in case large notes have to be changed early on, the total of all these floats being drawn from the bank as near

to the event as possible. The floats should be issued to each stall/sideshow holder against signature by the cashier for the day, who should be a responsible member of staff or committee member comfortable with handling cash.

During the event, the cashier together with an assistant (for safety/security reasons) should tour the stalls and side-shows, siphoning off notes and excess change, and providing small change, as appropriate, recording each transaction, against signature. At the end of the event, each stall/sideshow holder should count the money in their possession in conjunction with the cashier, the latter signing to signify receipt of the counted amounts. The total takings for each stall/sideshow should be calculated, after deduction of the floats, and the results published, ideally as soon after the event as possible. After checking, the total cash should be taken to the bank or placed in a safe, if outside banking hours.

Any stock left over should be counted, recorded and put into safe storage. Ideally, the actual takings from each stall and sideshow should be compared with the expected takings, based for example on the starting and finishing stock levels or the number of tombola tickets sold. In practice, this may not be possible, and due allowance must be made for errors by the stall-holders. Unfortunately, there are many and various ways and means of diverting goods and money at such events, and the general principle is for the organisers to be vigilant.

If netting off occurs, with stall-holders or side-show operators paying for expenses directly out of takings, typically because they supplied the goods for sale or as prizes out of their own pockets, to be clawed back from takings, you must insist that all stall/sideshow holders who do this must produce accounts showing

- ❖ What the takings were before deductions
- ❖ How much has been deducted and what for

and producing evidence, in the form of receipts, justifying the expenses.

Remember, charities have a legal obligation to account for all monies received, and paying in only a notional “profit” is the easiest way of hiding irregularities.

One or two words of advice:-

- ❖ Hundreds of pounds in coins weighs many kilos and takes up a lot of space. Your safe may not be big enough
- ❖ You need a secure space with a large stout table on which to count and bag up the money
- ❖ Many otherwise competent people panic when faced with a table full of coins
- ❖ A coin sorting frame, or ideally a machine, makes the job a lot easier
- ❖ Don't spend hours chasing the elusive 20p – it isn't worth it (it fell off the table and is under a filing cabinet – you'll find it next time you spring-clean or reorganise the office)
- ❖ Banks
 - Require coins bagged up with the types of coins and the amounts as specified on their plastic coin bags.
 - Often restrict when and how much you can pay in over the counter in coins

5.9. Cash income and Play groups/supplementary schools

Two of the drivers in determining how much effort you will need to put into your book-keeping are

- ❖ The number of transactions
- ❖ The number of headings in your analysis columns

Play-groups and supplementary schools, especially where

- ❖ There is a different mix of children at each session
- ❖ There are a lot of children enrolled
- ❖ Fees are levied per session
- ❖ Fees are paid in cash at each session

generate a lot of transactions, and if these are all recorded in the main books, they rapidly swamp all other transactions.

In such circumstances, good practice is to record details of individual fees collected in a supplementary book, putting only the total through the main books. The book can be a physical book, or an electronic book, in the form of a spreadsheet. Unless the entries into the computer can be made at the time, it will be necessary to have a paper record, say by printing out a blank copy of the spread-sheet template, see [figure 18](#).

If you set up the spreadsheet properly, and you put a 1 in any cell to indicate that a child has attended a session, and fill in the amount actually paid in the next cell, then the total attendance per session and the total fees collected will be given automatically. It is best to collect the fees in cash or by cheque before each session, giving each person who pays a receipt from a duplicate book, as evidence of payment.

At the end of each day, the amount collected in fees should be checked against the attendance/fees sheet, and the money should then be handed over to a responsible officer or employee of the community organisation, against signature, to be checked and then either banked, or if this is impracticable at the time, put in the safe to be banked later. Where the fees can't be handed over after the sessions, the play-group/after-school club organiser should be able to gain access to a safe in which to deposit the money, in front of a witness. The daily fees collected can then be entered into the Books of Account, as a single entry, leaving the detail in the attendance/fees book. At a pinch, it would be possible to collect all the fees for a week together, and treat this as one block entry, but a single entry might then cover up to 240 individual transactions (at 2 sessions per day, 25 children per session) and potentially £1,200 in fees (at £5 per head per session).

Where fees are levied per session, and paid per session, it is inevitable that some parents will not have the money on them, and thus there will be money owed. It is essential that any arrears of fees are picked up early, and dealt with as soon as possible, to avoid the arrears getting out of hand, both from your point of view, and from the defaulting parents' point of view. In the final analysis, and sooner rather than later, before the amount starts to mount up, you will have to exclude the child in question until the arrears are settled. This is difficult – you feel that you are visiting the sins of the parents onto the child – but not to take action is to penalise those who have had to struggle to pay, and arrears getting out of control is a major source of financial difficulties for playgroups and supplementary schools.

The administrative burden can be reduced by getting parents to pay per term, half term or calendar month in advance, against invoices, but if substantial sums are then settled by cheque, you need to allow time both for the cheques to clear and to deal with any that “bounce” (that is, a returned unpaid by the bank, because the parent has insufficient funds in their account.)

On no occasion should cash collected to pay fees ever be used to pay expenses. All fees should be paid into the association's bank account untouched. If there is a need for petty cash expenditure by the playgroup/supplementary school, they should have their own petty cash account, with an agreed imprest, and run under the same rules as the association's main petty cash account.

5.10. Theft, and informal borrowing leading to theft.

One of the most serious problems when dealing with cash is theft, and any system you put in place to handle cash must minimise both the opportunities for theft and the amounts that can be stolen. Leaving cash, either as cash received or the petty cash float, lying about unattended, say in a drawer of the reception desk, is just asking for it to be stolen. Losses of cash, even where amounts are small, whether as a result of stupidity, carelessness or dishonesty, can be a serious disrupting factor in a community organisation, sowing seeds of mistrust, suspicion and recrimination out of all proportion to the actual loss. Since the prevention of theft of charity assets is a primary responsibility of the trustees, any theft of cash, however small, must be taken seriously, and for all but the most trivial amounts, should, indeed, according to the Charity Commissioners

recommendations, must, be reported to the police. At the very least, the circumstances must be investigated and procedures tightened to prevent repetition.

Informal borrowing, in the form of advances from petty cash or cash advances to cover anticipated expenses, should not become an issue, provided you follow the principles set out in this publication and always ensure that, for an advance from petty cash

- I. The amount borrowed is always covered by an IOU
 - II. IOUs are not allowed to remain unredeemed for more than 24 hours, ideally less.
- and, for an advance against expenses,

- I. This has been properly authorised
- II. The expense claim to offset the advance is submitted within a week of the advance being given.

However, informal borrowings which can easily get out of hand, and ultimately drift into theft, arise where money is taken either from cash received or from petty cash without permission and either without IOUs or where little effort is made to oblige the informal borrower to redeem the IOU. Permission for such advances, without the justification of an imminent petty cash purchase or expenses to be incurred, should never be given. Indeed, for the trustees to authorise a loan to one of their number, or a member of staff or volunteer could lay them open to a charge of acting “ultra vires” (that is, outside the powers granted to them by their constitution.) Accordingly, any instances of informal borrowing must be nipped in the bud, with any repetition being treated as a breach of discipline.

On the face of it, the “borrowing” of the odd tenner, provided it is repaid promptly within a day or two isn’t a serious matter, but the odd tenner can easily become the odd hundred, and once the time taken to repay stretches into weeks the rot has already set in. Informal borrowing is especially worrying where it is done by the senior paid worker, because other more junior staff and volunteers may be reluctant to “whistle-blow” to members of the management committee, who, unless they have put in place appropriate procedures and processes, may be kept in ignorance until it is too late.

It is permissible to allow members of staff and volunteers to cash cheques from cash income, provided all such transactions are properly recorded, and the cheques clear without problems. It should be made clear that this is a privilege and not a right which will be withdrawn if a cheque bounces.

Chapter 6

6. Bank Reconciliation

Bank reconciliation is the name given to the process of comparing your accounts book entries, be they Excel workbooks, or manual books, with the entries on your bank statements and explaining any differences. It is a check of the accuracy of your records against those of an outside body (i.e. your bank's). Unfortunately, although a fundamental financial control, bank reconciliations are often not done at all by community organisations, or if they are done, are not carried through to conclusion, because the organisation doesn't know what to do if the reconciliation doesn't come out right.

Throughout this publication, it is recommended that you arrange to receive a bank statement from your bank every month, and you should aim to do a bank reconciliation every time you receive a bank statement. In practice, organisations making many transactions in a month may receive several statements each month, either all in a batch once a month, or at weekly or monthly intervals throughout the month. Organisations which make few transactions each month may find that, unless they insist on monthly statements, they will get them only when a statement sheet is full, which may take several months.

You should not expect your bank statements to be a mirror image of your accounts books. For a start, your accounts "book" is prepared from your point of view, whereas the bank statement is prepared from the bank's point of view. To the bank, unless you are overdrawn, you are a creditor. You have, in effect, lent the bank your money. Also, the bank statement date may not be the end of the month date, and even if it is, by the time you receive it, will be a few days out of date.

In addition, bank transactions aren't instantaneous. For example, when you pay a bill by cheque, you record this in your books as soon as you have written the cheque. You then put the cheque in the post. It will take a day or two to reach your supplier, who may take days or weeks to pay the cheque into their bank, and there will be a further delay before your bank debits your account. Similarly, you record an incoming cheque as soon as you receive it, but may delay paying it in to the bank for several days, where there will be a further delay before your account is credited. Remember, banks generally record withdrawals before deposits, and take longer to credit deposits than they do to debit withdrawals.

Further, and this is increasingly likely, there may be transactions in your bank statement which aren't in your accounts book. This covers such items as

- ❖ Bank charges
- ❖ Bank interest, both suffered and gained
- ❖ Deposits and withdrawals by electronic funds transfers – BACS, Direct Debits, Standing Orders and such like. Grants are increasingly paid this way, often without advance notice of the precise details

Carrying out a bank reconciliation is reasonably straightforward, if you follow this step-by-step guide:

1. Look at the bank statement and compare the items paid out with the entries in the payments side, section or sheet of your Analysis Book(s). Place a small tick in the book against each cheque payment that appears on the statement (if you are using a manual book, or a print-out of your spread-sheet. When using a spread-sheet, I put an r in a spare column I insert into the spreadsheet especially for that purpose.) Tick the bank statement entry too. Similarly, place a tick against each deposit in the "banked" column of your analysis book, which also appears on the bank statement. Tick the bank statement entry too. Remember to check and tick-off any items outstanding from the previous reconciliation which have now cleared the bank. I usually start by checking for these first.

2. Examine the bank statement for any entries without a tick. If you find any, enter them into the corresponding analysis book. For example, bank charges need to be entered in the payments side, but bank interest received

would be entered in the receipts side. Items such as Direct Debits and Standing Orders should be dealt with in the same way. Don't get hung upon dates being out of sequence, just add them to the bottom of the appropriate month's transactions. Once you have made these entries, tick them off in both the book and on the statement. When you have completed these two stages, you know that every item on the bank statement is also in your accounts book

3. Underline the end of month row in your spreadsheet, (or rule off your manual books) and sum all the columns (in your manual books, add up all the columns) and "cross-cast" to check that the adding-up is correct.

4. Complete the "Analysis Book Summary" section on the Bank Reconciliation Form, figure 19, and calculate the "Analysis Book Closing Balance" for the month:-

Balance brought forward (b/f)

+

Receipts for the month

-

Payments for the month

=

Balance carried forward (c/f)

The Analysis Book is now completed and balanced. The next stage is to deal with anything that is in the Analysis Book but not on the bank statement.

5. Look at the Bank Statement, find the balance at the end of the month and enter the figure, where indicated, on the Bank Reconciliation form.

6. Examine the Receipts side (or section or sheet) of your Analysis Book to see if there are any entries without a tick. Entries without a tick are called outstanding receipts — they have been banked, but have not yet cleared. List them in the outstanding receipts section on the Bank Reconciliation form.

7. Examine the Payments side (or section or sheet) of your Analysis Book for any entries without a tick. These are called outstanding cheques — you have issued the cheques, but they have not been cashed yet. List them in the outstanding cheques section on the Bank Reconciliation form.

Note that, in steps 6 and 7, it doesn't matter in either case if the cheques are still in your possession. If they are in your Analysis Book, they are included, even if you haven't

- ❖ Paid them into the bank (if receipts)
- ❖ Put them in the post (if payments)

8. Last of all, add the outstanding receipts to the bank statement balance and subtract the outstanding cheques to arrive at the Adjusted Bank Statement Balance. The Closing Analysis Book Balance and the Adjusted Bank Statement Balance should now agree. You will have confirmed that there are no discrepancies between the books and the bank statement, and proved the accuracy of your bookkeeping.

Here are some additional hints and tips which should help you either to avoid problems, or to deal with them as they arise, when dealing with the bank statements:-

- ❖ Check carefully the monetary value of each entry on your bank statement with the corresponding entry in your Analysis Book, noting any amounts that differ. These will need to be investigated. Is it your mistake, or the bank's? If the former, you should correct the entry in your Analysis Book. If the latter (not as uncommon as you might expect), you should approach your bank, even if the error is in your favour, to resolve the discrepancy. If the errors are small, and in your favour, the bank may decide to let the matter rest, since the cost to them of correcting the mistake will be much greater than the cost of the mistake itself. However, you should not assume this until you have spoken to the bank.

- ❖ Do not expect the cheque numbers shown in sequence in your Analysis Book to be replicated in the same order on the bank statement.
- ❖ Check particularly for any gaps in the sequence of cheque numbers. Cheques are valid for 6 months, and some organisations, particularly voluntary organisations, are notoriously tardy at paying cheques in. A large cheque written months before and suddenly presented can play havoc with your cash flow. Also, until the cheque has cleared your account, you haven't actually paid the bill, even if the delay isn't your fault. In addition, check that any gaps aren't a result of your having not issued the cheque (usually because a mistake was made when the cheque was being prepared, and it has been "destroyed".)
- ❖ Always check your arithmetic. If adding up using a calculator, don't assume the first number you get is the correct answer. It is only correct if you get the same answer the next time you do it. If you have set up a spread-sheet, check the formulae, especially if you have made changes, like adding or deleting a row, particularly at the bottom of a spreadsheet.
- ❖ If a discrepancy (difference) is exactly divisible by 9, you have probably transposed a figure e.g. £631 instead of £136 or £49.23 instead of £42.93.

6.1. What if the Bank Reconciliation Doesn't Agree?

If you find that your reconciliation does not work, there are a number of things to look for:-

- ❖ If the Closing Analysis Book Balance is more than Adjusted Bank Statement Balance
 - An item paid in to the bank account but not yet cleared has been omitted from the outstanding receipts list. (Ticked-off by mistake).
 - There is an item in the outstanding cheques list that has in fact been cashed. (Should have been ticked-off but was missed).
 - Something has been paid out by the Bank but has not been entered in the Cash Book. (e.g. Bank Charges not picked up from statement).
 - A receipt has been entered in the Analysis Book more than once, or its value has been overstated.
- ❖ If the Adjusted Bank Statement Balance is more than Closing Analysis Book Balance
 - An outstanding cheque has been omitted from the outstanding cheques list (Ticked-off by mistake).
 - There is an item in the outstanding receipts list that has in fact been cleared. (Should have been ticked-off but was missed).
 - Something has been credited by the Bank but has not been entered in the Analysis Book. (e.g. Interest received but not picked up from statement).
 - A payment has been entered in the Analysis Book more than once or its value has been overstated.

In either case, there will be an arithmetical error in your bank reconciliation, and you will have to repeat it, from scratch. If you try and cut corners, by assuming that some steps have been done correctly and don't need to be repeated, you'll end up going round in circles! The commonest mistakes are all around the outstanding cheques list, especially for those cheques which first made their appearance months ago.

For Further information, see Bank Reconciliation on CASH's website: www.cash-online.org.uk/cashfacts

Chapter 7

7. Management Accounting

In the introduction, two of the four main aspects of accounting are defined as:-

- Classifying and summarising the recorded data so that it can be understood by and made use of by the group
- Communicating to the group and other interested people and organisations what has been learned by classifying and summarising the data

We call this aspect of accounting management accounting, and for a community organisation managed by a voluntary management committee, the most important part of management accounting is reporting to the management committee.

7.1. How often should the Management Committee meet?

This is one of those “how long is a piece of string?” questions, to which there is no absolute answer. It depends on the nature of your organisation, the degree to which day-to-day running of the organisation has been delegated to others, and the general situation. Many authorities suggest that it is sufficient for the management committee to meet quarterly. However, except for very large organisations which are in fact managed by the paid staff, or very small organisations which do little or nothing from one year’s end to the next, this is, in my experience, not frequent enough, and accordingly, it is recommended that the management committee of a community organisation running a community building should meet monthly.

Remember, as charity trustees your management committee are collectively responsible for the day-to-day management of the charity, and it is difficult to see how they can take on this responsibility if they only meet quarterly. Where trustees meet quarterly, the reality is that they have abrogated their responsibility, and in practice you will find if you scratch hard enough that the community organisation is actually being managed either by a quartet comprising the chair, the secretary, the treasurer and the manager/warden (or whatever you call your senior paid worker) which is bad enough, or even worse by that unholy duo the chair and the senior paid worker.

Management responsibility is joint and several, that is, collective, not individual, with no one trustee, not even the chair, having more or less responsibility than any other. Responsibility cannot be delegated, in spite of what is commonly believed – it is authority which is delegated, not responsibility, so if you delegate the running of the community building to a sub-committee or paid manager, and things go wrong, it is still your fault. It is this principle which means that the captain of a naval vessel is court-martialled if the vessel runs aground, even if they were asleep in their cabin at the time. As a charity trustee, it is always your watch.

It follows that members of a management committee cannot discharge their responsibilities solely by attending management committee meetings. They need also to “walk the job”. If the job is running a community building, they can walk the job just by participating in the activities in and around the building, both as volunteer and as user.

7.2. Reporting to the Management Committee

Responsibility for the management of community organisations falls on their management committees – the managing trustees, if your organisations are charities. It is they collectively, not just the treasurer, who are responsible for managing your organisations’ money. In order to do this, they need to know where the organisation stands financially, to know this regularly, not only before each management committee meeting but in sufficient time to make decisions which can change outcomes. Accordingly, Management Committee members, especially if they are charity trustees, are failing in their duties of trust and care if they do not receive, consider and act on a report on the financial affairs of their community organisation at each and every meeting of the management committee.

In principle, the Books of Account could be made available to all Management Committee members in the days before meetings. Indeed, it is essential that the Books of Account are open at any time for inspection by the management committee. However, although this is a good way of keeping the books honest, this isn't a good way of keeping the management committee up to speed financially - they haven't the time, and may not have the expertise, to interpret the raw data.

Preparing, or at least ensuring that the report is prepared and reading it, is the responsibility of the treasurer. In fact, it is the most onerous of the treasurer's duties. The report should comprise

- ❖ A statement of financial affairs, in the form of a receipts and payment account,
- ❖ A statement showing how much was owed to and by the organisation and the amount of cash at the bank and in hand,
- ❖ A variance analysis, with actual receipts and payments compared to and contrasted with budgeted receipts and payments
- ❖ A projection of the state of the organisation's finances at the year end
- ❖ A written commentary on the financial statements, with particular emphasis on the variance analysis, drawing attention to any areas of concern and outlining courses of action, if action is required to get things back on track.

Although this sounds like a lot of work, it needn't be if you have followed the earlier recommendations in this publication, and have monthly budgets and keep monthly accounts, analysed under the budget headings.

7.3. Preparing the report

If you follow the recommendations in this publication, you will have

- ❖ an Excel workbook in which your monthly budget and cash-flow forecast are set out
- ❖ another Excel workbook forming your Receipts and Payments Analysis Account, which has within it a worksheet containing monthly summaries of the receipts and payments account.

In preparation for the report to your management committee, you need to create a third Excel workbook. On the first worksheet of this workbook, make a duplicate of your monthly budget and cash flow. If you select the whole worksheet before copying and pasting the data from your budget and cash-flow workbook and paste it into your new management reporting workbook, you will automatically set up links between the data in your budget and cash flow workbook. In principle, you do the same on the second worksheet in your new workbook, but using the actual receipts and payments on the summary worksheet of your receipts and payments analysis workbook. In practice, you are going to have to do some manipulation of this data, using the transpose function embedded in the "paste special" command within Excel, so that both the budget and actual data are in the same format. Your budget worksheet will have the budget headings in rows and the monthly budgets in columns, whereas your actuals summary worksheet will have the budget headings in columns and the monthly totals in rows. When you have finished, the format of the first two worksheets should be identical, with the first column being the budget headings and the next 12 columns being the months of the year, see [figures 20 and 21](#). I'm assuming that your financial year is April to March, so your columns will be headed April to March. You should also have a totals column.

You may have already gathered that you are going to be asked to set up a third work-sheet on which to work out the variances, which is a correct deduction. As you have the workbook set up now, the variances will compare budgets and actuals month by month. This is worth doing, but isn't the best way to look at variances, which are best looked at on a cumulative, that is year to date, basis. To do that, you need to set up on your budget and actuals worksheets en bloc below the monthly individual totals monthly cumulative totals (by adding the next monthly total to the previous cumulative total cell by cell). Having done this, you then on the third worksheet work out the cumulative variances, [figure 22](#).

Variance is the name that accountants give to the difference between a budgeted value and an actual value. You can calculate variance as either budget – actual, or actual – budget. We talk about variances being

favourable or unfavourable, rather than positive or negative, which gives a clue to which way round to calculating variance. For receipts, a favourable variance is when our actual receipts are greater than our budgeted receipts, so for receipts, you should calculate variance as actuals – budget. For payments, a favourable variance is when your actual payments are less than your budgeted payments, so for payments, you should calculate variance as budget – actuals.

So, you are now in a position to produce the receipts and payments account, by summarising the actuals spread-sheet, (either on the annual summary work-sheet, or an additional worksheet – another opportunity to use the copy special – transpose function) and to print out the variance report. The list of debtors and creditors need be no more than a summary of the data in the incoming invoices waiting payment and the outgoing invoices waiting remittance section of your filing system, though it is good practice to forewarn of any large bills looming in the offing, and of any outstanding remittances which might turn into a bad debt – that is, where the person or organisation can't (or won't) pay you.

Forecasting out-turn involves substituting actuals for the year to date into a spread-sheet containing the monthly budget, with adjustments to take account of early or late payments (to avoid either counting an item twice, or leaving it out). This is another straight-forward piece of applied spread-sheet logic, with manual adjustments, creating another new work-sheet in your reporting work-book. You can either do the substitution manually, using copy and paste between your actuals worksheet and a copy of your budget worksheet, or automate it using the "if" statement function. See [figure 23](#).

Now you have the set of tables, and need to produce a written commentary. Some words of warning before you begin.

It is all too easy when the treasurer, after hours, if not days, of work, puts on the table a print-out of a spread-sheet fitting at the edge of legibility on an A3 sheet, supported by a stack of intricate graphs and a report pages long written in the treasurer's best bureaucratese, for the other committee members either to switch off or to take the treasurer's words on trust, and to have no discussion on the figures. However, in expecting the treasurer to come down to their level of ignorance, indifference and innumeracy the other committee members are failing in their responsibilities by refusing to come up to the treasurer's level. Remember, on matters financial the treasurer is at best only "primus inter pares" (first amongst equals), and the management committee are all jointly and severally responsible for financial management. If things go wrong financially, it is the whole committee who will "hang", not just the treasurer.

This aspect of the treasurer's report, especially the written commentary, that is, the imperative to engage the other management committee members, which makes this task by far the most difficult for a treasurer. In practice, the treasurer and committee will have to meet each other half way, with the treasurer making an effort to produce figure and a report which the rest of the management committee has a chance of understanding, if they make the effort, and it is up to the rest of the committee to make that effort.

How does the treasurer do his or her half of the deal? Primarily, by a process of simplification and concentrating on the vital few and not the trivial many, and by giving his or her report to the management committee sufficiently far in advance of the meeting for the committee to study the figures and the recommendations.

In order to do this last bit, the committee needs to fix its dates with due regard to the time it takes to make up the books, extract the figures and prepare the report. If as is recommended trustee meetings are held monthly, it will take up to a week for an efficient financial administrator to make up the books after the end of each month, and another week for a competent voluntary treasurer to prepare the reports, so allowing yet a further week for the committee to read and digest the reports, realistically, the management committee can't expect to meet until the 4th week of each month. You also need to bear in mind the accounting truth that the nearer to the end of an accounting period accounts are prepared, the less accurate they will be. You have always to trade off accuracy for timeliness - you can have accurate accounts, or timely accounts, you can't have both. Note that for

management purposes, the reports don't need to be dead accurate, just accurate enough for the variance analysis not to give misleading results.

Since what you are producing is not a set of statutory accounts, there are no set requirements, and the numerical tables can and should be simplified and results presented in the form of charts and graphs to make them more accessible. Thus, the primary weapon in the treasurer's armoury is simplification. A typical community group might have 24 budget headings for income and 36 for expenditure, [figure 24](#). With a little effort, both income and expenditure headings can be combined under half a dozen headlines, [figure 25](#). This needs to be done with some thought, say by grouping together all restricted grants, or all income from lettings, on the one hand and all the costs associated with staff and all the costs, other than staff, of running the office, on the other. The variance table, that is actual incomings and outgoings for the year to date compared with the budgeted incomings and outgoings for the year to date (taken from the cash flow projection), then becomes simple with only half a dozen entries under both income and expenditure, rather than typically 24 and 36, [figure 26](#). Displaying this information graphically, in bar chart form is both simple and illustrative, [figure 27](#). It is also worth-while preparing line graphs showing budgeted versus total income, expenditure and the balance between them, [figure 28](#). Where a significant variance is hidden within a heading, further graphs and a table can be easily prepared expanding the heading to show the individual items, which should be easy to grasp, with only half a dozen items per heading.

All the graphs and tables, including the variance analysis should be done on a cumulative (that is, running totals for the year to date) basis. This will smooth out any month by month fluctuations. Also, don't get hung up on the precise numbers, remembering that no budget is ever accurate to the nearest £, it is the trends that count.

Also, when looking at variances and trying to decide which ones to worry about and thus to draw to the attention of the committee we need not only to apply Pareto's principle, and concentrate on the vital few not the trivial many. We need also to shave with Occam's razor. (William of Occam was an English philosopher who first set out the important principle that when faced with alternative explanations for something that has happened, the simplest is the most likely to be true. This principle is called "Occam's razor", and the expression "shaving with Occam's razor" has come to mean applying the principle.) For variance analysis, the simplest solution is that the budget is wrong, so your first action when faced with a variance is to check the budget, or rather the assumptions we made when drawing up the budget.

7.4. Reporting hints and tips

When you come to write your report, here are some reminders and hints and tips:-

- ❖ A positive variance shows that what you actually received or spent out was greater than what you expected (budgeted) to receive or spend out
- ❖ A positive incoming variance is good – your actual incoming was greater than your budgeted incoming
- ❖ A positive outgoing variance is bad – your actual outgoing was greater than your budgeted outgoing
- ❖ A negative outgoing variance isn't automatically good. It may show that something planned hasn't happened. Projects running late always show a negative variance.
- ❖ Don't read too much into the precise numbers. Realistically, can you really forecast (budget) your incomings and outgoings to the nearest £1 (or £10, or even £100?)
- ❖ Is the variance just a matter of timing, and everything will be back on course by the time of the next report For example, if you budgeted for a grant to be received during the last week of July, but it actually arrived during the first week in August, your end July report will show a significant variance, but your end September report will show everything back on track. This is one good reason for carrying out the variance analysis on a cumulative basis – it smooths out variances due to such timing effects
- ❖ Apply Pareto analysis. That is, concentrate on the vital few – the major items of income or outgoing, particularly those over which you have some control – rather than the trivial many.

- ❖ When looking for explanations, shave with Occam's razor. That is, pick the simplest explanation, it's the most likely. The likeliest explanation for a variance is that the budget is wrong, so before looking at other explanations, review the budget, and especially any assumptions which underpin it
- ❖ It is trends which are important, not individual events, so look at previous reports before deciding if a variance in a line item is significant.
- ❖ Don't just report by exception, this usually ends up dwelling on what is going badly, so also point out where things are going well
- ❖ If you have paid staff, or volunteers who are closer to the action than yourself, talk to them. They may have a feel for what is going on, both positive and negative
- ❖ When making suggestions, be realistic, and don't expect either miracles or your people to act out of character. Any suggested action must be within the existing capabilities of your group
- ❖ Don't delay giving bad news, don't duck difficult issues, and don't put off till tomorrow what must be done today. The only result is to turn a current solvable difficulty into a future insolvable crisis. Remember, responsibility for managing money is a collective one, not yours alone, so make sure the management committee are told. As treasurer, this is your responsibility

To reinforce one of the points, when recommending courses of action, we need to recognise that large areas of the budget are outside our control. For example, if we find our income is down, because hall bookings are down, our first reaction might be to cut costs. Since staffing is the lion's share, we might look to make savings here, but how? We could, I suppose give someone the sack, but if they have been with us for more than 2 years we would have to pay them redundancy, and even when they have been with us less time, we might find ourselves on the wrong end of an industrial tribunal! We can at the margins put off buying equipment or making repairs, and can try and squeeze the heat, light, telephone and stationery bills, but if you already run a tight ship, there won't be much mileage in any of these, and the whole exercise can rapidly become, like rearranging the deck chairs on the Titanic, an exercise in futility, or at best, locking the stable door after the horse has bolted!

This brings out the one major disadvantage of variance analysis, and that it is a historic measure, of past performance that is, and often too far after the event to make corrective measures effective in the short term. By the time a variance has occurred and you have realised it, it is usually too late to do anything about it which will have sufficient effect to reverse the variance before the year end. There are two lessons:-

1. You must monitor your income and expenditure against budget frequently - for most organisations this means at least monthly. Traditionally, quarterly has been used, but this is only really satisfactory if your organisation is small or if you have adequate reserves
2. You must have reserves, that is, cash in the bank for the inevitable rainy day. These will tide you over until your corrective action kicks in. Reserves are discussed later in this publication.

In the foregoing, the implicit assumption is that variances will be adverse. That is, income less than budget, and/or expenditure greater than budget. Sometimes, variances will be favourable, with income up and expenditure down.

If you keep your finger on the pulse of your organisation, and as a trustee this is what you should be doing, since it is your responsibility to manage its day to day affairs, you may well be able to detect changes in the patterns of activities which will have an impact on your plans (the budget, in financial terms) long before these work through into the accounts and show up as a variance. For example, you have run for years pensioners afternoon bingo sessions, primarily for fellowship and support reasons, but it has proved a nice little earner. Many of the pensioners come to the bingo sessions straight from your lunch club. The commercial bingo hall in your town has new management, determined to halt and reverse the recent decline in its fortunes, and they decide to bus in pensioners from all over town, offering as an additional incentive to the free buses a lunch at heavily subsidised prices. Your pensioners desert your bingo sessions and lunch club in droves. You don't need

to be a rocket scientist to realise that it won't take long for this to work through your accounts as a series of adverse variances, and you need to get your retaliation in first, or at least before the variances show through into your accounts.

This anticipation or prediction of variances comes with knowledge and experience, but relates to another aspect of a good budget broken down by month, and that is that it is a mathematical model of your organisation, which you are using to predict the future. In the section on budgeting I wrote about sensitivity analysis - making changes in your assumptions to see what affect these would have. Predicting out-turn - what your financial position will be at the end of the year - is an extension of this. In fact, this is a good way of testing a variance for significance (meaning should I worry about it), since if out-turn isn't affected, the variance isn't (yet) significant. If the predicted out-turn is such that you can't live with it (because the deficit will eat into your reserves too deeply), then you have little choice but to revise the budget, either by looking to turn a problem round or make economies (i.e. spend less) or by obtaining additional income. If your recommendation to the management committee includes a revised budget, you should of course supply copies of the changes in the assumptions you have made.

To emphasise a further point; there is one disadvantage in using Excel (or indeed any similar spreadsheet) to prepare budgets, perform variance analyses and predict out-turns and that is it invests all the data with an air of false precision, with variances calculated and out-turns predicted to the nearest penny, when the accuracies of the budgets in the first place and the subsequent predictions are no better than at best + or - 2%. So don't get hung up on the precise numbers, and don't let your committee get hung up either. (Large organisations do this by providing figures rounded to the nearest £1,000. In principle you could do the same, but round to the nearest £100. However, this may be more extra work than the effort is worth).

For those of you who need or want to be able to do better than what is suggested above by way of predicting variances, especially if you are tracking income and expenditure at project level which is best practice, there is a technique called earned value analysis which goes a long way towards doing this. This is another of those techniques like risk management which was developed by the rocket scientists, but unfortunately, unlike risk management, which is discussed elsewhere in this document, it hasn't yet been simplified down for lay use. The technique has grown up on and out of critical path analysis (e.g. PERT), requiring both detailed logically connected plans covering every activity, and ways and means of measuring the progress of each activity. Such techniques work, but require both specialist knowledge and time and money to put into practice, such that they are really only worth-while when applied to large projects, well beyond the scope of the sort of community organisation envisaged in this publication.

Chapter 8

8. Turning a Receipts and Payments Account into an Income and Expenditure Account

In this publication, I'm assuming that you will prepare your budgets, keep your books of account and compile your reports to your management committee on a receipts and payments basis. I'm also assuming that you will be preparing your end of year accounts on an income and expenditure (that is, **accruals**) basis. These terms were outlined in the opening chapters.

The purists will tell you that only income and expenditure accounting provides a "true and fair view" of the financial affairs of an organisation, and the purists are right, which is why I'm recommending that you prepare your annual accounts on this basis. However, what the purists don't tell you is that it can take a lot of effort over several weeks to make the necessary adjustments to turn a receipts and payments account into an income and expenditure account, with a lot of this time taken up with getting the information together, and that is assuming you do get and keep everything and neatly file it away. As a result, even for community organisations with professionally qualified finance staff, it isn't really practicable to produce an income and expenditure account more frequently than quarterly, and by the time it is available, it is likely to be so out of date as to be next to useless for making management decisions. Hence my espousal of monthly monitoring of receipts and payments accounts and management by cash flow.

That said, some organisations will want to prepare quarterly reports on an accruals basis, and all but the smallest should aim to do so for their annual accounts, so how do we go about it?

8.1. The Accruals Concept

If we simply list all the money received and paid out during a period of time (Receipts and Payments Account), we probably won't have a complete picture of our financial situation. This is because our list doesn't show which accounting period (financial year) the receipts and payments belong to - it only lists what was received and paid out during the period. For instance, it doesn't take into account any unpaid invoices which were received during the period, or any bills paid in advance. Nor does it reflect any money received in advance, or any money owed to the group but not received during the period.

One of the basic ideas that runs through accountancy is the accruals (or matching) concept. This means we match up all receipts and payments to the accounting period in which they were earned or incurred. When we prepare accounts for a period of time (it may be for 1 month, 1 quarter, or, as in our case, 1 year) we should therefore only concern ourselves with the receipts and payments that relate directly to that period.

In practice, this means we need to:

- a. identify what income was actually "earned" during the accounting period (rather than what money was received and banked), and
- b. identify what expenditure was actually incurred during the period (rather than what payments were made)

Another of the ways in which income and expenditure accounts differ from receipts and payments accounts is in their treatment of capital items. Receipts and payments accounts show the full cost of these items at the time of purchase. Income and expenditure accounts spread the purchase over the life of the item, charging only a proportion of the cost to each year. This annual charge is called depreciation, arrived at, in principle, by dividing the cost of the item by its life. In practice, there are several techniques for working out depreciation, aimed at taking account of the faster loss in value of items the newer they are.

To convert a set of receipts and payments accounts into a set of income and expenditure accounts, first we need to do three things:-

1. Identify anything else which belongs to the year just ended and bring it in

2. Identify anything which does not belong to the year just ended and take it out
3. After we have done this, we need to identify all expenditure on fixed assets and replace it with a depreciation charge

8.1.1. To work out income:-

1. Start with the receipts for the year
2. Subtract (take out) grants or other money received in advance (i.e. income received last year for this year's work)
3. Add (bring in) any money owed to the organisation (debtors)
4. Add (bring in) any grants or money received in advance during the previous year for the year just ended's work.
5. Subtract (take out) any money owed to the organisation at the end of the previous year (the previous year's debtors (assuming that is that they actually paid up)

8.1.2. To work out expenditure:-

- ❖ Start with payments for the year
- ❖ Add (bring in) any money owed by the organisation (creditors and accruals)
- ❖ Subtract (take out) any payments made in advance (i.e. money paid out last year for this year's work)
- ❖ Subtract (take out) any money owed by the organisation at the end of the previous year (i.e. the previous year's creditors and accruals) (assuming that is that you actually paid up)
- ❖ Add (bring in) any prepayments made in advance as at the end of the previous year (last year's prepayments)

8.1.3. To adjust for depreciation:-

- ❖ Subtract (take out) any payments made to purchase fixed assets and add back (bring in) the depreciation charge not only for the fixed assets purchased in the year but also for all the fixed assets purchased in previous years

We actually make the adjustments using a working sheet or sheets, [figure 29](#), starting in the first numerical column with the balances taken from our receipt and payments account, after we have added in the petty cash expenditure. We then work through the working sheet systematically, identifying and listing in the appropriate adjustment column the value of each adjustment, and then adding in or subtracting the adjustments to give us the income and expenditure account in the appropriate column. Note that all the adjustments we make will also appear in our balance sheet, either as adjustments to assets or liabilities, or as assets and liabilities themselves. [Figure 30](#) is an example of a completed working sheet, and [figure 31](#) shows the resulting income and expenditure account.

8.2. Depreciation

Depreciation is an accounting concept much misunderstood. For a start, it is a non-cash item, that is something expressed in money's worth which doesn't represent money actually paid out. For another, it is not a sum of money set aside to replace an asset when it is worn out. What it is is an estimate of how much of the value of an asset we use up in a year. This is easy to visualise if the asset is a coal mine. The total value of all the coal in the mine when we first started the mine is the original value of the asset. Each year, we dig out an amount of coal, and the value of that amount is depreciation – the loss in value of an asset due to its being consumed. We actually need two figures for our accounts. One is the depreciation charge for the year, which is the value of the coal we dug out in the year, and the other is the current value of the coal mine, the value of the coal left in the mine, in other words, but always calculated as the value shown in last year's books, less this year's depreciation.

What is less easy is to extend this concept to items, like furniture or computers where we can't see or measure how much of their value is used up each year. For these, (and in practice for all fixed assets) we resort to calculation. We know what we paid for the asset, a computer, say, and we can make an educated guess

at what it will be worth when it is no longer of any use to us, because it is broken and not worth repairing or so out of date it won't run the software we need to use. We also know from past experience, or can make another educated guess, that this will be, on average, a number of years after we purchased it, say 4 or 5 years.

In principle there are two basic methods for calculating depreciation, the straight line method and the reducing balance method. Which you use depends on the nature of the asset, and ultimately on your judgement.

The straight line method simply divides what we paid for the item, less what we expect to get for it when we dispose of it (i.e. its residual value), by its estimated life. In our example, if a computer cost us £500, we expect to keep it 4 years, and think we'll be able to get £50 for it at the end of the 4 years, then the depreciation charge per year is $(£500-£50)/4 = £112.50$. We could express this as an equation

$$d = (p-r)/l$$

where d = depreciation charge per year

p = purchase price

r = residual price (i.e. its second hand value)

l = useful life

Since the straight line method is simple, why don't we use it for everything? Because life isn't that simple, and our experience tells us that some items, motor cars are an obvious example, lose value much faster when they are new than when they are older. We all know that, having just paid out £10,000 of our redundancy money on a new motor, immediately we drive it out of the show-room it is worth £1,000 less than we paid for it! For such items, and computers and similar high technology equipment are also such items, we use the reducing balance method.

The reducing balance method deducts a fixed percentage for depreciation each year, in the first year on the purchase price, but in the second and subsequent years on the purchase price, less the depreciation charged in all the previous years. In our example, and taking a percentage of 25%, in the first year, the depreciation charge will be 25% of £500, or £125. In the second year, the depreciation charge will be 25% of $(£500-£125)$ or 25% of £375 = £93.75. In the third year, depreciation will be 25% of $(£375-£93.75) = £70.31$, and in the fourth year 25% of $(£281.25 - £70.31) = £52.74$. This would imply that our computer has a residual value of £158.2, which we know is too high, having judged its residual value to be £50. So what is wrong? The answer is simple – our % rate of depreciation is too low. How then, apart from guess-work, do we know what % rate to apply? There is a way of calculating this, as follows:-

$$\%d = 1 - (r/p)^{1/l}$$

where %d = % depreciation rate per year

p = purchase price

r = residual price (i.e. its second hand value)

l = useful life

In our example, $1 - (r/p)^{1/l} = 1 - (50/500)^{1/4} = 44\%$.

But, what if your maths isn't up to finding the nth root of a number? The answer is to get Excel to do it for you. Excel has a whole range of mathematical functions, including several which calculate depreciation. In Excel the reducing balance method is called the declining balance method.

There is one problem with the reducing balance method, and that is the equation only works if the item has a significant residual value. If after 4 years, say, we expect our computer to be so old technology that it will be worthless, our formula won't work, because we can't divide by zero. What do we do? The simple answer is to use an alternative method of calculating depreciation. Excel has several to choose from, but the easiest to understand is the sum of the year's digits method.

The sum of the year's digits method adds up all the digits in all the years over the life of the item, in our example, for an item with a 4 year life if is $4 + 3 + 2 + 1 = 10$. Then, in the first year, depreciation is charged at

4/10 of the difference between the purchase price and the residual price, in the second year at 3/10, in the third year at 2/10 and in the 4th. Year at 1/10. Again, we can let Excel take the strain.

As with anything in accountancy, there are rules:-

The rules say that we must depreciate every fixed asset we own, except land. Hang on, though, what about buildings, surely they increased in value over time? Yes, they do, but you should still depreciate them over their useful life – assume a useful life of 50 years, and a residual value of 10% of the purchase price.

One of the other rules of accountancy says that, in addition to charging depreciation each year, we must carry out an impairment review of all our fixed assets each year, and it is through the impairment review that we account for the fact that our property has increased in value. As the name suggests, the real purpose of an impairment review is to look at the current value of each item on our books and adjust this value to reflect the current market value, if necessary. For example, we spent £2,000 on a state-of-the-art desk-top photocopier, which we expected to have a useful life to us of 5 years, and fetch £500 when we came to sell it at the end of 5 years. We used the sum of the year's digits method to calculate depreciation, and at the end of the third year the value of the photocopier on our books is £800. Unfortunately, we have just learned that there has been a breakthrough in technology, and a new technology machine with better performance to ours now costs £1,000. Clearly, our old technology machine isn't worth anything like £800, and we need to make an adjustment in our accounts by charging additional depreciation. For property, we do the same, but in this case, the revaluation charge will have the affect of increasing the book value of the property, not reduce it.

Another accounting rule says that we can't chop and change our method of calculating depreciation from year to year. Once we've made a decision about the method to use, the useful life and the rate of depreciation for each type of fixed asset, and we are supposed to set out the rules we apply in the notes to our accounts, we can't change the rules, unless and until some external factor means that the rule is no longer valid. If we do change the rule, not only must we justify our decision in the notes to our accounts, we must go back and recalculate all the numbers in last year's accounts affected by the change in the rule. This "status quo" rule applies to all our accounting policies and procedures, not just to depreciation.

If you, as you should, maintain an asset register (qv), it is in the register that you should note the original cost of each item in the register, work out the depreciation on each item in each year, recording its accumulated depreciation (the sum of the depreciation charges in each of the years you have had the item) and its net book value (what you paid for it, less the accumulated depreciation).

8.3. The Balance Sheet

Another major way in which income and expenditure accounts differ from receipts and payments accounts is that they are always accompanied by a balance sheet. That is, a statement of a group's assets – it's fixed assets, it's cash in hand and at the bank, and its debtors – and its liabilities – it's creditors, at a particular date. The fixed assets – the capital items purchased – are shown in the balance sheet at their current worth, arrived at by subtracting depreciation from their worth the previous year.

8.3.1. The accounting equation

Another of the basic concepts that runs through accounting is the accounting equation. This states that
Capital = Assets – Liabilities.

Because in this basic form the equation raises the hackles of some in the voluntary sector, for them the equation is usually restated as

Accumulated Fund (or Available Fund, or just plain Funds) = Assets – Liabilities.

If there is capital, who are the capitalists? In a business, and in this category are included the trading subsidiaries of charities, they are the owners, i.e. the shareholders or partners. In a non-charitable club or society, the owners are the members, even if the stated intention of the club or society isn't to build up capital.

In a charity, there are no owners as such, certainly not the members or trustees, but the accumulated fund does belong to somebody, and that is the beneficiaries. The trust of any charity is strictly its accumulated fund, and this is held by the trustees on behalf of the beneficiaries.

The formal statement of the accounting equation for an organisation at a defined point in time is the balance sheet, drawn up in the form of a list:-

Assets

- Liabilities

= Accumulated Fund

The object of a balance sheet is to show a record of the assets and liabilities of an organisation at a particular date. It "takes stock" of the wealth of an organisation, at the agreed date, by listing all the assets and liabilities at that date, and not just the bank balance, and then adds up the assets and subtracts the liabilities to arrive at the "net wealth" of the organisation at the agreed date, usually the financial year end. The balance sheet does not cover a year of transactions in the way the income and expenditure account does.

Assets are of 2 types: Fixed Assets and Current Assets. Fixed Assets will have a useful life of more than one year. Examples of fixed assets include land and buildings, office equipment, motor vehicles and furniture. Fixed assets are depreciated over their useful life. Current assets can be converted into cash in a relatively short time (i.e. they are liquid assets). Examples of current assets are stock, debtors and pre-paid expenses, bank account balances and cash in hand.

Stock is the items of value we keep by us, primarily to sell or use, include the alcoholic and soft drinks, the cigarettes for the vending machine, the pre-packaged snacks, tea, coffee, soft drinks, and the uncooked and processed food, fresh and frozen, for the coffee bar and lunch club, and all the stuff not only in our stationery cupboard but also in the cleaners cubby-hole.

Debtors are people or organisations who owe us money at the end of the accounting period, but have not yet paid us. These might be people who have come on a training course but not yet paid for their places, or bought booklets but not yet released the money. In all these examples, we have "earned" the money during the period, so we need to include the amounts in our income.

Prepaid expenses are amounts which we have paid out for a future period. They don't relate to the period in question so we need to deduct them from our expenditure. A common example of prepaid expenses is an insurance premium, which is usually paid in advance for the whole of the following year.

Bank account balances are the balances held in current, deposit or any other bank accounts at the end of the accounting period are included in the balance sheet. The figure from your reconciled cash book is the one to use, not the balances shown on the bank statements. Note that an overdraft will be shown as a liability.

Cash in hand is the amount of money left in the petty cash tin at the balance sheet date.

Debtors and prepaid expenses form part of our ASSETS on the balance sheet because they are favourable balances.

Liabilities are divided between current liabilities and long term liabilities. Current liabilities are short term liabilities, to be paid within one year of the balance sheet date, including creditors and accrued expenses and any short-term loans, such as a bank overdraft. Long term liabilities are any liabilities not due to be repaid for more than a year from the balance sheet date.

Creditors are people or organisations to whom we know we owe money at the end of the accounting period, but have not yet paid. These will be bills in our unpaid invoices file, such as stationery bills, electricity bills, etc. We need to include these amounts in our accounts because we have already incurred this expenditure even though we haven't yet paid out the money.

Another type of creditor occurs when money has been received in advance (for a future period). For example, a funder may send us a grant cheque for a project that hasn't started yet. If we decided to abandon the project, we would have to pay this grant back. Any grant received in advance needs to be deducted from our receipts for the period.

Accrued expenses: Sometimes we know we have incurred expenditure even though we haven't actually received a bill yet. We may not even know how much we will have to pay, but if we can make a reasonable estimate we can include this in our expenditure as well. Common examples of this are the cost of telephone calls or gas and electricity for which we only receive bills every three months.

Creditors and accrued expenses for part of our LIABILITIES because they are unfavourable balances.

Long term liabilities are amounts we have to repay more than a year into the future, usually loans and mortgages which we have taken out or entered into to carry out major repairs or improvements to our community building. Also, when groups start, they may well be lent money on favourable terms by their founders to be repaid at some future date. It is important to establish when any loan is repayable, as your group may need to seek alternative sources of finance to repay them.

Having got these definitions out of the way, we can now express the accounting equation in terms we can understand

Fixed Assets

Land & buildings - net book value

Fittings and Fixtures - net book value

Furniture and Equipment - net book value

Office Equipment - net book value

Total Fixed Assets

Current Assets

Stock

Debtors and pre-paid expenses

Cash at Bank

Cash in Hand

Total Current Assets

Creditors – amounts falling due in less than one year

Creditors and accrued expenses

Net current assets (= Total current assets – Creditors)

Net Assets (= Net current assets + Total fixed assets)

And Net Assets must = **Accumulated Fund**

Figure 32 shows a completed balance sheet.

The accumulated fund is the amount of money your organisation is worth (on paper) after collecting all the money in and paying off all its debts. Assets would have to be re-valued to the latest market values before this is achieved. For charities, the accumulated fund is made up of three elements:-

- Restricted funds – these have conditions attached
- Unrestricted funds – these don't have conditions attached
- Endowment funds – usually, only the income from these can be spent.

The accumulated fund is also the sum of the surpluses and deficits made since day one of an organisation's life. At the end of the first year, it will be the same as the surplus or deficit for that year. At the end of the second year, it will be the surplus for the first year plus the surplus (or minus the deficit) for the second year, and so on. Overall, your accumulated fund must be in surplus, or your organisation is insolvent, and will be unable to pay its debts, if these are called in.

Another common misconception is that charities cannot be bankrupt. Whilst it may be true that creditors are reluctant to force a charity into bankruptcy, there is nothing stop them doing so. Indeed, it is when a charity is insolvent that its trustees (i.e. the management committee) are most at risk, for if the charity is unincorporated, the debts of the charity become the joint and several responsibility of the trustees personally, and if it is a limited company, the directors (i.e. the management committee) risk being prosecuted under the criminal law for trading whilst insolvent.

Chapter 9

9. End of Year Accounts

Earlier in this document, it is recommended that you should prepare your end of year accounts on an accruals basis, to show a true and fair view of your position at the year end, rather than on a receipts and payments basis, and the preceding section has shown how to turn a receipts and payments account and its accompanying SOAL (Statement of Assets and Liabilities) into an accruals account to produce an income and expenditure account and a balance sheet.

The layout of an income and expenditure account will be identical to that of a receipts and payments account, with each entry, corresponding to a budget line item being a summary of a column in your analysis book, with adjustments for prepayments and accruals, and so on. However, if you are a charity, in order to meet the requirements of the charities SORP (statement of recommended practice) you need to present your income and expenditure account in the form of a SOFA (Statement of Financial Activities). It is further recommended later in this document that you do this by obtaining and filling in Charity Commission pack CC17.

The first thing that will strike you when you look at the SOFA template in CC17a, [figure 33](#), is that the suggested labels in CC17a bear no relation to your own analysis headings and budget line items labels. Your headings should reflect your management needs, with the information collected by you and summarised only because you need it to make proper decisions about your charity's money. In practice, there may be some modification of this principle to make it easy to locate information requested or required by your funders and even the Charity Commissioners, but the principle still stands.

The SOFA headings start from a different premise, and that is the need to be able to compare one charity's accounts with another - to compare apples with apples, and if this is to be done, all accounts must be presented on an identical basis. The SOFA seeks to do this, and compliance would require you either to keep your accounts using the SOFA headings (mostly meaningless from a day-to-day management perspective) or for you to conduct a mapping exercise so that you could translate your management headings into SOFA headings, in effect requiring you to produce both an income and expenditure accounts and a SOFA. The good news for unincorporated charities below the current audit threshold (£250,000, increasing to £500,000 in early 2007) is that the SOFA headings aren't compulsory, so you can safely ignore them when preparing CC17, by ticking the box to indicate you are using natural classification and proceeding to do just that.

Apart from the format, the significant difference between an income and expenditure account and a SOFA is that the latter is in fact not one account but (potentially) 3, with each of the three funds of a charity, the restricted fund, the unrestricted fund and the endowment fund (if you have one) accounted for separately. Note that, even if you opt to prepare receipts and payments accounts you will still have to separate out the three funds.

In principle, we shouldn't talk about a restricted fund but about restricted funds, since each source of restricted income is a separate charitable trust. In practice, we lump all the restricted funds together in our end of year accounts. However, in the notes to the accounts we should show the movements of each and every restricted fund separately, and this is where any papering over the cracks begins to show.

There are two common issues with restricted funds, surpluses and deficits:

1. Surpluses occur when all the work which a restricted fund was paying for or towards is completed without all the money being spent. In principle, we should hand this money back to the funder. In practice, we operate the first law of Ferengi economics - when we have got our hands on the money, we never, ever, give it back. If the sum of money left is substantial we need to write to the funder proposing a project, or other use for the money, which is in spirit within the intent of the original grant or donation. If the sum is small, we propose that it be transferred to our unrestricted fund. Note that restricted surpluses can arise if an appeal we make for funds is

over-subscribed. What we need to do is to add small print to our appeal literature to the effect that if the appeal is oversubscribed and surplus will be put to the general purposes of our charity. If we didn't remember the small print, and we can't individually identify our donors, we need to hold a public meeting and obtain the consent of those present to whatever we propose to do with the money, either put it to the nearest similar project, not necessarily one of ours, or to put it into our general funds.

2. Deficits are the opposite of surpluses, occurring when it cost us more to do the work than the funder made available. One school of thought points out that there cannot be such a deficit, with any overspend automatically being picked up and paid for out of general (unrestricted) funds. This line of logic is reasonable if you are on the ball with your management of projects and if you have adequate unrestricted funds, but doesn't allow for the real world, where there may be both limited unrestricted funding and less than perfect project management. For many organisations, the true state of affairs only comes to light when they are preparing their end of year accounts, which show that they have one or more restricted funds in deficit, and that these deficits have been funded by "robbing Peter to pay Paul", that is, using other restricted funds, currently in credit, to finance the ones in deficit. In a strictly legal sense, it is not permissible to use one restricted fund to bail out another. In practice, it is widely done, especially where organisations have become over-dependent on restricted funds (which shouldn't be the case with a community organisation.) Nobody is going to get too worked up if you "borrow" money from a restricted fund for cash flow reasons or to cope with a short term problem, provided that once the fund you have "borrowed" from needs its money it is available. Indeed the Charity Commissioners in their guidance on annual accounts and reports anticipates that some restricted funds might be in deficit because it charges the trustees with saying what they intend to do about it.

The real problems arise when robbing Peter to pay Paul becomes a habit, with every year a new restricted funds having to be brought on stream to fund the increasing accumulated deficits of previous restricted funds. The best way to avoid sliding down this particular slippery slope is have sufficient unrestricted funds so that any deficits can be made good from these, and is another good argument for building up reserves (qv).

There is one further issue about restricted funds in deficit and that relates to one of the disadvantages of being a limited company. Technically, an organisation which cannot settle its debts except by "borrowing" clients money, for that is what restricted funds are, is insolvent. Trading (in this context, continuing to operate) whilst insolvent is a criminal offence for limited company directors. Whilst all concerned might turn a blind eye to the situation, it is neither comfortable nor sustainable.

The way to avoid the discomfort resulting from overspending a restricted fund is to manage your restricted funds, that is projects, properly, so you get fair warning of them slipping into deficit and can do something about it before it is too late.

Chapter 10

10. Grants, Service Level Agreements, Contracts and Best Value

A grant is a sum of money given to you for a specified purpose. The specified purpose may have been set out by you, or by the grant giver. It may be unrestricted, that is, without conditions, or restricted, that is with conditions attached. Unrestricted grants are usually given to help you further the objects, in whole or in part, set out in your constitution. Restricted grants are more specific, funding or part-funding a project, an activity or the purchase of a fixed asset.

A contract is a legally enforceable agreement between two parties (individuals or organisations) for one of the parties to do something for or supply something to the other party in exchange for money (or something worth money). Strictly, contracts don't have to be in writing, but without a written agreement, may be difficult to enforce if a dispute arises. For a contract to be valid, the parties to it must be in a legal sense both competent and a person, and herein lies a problem for unincorporated community organisations, since they aren't legal persons (unlike registered companies) and thus can't enter into contracts. In day-to-day dealings with statutory authorities, suppliers and the public, most of whom neither know nor care about the strict legality, this won't matter, provided you pay your bills on time, and they deliver the goods, but ignoring the niceties won't help you when things go wrong. To get round this problem, it is the management committee members, usually one or more of the officers, who enter into contracts as individuals, but on behalf of the unincorporated organisation. Such arrangements must be discussed at management committee meetings, with the discussion and especially the decisions, minuted. It is also why there has to be all that palaver about holding trustees, when you finally manage to get the lease sorted.

Another pre-requisite for a contract is the money or something of money's worth – the consideration, in contract law. If you don't pay for it, or the other party doesn't pay you for it, there is no contract, which is why for leases, licenses and the like to be worth the paper they are written on there has to be a nominal sum of money – traditionally, a peppercorn was recognised as being the smallest item worth money, which is why a peppercorn rent makes a lease a legally enforceable contract.

A service level agreement is just, ignoring the niceties of adjectival nouns, what it says – an agreement for you to provide a service at an agreed level. For example, your community centre kitchen may be providing 50 hot meals a day to the residents of the local sheltered housing scheme for the elderly, under an agreement with Social Services. There will be a contract, specifying what the service is (the supply of hot meals to the sheltered housing scheme, in our example), and what level of service is required (50 meals a day), and setting out how much money you are to be paid for delivering the service. The contract should also specify the type, variety and quality of the meals, and the means of delivery.

Ah, I hear you say, grants are different to Service Level Agreements. Would that it were that simple! Unrestricted grants are almost certainly not contracts, they are donations. However, restricted grants may well be contracts, indeed may well be to all intents and purposes Service Level Agreements, depending on the terms and conditions which form the restrictions. But, I hear you say, all this is academic – if our restricted grants are in fact service level agreements (and we've got some of those too), all this is primary purpose trading, (of which more anon) so what's the problem? The problem is the VATman.

If a grant is in fact a donation it falls outside the scope of VAT, and therefore doesn't count in your VAT threshold calculations. If, however, the restrictions on the grant are such that it is, in effect, a service level agreement, then this falls within the scope of VAT, and does count towards your VAT threshold. Since at the time of writing the VAT threshold is only £61,000, a £65,000 restricted grant could take you over the VAT threshold, obliging you to register for VAT, and charge VAT on many of the services you provide.

Further Information:-

CC37 - Charities and Contracts

A guide for smaller charities entering into contracts to provide services on behalf of public bodies

10.1. Best Value

Local governments employ a lot of people and since employing a lot of people costs a lot of money, a significant percentage of the money raised in taxes, VAT, rates and so on end up being spent by local authorities. Over the years, many individuals and organisations, including central government, had come to the conclusion that a lot of the money - our money – wasn't being particularly well spent, and in 1999 central government passed legislation which obliged all local authorities in England to embark on a review of all their services, with the objectives of providing

- ❖ Better quality services at reasonable cost
- ❖ More say for local people

The government of the day called this process, which is on-going, "Best Value".

What "best value" obliges local authorities to do is to review each and every service it provides, directly or indirectly, over a 5 year cycle, and then at least every 5 years thereafter, against 4 criteria. They are to

1. Challenge each service to ensure that
 - a. It is necessary
 - b. The way it is being provided is the most appropriate
2. Consult with local people and organisations, their employees and other service providers, to ensure that
 - a. Services are supplied in a way which satisfies local people and organisations
 - b. Suggestions for improvement are considered and implemented
3. Compare their services to those of other local authorities and service providers to ensure that they are up with the best
4. Compete each service, to ensure that either they or their service provider, separately or in partnership, are the best available.

The implication behind these questions is that the answers are:-

1. The service isn't necessary, or if it is, isn't being provided in the most appropriate way
2. The service should be responsive to local needs and influenced by local opinion
3. Other local authorities and service providers are doing it better
4. Other service providers, including the voluntary and community sectors could do a better job with the money

There are at least 4 reasons why this process is relevant to community organisations.

1. Local authorities are often the major sponsors of community organisations, providing for the fortunate both grants and premises at reduced rents, and advice and other assistance. Accordingly, at least once every 5 years the grants, rents and other non-financial indirect assistance will be subjected to a best value review, as will any services you provide, such as elders lunch clubs, which are commissioned by or supported by local authorities
2. There are opportunities for community organisations to take on the provision of essential services to local people. In fact, many already do, including running community buildings a darn sight better and at a fraction of the cost than when the local authority ran it
3. Community organisations are the natural vehicle through which local people to have their say
4. The principles behind best value apply equally to community organisations as to local authorities

The radical change which best value was supposed to engender hasn't come to pass, and local authorities aren't noticeably more efficient and effective than they were 6 years ago. The whole process has got bogged down in the sort of bureaucracy and vested interest that it was supposed to rise above. That said, the regular reviews of their services by local authorities, even if in reality it ends up as going through the motions, is no bad

thing, and applying the 4 Cs (as the 4 questions are called) to a community organisation's own services is good practice.

Your local authority will have published Best Value Performance Plans and Reviews, which you should consult to find out what is going on and how you can get your organisation involved in your area. You can obtain further information on Best Value from the Department for Communities and local Government at: www.odpm.gov.uk <http://www.communities.gov.uk/index.asp?id=1135897> and following the links from the local government page.

Chapter 11

11. Full Cost Recovery, marginal costs, unit costs and pricing.

11.1. Full Cost Recovery

What is full cost recovery?

1. A budgeting tool for determining the true cost of a project, not only the direct costs but also a fair proportion of the organisation's overheads.
2. The pricing of projects such that the funds received cover not only the project's *direct cost* but also a fair proportion of the organisation's *indirect costs*.

If your community organisation has been using full cost recovery for years, or has already switched to using full cost recovery, then you can give yourselves a pat on the back, and can skip this section. If you haven't, then this section is your wake-up call.

Too many voluntary organisations, including many community organisations, have fallen into the trap of dividing their costs into project costs and core costs. Project costs they define as those costs which relate directly to the service they deliver, such as the wages of the staff working on the project, and the materials used by the project. Core costs they define as the costs of "minding the shop", that is, the costs of running the community building, including staffing it, cleaning it, heating it and lighting it. Some organisations, recognising that projects also need to be "housed, fed and watered" charge a notional rent to the project, or make an administration charge, in the vague hope that these will cover the core costs. Traditionally, such organisations have sought grants to cover project costs, and fundraised to cover core costs, since funders, being canny beggars, have traditionally declined to provide grants for these. Inadvertently, such organisations have been using marginal costing to price projects

It has slowly begun to dawn on voluntary organisations that they have been subsidising projects, many funded by statutory bodies, because even where contributions are taken from projects towards core costs, they are nowhere near sufficient to cover these, which are in fact shared costs across projects and on-going activities alike. Recently, both the voluntary sector and the statutory agencies have realised that such a state of affairs cannot be sustained, and there is a move afoot to re-educate both funded and funders so that projects are costed to include a realistic contribution towards core costs, and that such costings are acceptable to funders. This move is being spear-headed by ACEVO (The Association of Chief Executives of Voluntary Organisations), who have developed a methodology, and have commissioned Sayer-Vincent (Accountants specialising in charities) to provide training in its use.

The principles behind full cost recovery are simple, the practices for complex organisations like community associations less so. Starting with the simple. A voluntary organisation does community development work on a run-down housing estate. It has three projects on the go, separately funded, each employing one worker. It operates out of a house on the estate, rented from the housing authority, where the workers are based, and where a paid administrator is based. We can easily see that each project ought to bear the cost of its worker, and of any equipment, like the rugged laptops they have, and the materials they use. We can also see that they ought to pay towards their share of the rent, rates, heat, light, telephones and so on and so forth.

Since there are 4 people based at the house, common sense suggests that each project ought to pay 1 person's share of these overheads, or $\frac{1}{4}$ of them. But what about the administrator, and her share of the overheads – the core costs, if you like? If there are no other sources of funding to cover these, then full cost recovery requires that her wages and her share of the overheads be apportioned to each project, so that, in addition to the wages of each worker, and the costs of laptops and materials, each project should pay $\frac{1}{3}$ of the administrator's

wages, and 1/3 of her share of the overheads. In effect, if all 4 workers are paid the same, each project picks up the bill for 1/3 of the total expenditure of the organisation.

Where real life gets more complicated is that the workers aren't all paid the same, the projects aren't all of the same size and don't all employ the same number of people, the administrator also works (part time) on one of the projects and there are other sources of income, apart from the project grants. The ACEVO methodology is a way of dealing with cost allocation and cost apportionment in these real life situations. Cost allocation is where a cost directly attributable to a project, like the wages of staff wholly employed to do the project – we call these direct costs – is charged to the project, and cost apportionment is where costs which are shared by several projects, like the rent of a shared office, or where costs aren't directly related to a project, such as the office manager's wages – we call these indirect costs – are shared out amongst the various project. Our method of allocation must be logical and consistent. It is in trying to make it fair that organisations come unstuck, because it all becomes too difficult. For most community organisations, once direct costs have been allocated, the simplest way is to spread all other costs – the indirect costs – across all the projects in proportion to the number of full-time-equivalent staff each project employs.

For example, we have 3 projects, one employs 1 full time staff, one employs 3 staff, one full-time and 2 on a job share, and one employs 4 part time staff, who work term time only. We also have a manager (full time) and an administrator/book-keeper (part time). All the part timers works 50% of the hours of the full-timers. The total number of our project staff, expressed as full time-equivalents, is $1 + 1 + _ + _ + (4 \times _) \times 39/52 = 4.5$. The first project is charged $1 / 4.5 (= 0.22, \text{ or } 22\%)$ of the indirect costs, including the wages of the manager and administrator/book-keeper, who aren't included in the project staff total, the second project is charged $2 / 4.5 (= 0.44 \text{ or } 44\%)$ of indirect costs, and the third, term time only project., is charged $1.5 / 4.5 (= 0.33, \text{ or } 33\%)$ of indirect costs. $22\% + 44\% + 33\% = 100\%$ (after rounding), which is what we are after.

There are more sophisticated ways of doing it, by trying to work out how much of their time the manager and administrator/book-keeper devotes to each project, but they probably aren't worth the effort for smaller organisations.

If it's that simple, why don't more community organisations do it? There are three reasons:-

1. Because they think it is too difficult – it isn't, or doesn't have to be, as illustrated above
2. Because they don't like the answer – their projects turn out to be a lot more expensive than they thought.
3. Because their funders don't like the implications – they can fund fewer projects for a given sum of money

. To illustrate, the last two points, let's run a few numbers, starting with full cost recovery, as a reminder about how straight-forward it is. In our example, a project workers are all paid £20,000 a year (part-timers pro-rata), the administrator/bookkeeper gets £22,500 a year (pro-rated to £11,750) and the manager gets £25,000 a year. Rent and rates are £10,000 a year, and all other costs are £20,000 a year. In our example, indirect costs are thus $£25,000 + £11,250 + £10,000 + £20,000 = £66,250$, apportioned across or 3 projects as £14,722, £29,444 and £22,084. Adding in the direct costs (in our simplified example, just project workers' wages), we get project 1 = $£20,000 + £14,722 = £34,722$, project 2 = $£40,000 + £29,444 = £69,444$ and project 3 costs $£30,000 + £22,084 = £52,084$. Total costs for the year are $£34,722 + £69,444 + £52,084 = £156,250$. (check: Direct wages = $4.5 \times £20,000$, indirect wages = $£25,000 + £22,500 / 2$, and other indirect costs = $£10,000 + £20,000$, for a total of £156,250)

So far, so good. But, in order to understand why some organisations and funders have concerns, let us now compare this full cost recovery method with the traditional method, in which we charged only part of the indirect costs to the projects, as follows:-

We have 6 full-time equivalent staff, and we decide to spread the office rent and overheads (less staff) across the projects in proportion to the number of staff they employ. Our “rent and overheads” are £30,000, which mean we are going to charge each project person £5,000 (= £30,000/6 to cover these) Our project costs then come out at Project 1 = £20,000 (wages) + £5,000 (overheads) = £25,000. Project 2 = £40,000 (wages) + £10,000 (overheads) = £50,000, and Project 3 = £30,000 (wages) + £7,500 (overheads) = £37,500.

Our core costs are the wages costs of the manager and administrator/book-keeper, at £36,250 (= £25,000 + £11,250) plus their share of the rent, rates and office overheads, at £7,500, for a total of £43,750. This is an awful lot of jumble sales, coffee mornings and car boot sales!

. If we, and our funders, have come to expect one of our projects to cost £25,000, when its’ real cost, determined by full cost recovery, is £34,722, then it isn’t surprising that neither of us trust the full cost recovery answer. From a narrow viewpoint, at least from the funder’s perspective, the implication is that they can either fund fewer projects for a given “pot of gold”, or they need a larger, indeed significantly, larger “pot” to fund the same number of projects. Fortunately, wiser counsels amongst funders now prevail, which take a long view, and recognise that, in the long term, organisations which are sustainably funded have a future. Those that aren’t, don’t.

Turning now to the viewpoint of the concerned community organisation, apart from disturbing the status quo and requiring the organisation to adopt new and apparently complicated procedures, is there some other reason why they are tempted to play ostrich? The answer is yes. Many community organisations pride themselves on being efficient and effective. Some are, but some are not, and costing projects using the full cost recovery method exposes those that have more chiefs than Indians. In principle, voluntary organisations ought to have an edge over both public and private sector organisations, in that their senior management comes free. For such organisations, full cost recovery is seen as a threat. It ought to be seen as their salvation, because unless they address the issues of their top-heavy structure, they won’t survive.

As an alternative to full cost recovery, we could have used an arbitrary percentage surcharge to try and cover our core costs. Clearly, 10% or even 25% won’t hack it, and we would have to add 75% (actually 73.6%) to our wages costs to cover all our true overheads. If you think that such a mark-up is unrealistic, work out the ratio of your staff costs to your overall costs. My rule of thumb says that these will make up anything between 50% and 75%, typically around 2/3, of your overall costs. Since this calculation ignores the overhead of your managers and administrators, a mark-up of 75% to cover all overheads looks fair enough. Most garages use full cost recovery costing, which is why they charge you £40 to £50 an hour for labour – garage mechanics aren’t that well paid, and the majority of the charge is to cover their overheads, including the wages of the store-keepers, foremen, clerks and managers as well as all the high-tech equipment they now need.

To emphasis a point, a Full Cost Recovery method should, nay must, be the standard way you prepare your budgets and cost your projects, whether or not (as you increasingly will be) are required to use full cost recovery by your funders. If, as a result, you find that your community organisation has a level of overheads which is difficult to justify, don’t ignore it, but take steps to turn your organisation into the lean, mean, fighting machine which it will need to become if it is to be fit for the future.

11.2. Marginal Costing

What about marginal costing, then? This is a widely used (and abused) method of costing looking at the cost of taking on an additional project, when all your costs are already covered by other projects, or of using spare capacity. For example, in the context of our community development organisation, we decide to run a holiday play scheme. The play worker can use one of the desks and computers “belonging” to project 3, which operates in term times only, and we judge that the extra supervision and administration/book-keeping can be coped with

by the existing staff, without requiring longer hours of work. The play worker is on a salary of £17,500 pro-rata, which for the 13 weeks of holidays costs us £4,375. Since our other costs are already covered, we quote £4,750 as the cost of the project. If we are canny, we might make an additional charge, as a contribution towards overheads. In our example, this would be £5,000 x 13/52, to be consistent with our standard (pre-full cost recovery) method, or £1,250, giving a total project cost of £5,625.

All sorts of arguments then arise about whether this isn't double charging, all of which fail to recognise that the reality of any method of costing depends on the assumptions you make about the level of your activities and the productivity of your staff. We all know (I hope) that when planning the annual char-a-banc trip to Skeggy we don't assume, for costing purposes, that all the seats on the coach will be filled, or that when organising the fund raising dance that all the tickets will be sold.

Incidentally, there is nothing wrong about taking on work, or even letting out a spare room, on a marginal costing basis, provided that we recognise that there will always be additional indirect costs, albeit small, and that we allow for these when pricing the work (or the room). However, once you extend the technique into areas where you need to add new capacity rather than absorb existing spare capacity, you are on increasingly shaky ground. In addition, if you do have 3 projects on a full cost recover basis, and one on a marginal cost recovery basis, the funders of the original 3 will soon want to know why their projects are so much more expensive than the new projects, which is where this all started!

11.3. Unit Costing

Unit costing is an extension of full cost recovery looking at our costs per unit of input or output – the garage example used earlier of £40 to £50 an hour is a unit cost, based on a mechanic's time – rather than the cost per project. When we want to work out how much we ought to charge for renting out our meeting room, or what we ought to charge per head for the senior citizens' lunch, we need to go into unit costing. When comparing the cost of our services with those of other organisations doing the same or similar things, we can't avoid unit costing, and if we do, our local authority when looking at best value certainly won't (though they might struggle to get the necessary figures!).

As I hinted at earlier, unit costing rests on a number of assumptions, not least for community organisations running community buildings, the number of hours the building is going to be used (used, note, not available), and how many hours do our staff actually work in a year (as opposed to being paid for). Taking the latter example first, and I'm not getting at staff here, we typically pay our staff to work for 35 hours per week for 52 weeks a year, at a notional salary of £20,000. 35 x 52 weeks is 1820 hours, giving an hourly rate (unit labour cost) per staff member of £10.99. Hang on, though – what about holidays and sickness? We are a generous lot, and give 5 weeks a year (plus bank holidays), and our sickness absence averages 1 week per member of staff a year. Taking these into account, our staff actually work only 52 – 5 – 2 – 1 weeks, or 44 weeks, which is 44 x 35 = 1540 hours. Using this gives us an hourly rate of £12.99. Oh, dear I've forgotten about training, and that our staff are only human and can't actually work at maximum efficiency all day and everyday, so we better assume that 10% of available hours are effectively "lost", meaning that we expect our staff to actually be working 1,386 hours a year, giving a more realistic hourly rate (unit labour cost) of £14.43.

Let's now look at room hire. Our community building has a hall and a meeting room, the latter being _ the size of the former. In theory, the building is available 24/7 (which is 8736 hours a year). In practice, it will be less than this, realistically, a lot less. Let's assume that we are in principle open from 9 am to 10 pm, with a hour for lunch and tea, 7 days a week, which gives 9 hours per day, 365 days a year, or 3,285 hours. Let's also assume that our costs are £50,000 a year. To recover these costs, we should charge £15.22 an hour for the building as a whole, which we translate into £3.04 per hour for the meeting room (1/5 of £15.22) and £12.18 per hour for the hall (4/5 of £15.22). In practice, we find that the building is only used 50% of the time it is available, so we are actually used only 1,643 hours. Our hourly rates then become £6.08 per hour for the meeting room, and £24.36 per hour for the hall. In reality, it will be a lot more complicated than this, with demand on some days greater

than on others, some days the hall being wanted and not the meeting room, and vice versa, and with costs being variable, since if the building is used after office hours and at week-ends, we have to employ hall-sitters at £5.35 an hour, time and a half on Saturday evenings and Sundays, and we can only arrive at a cost figure by assuming which particular hours will be taken, and what staffing and overhead costs will be incurred as a result, and arrive at separate unrelated rates for the meeting room and hall, which are strictly only valid for the conditions we have assumed. If we are feeling very clever, and have the time to spend, we might run to a sensitivity analysis, which is to make different assumptions, say assuming less or more hours, and look at the affect of these on the hourly rates. (This is when that algebra you did at school, and the functions in your spread-sheet program come in very handy!)

To finish off the topic, let us look at one of our outreach projects. This has one full time and 2 job share workers, giving in effect 2 workers. Their job is to visit homes and help whoever does the food buying and cooking towards healthier eating. We know that the true cost of the project is £69,444, and the workers achieve 1,386 hours of productive work a year, for a project hourly rate of $£69,444 / (2 \times 1386) = £25.05$. However, what we are interested in, and what our funder is paying for, is the number of clients helped. We know the staff can't make more than 2 visits on average a day each, and it takes on average 5 visits (over several weeks) to make a difference to the clients' diet. Given that they work 44 weeks a year, and thus make $44 \times 5 \times 2 = 4400$ visits, this translates into 88 clients helped per year each. Thus, the cost per client is $£69,444 / (88 \times 2) = £394.57$, which is our unit cost.

11.4. Pricing and costing.

Surely, these are two sides of the same coin? Yes, and no. Costing is what it costs you to provide goods or a service. Pricing is what you charge the customer for the goods or services.

You could price your goods or services at cost, but that way, there is neither margin for error nor the possibility of building up reserves for the inevitable rainy day.

You could, perhaps, should price on a cost plus basis, the plus being the profit margin - 5% is traditional. Remember, not for profit is a serious misnomer for the voluntary sector. Voluntary organisations should make profits, but invest these in improved services, rather than distributing them. How else are they to grow? Community organisations regularly have some very profitable activities, and use these to subsidise unprofitable ones. What voluntary organisations are

- ❖ Are not principally for profit
- ❖ Are not profit distributing

Alternatively, you could price your goods or services at what people and organisations are prepared to pay for them. If this is a lot more than it costs you, all well and good. If it is less, you have a problem. Because of their failure to embrace full cost recovery, many voluntary organisations have been supplying goods and services at less than cost and, what is unforgivable, not realising that this is what they have been doing. In reality, whether you realise it or not, market forces will determine your prices. To illustrate, taking the letting of our community building, what we can charge for lettings will to a large extent be determined by what other organisations with rooms for hire in our area are charging. Whether we like it or not, we are competing with them.

The same is true for services, such as our elderly persons lunch club, and therein lies the problem. If others are supplying a service at less than cost this becomes the market price, and we can do one of 3 things

- ❖ Provide the service, and hope to make up the difference from some other activity
- ❖ Decline to compete
- ❖ Wait for them to go bust (which they will eventually, unless they are offering the service as a loss-leader)

You could, I suppose try and persuade the funder that pricing at less than cost isn't sustainable in the long term, but if the funder has been getting the service for years under similar conditions (and perhaps subsidising the service indirectly through grant aid to cover your core costs) you are likely to receive short shrift. Another

downside of this approach, if your funder is prepared to play ball, at least in principle, is that they may want intimate details of how you have arrived at your costs, including all those assumptions about how productive your staff are, and what your ratios of direct to indirect staff are, and why, all of which you would rather not have made public.

You could try and compete on quality (which is what the management gurus always suggest), but if the problem with the existing service isn't quality but price, increasing your quality just puts up your costs even higher.

11.5. The Compact Code on Funding and Procurement:

The revised Code was published in March 2005. It has been revised to help maximise outcomes from government funding of voluntary organisations. This Code aims to influence behaviour in both the voluntary and community sector and government to achieve this vision by:

- ❖ Setting a framework for the financial relationship
- ❖ Setting out undertakings for both sides, based on what each side can expect from the other

The Funding Code has been revised in full consultation with government departments and the voluntary and community sector.

HM Treasury has developed useful information on working with the voluntary sector on its website. The Home Office State of the Sector Survey, the first part of which was published in January 2005 shows that the sector is generally hampered by lack of: capacity funding, premises, paid and volunteer staff, information, technology, and government regulation.

11.5.1. Key issues covered in the Code:

- ❖ Full cost recovery - organisations can develop their capacity through covering their organisational overhead costs in funding
- ❖ Longer term funding - enables organisations to plan their future work and means that they don't spend disproportionate resources chasing new or renewed funding
- ❖ Less bureaucratic application and tender process - again so resources go on delivery rather than applying for funding
- ❖ Payments in advance - so risk is properly allocated allowing organisations to develop in a sustainable way and plan future work
- ❖ Proportionate monitoring - resources are focussed on outcomes, not on unnecessary and disproportionate monitoring
- ❖ Proper planning for and notice of end of funding - allowing organisations to plan and develop more sustainable outcomes rather than face financial problems at the end of funding
- ❖ Effective governance principles for local partnership boards and how Local Compact development is to be paid for

11.6. The Big Lottery Fund and Full Cost Recovery

"In a response to the first phase of public consultation on how millions of pounds of National Lottery good-cause funds should be distributed, the [Big Lottery] Fund restated its commitment that 60-70% of all funding will go to the voluntary and community sector.

The Big Lottery Fund will also:

- ❖ Adopt the principle of full cost recovery to allow all legitimate overhead costs to be recovered by voluntary and community organisations;
- ❖ Introduce more flexibility in the length of funding available, including longer-term arrangements;
- ❖ Reduce 'red tape' by ensuring that application processes are minimised and monitoring procedures are proportionate to the size of the grant; and
- ❖ Remove administrative burdens by seeking opportunities to work closely with other funders at the programme planning, application and monitoring stages, where similar activity is being funded".

Further Information:-

Full Cost Recovery: A guide and toolkit on cost allocation, by Caroline Fiennes, Cathy Langerman & Jeni Vlahov
The guide is available in hard-copy or interactive CD Rom format and can be purchased from acevo (0845 345 8481) www.acevo.org.uk

Training on Full Cost Recovery has been developed by Sayer Vincent:

<http://www.sayervincent.co.uk/render.aspx?siteID=1&navIDs=1,5,39>

Acevo and NAVCA are undertaking a 3-year programme of education and training in full cost recovery. The programme will train development workers and other staff at local infrastructure organisations, providing them with the skills, knowledge and tools to offer affordable and sustainable support in full cost recovery to the smallest third sector organisations operating at a local level:

<http://www.fullcostrecovery.org.uk/main/index.php?content=home>

CASH's website has factsheets on

Full cost recovery: www.cash-online.org.uk/docs/1131390468fcr.doc and <http://www.cash-online.org.uk/docs/1131569162fcr.xls>

and on

unit costs and pricing: www.cash-online.org.uk/docs/1111522755unitcosts.pdf which is particularly relevant to community associations, since the case study is of the Tadshall Community Association which provides a wide range of services for refugees who have come to London in the last few years, fleeing a horrific civil war in their country.

Chapter 12

12. Alternatives to Excel - computerising your accounts.

“To err is human, to really screw up, you need a computer”

Those with experience of computerising anything will recognise the truth in the statement that choosing computer software is where dreams are planted, and nightmares harvested. Computerising your accounts is a serious step. Unfortunately, your books won't magically be kept and your final accounts appear at the press of a button, and in the short term, there will be more, not less, work.

Accounting software aimed at either the personal or small business markets is now widely available, affordable, and intended for day-to-day use by people without specialist knowledge, so what's the problem? Personal and business users have different needs to the voluntary sector. Generally, they only have one or two types of income and don't need to do project or fund accounting (that is, be able to account separately for the money received and spent against each individual grant). Voluntary organisations, especially if they are charities, generally have lots of different types of income and need to do project or fund accounting. Personal accounting software (Microsoft Money is the example, now that Quicken is no more) isn't generally suitable for community groups running community buildings. Business use software – Sage in its various flavours is typical - can be suitable, but specialist knowledge is needed both to set it up and more especially to configure and adapt it for use by the voluntary sector. By default, the format and presentation of the end of year accounts should be set up for a commercial enterprise, consisting of a Trading and Profit and Loss Account, and a Balance Sheet.

There is some accounting software designed or adapted specifically for the voluntary sector. Cashcall, by Data Developments written primarily around the requirements of churches, which are bound by charity law, is one example, and adopting one of these will help to reduce the risks and the work-load. By default, the format and presentation of the end of year accounts should be set up for charities, consisting of a Statement of Financial Activities and a Balance Sheet. However, what precisely is it that you want or need the software to do, and what are the advantages and disadvantages?

For many community organisations, staff are by far the largest expense, so if we follow Pareto's principle and concentrate on the vital few, perhaps it is payroll software we need? Here, there are no special rules and requirements for voluntary organisations, and payroll software for small businesses is equally suitable for community groups. There are a couple of provisos

- ❖ You have somebody who knows what they are doing
- ❖ You have worked out what to do when the woman who knows is off (sick or on holiday)

If you don't have either a woman who knows or a clue about what to do when she's off, you are better off sticking with a payroll bureau.

If you want to go beyond the payroll, what is it that you're after? Are you just looking for something which just does the book-keeping, or do you want management accounts, and/or end of year accounts, and if so, do you need these to comply with the charities SORP? Do you want or need sales and purchase ledgers (aka sold ledger and bought ledger, or accounts receivable and accounts payable)? Do you want or need to account for VAT? Do you need to have a clear and affordable upgrade path, starting simple and getting more complex as you grow? Who is going to operate the software, and what is their knowledge and experience? Who is going to provide support if and when they get stuck? Are we going to have to pay an annual fee, or upgrade the software frequently?

These are just a few of the questions you need to ask, and answer, before you can choose suitable accounting software for your group. That said, the choice of accounting software is decision-robust, so it doesn't matter too much precisely which software you buy, provided you have realistic expectations, and your staff, paid or volunteer, are up for it.

In case you haven't come across the concept before, it is possible to categorise most situations where a decision is required as either decision robust or decision sensitive. An example of a decision robust situation (and most consumer decisions are decision robust) is choosing a new washing machine when the old one is beyond repair. Provided we get a good price, and the make and supplier are reputable, it doesn't really matter whether we buy a Hotpoint or a Hoover, they'll, if we are brutally honest, both do an equally satisfactory job, and which one we choose is down to personal preference. A decision-sensitive situation is where the quality of our decision really matters – choosing a partner to spend our life and raise a family with is a prime example. Unfortunately, the perversity of human nature makes us behave as if decision robust situations are decision sensitive (which apart from being a waste of time and energy doesn't matter too much) and as if decision sensitive situations are decision robust (which is fraught with disaster).

Accountants and book-keepers will argue endlessly about the supposed merits and de-merits of Sage and Quick-books (and there are more suitable and cheaper alternatives, Moneysoft's MoneyManager for instance, to either), with some favouring one and some the other, but in the final analysis, provided you've computerised for the right reasons, and have readied yourselves for it, it won't matter which you pick – either will do the business.

What are the right reasons?

- You'll save time
 - It will require less effort for the same output and or timescales to produce outputs will be shorter
- You'll save money
 - We can pay our bookkeeper for less hours
 - We can employ a data entry clerk at a lower rate instead
- We can save on accountancy and independent examination fees
- You'll get information for decision-making you need but don't get now
- You'll get the information you get now quicker

Beware the siren voices about saving money through de-skilling. That is, employing a less skilled person to do the work at a lower rate of pay. In larger organisations with many book-keeping staff, this may be a realistic prospect, since you can reduce the average skill level and number of staff required whilst retaining a cadre of well-qualified and experienced staff, thus driving down the wages bill, but in an organisation where the book-keeper is a one-man-band, this can be fraught with disaster. Accounting software does or should make routine tasks simpler and easier. However, it is full of traps for the inexperienced and those lacking knowledge, and correcting miss-steps can rapidly become a job for experts. If you don't have an expert in house, you will have to buy them in, and you can easily spend a lot more on the trouble-shooter than you saved by de-skilling the job.

Remember, the software will embody double entry bookkeeping principles, though most don't advertise the fact, and/or hide it well, to avoid frightening off potential customers. The one time you need to know what these principles are is when undoing mistakes. If you don't have the knowledge in house, do you know someone who does, and what will it cost you?

If you do the sums, you will find that buying the software is the cheapest part. The most expensive part will be sending at least 2 people on the course to learn how to use it (and that will be just the standard bits, not the bits special to the voluntary sector). Especially if the program is aimed primarily at the small business sector, you must be prepared to pay for specialist help in reconfiguring it for you, in preparing it for use and in extracting the necessary starting data from your old system. You will also have to pay for access to the supplier's help line, for a broadband internet link (because that is the way that help will probably be delivered) and for annual upgrades (especially if the software has a payroll module).

Don't even think about accountancy software until

- You have good Excel spread-sheets (or good manual books) fully supported with filed paper

- You know what you want out of the software
- You have the hardware (high resolution monitor, up-to-date CPU with lots of hard disk space, a back-up system, a broad-band internet connection, a laser printer)
- You are computer literate and numerate
- You have access to expertise
- You have access to training
- You have the money to pay
 - For the software
 - For the annual upgrades
 - For the set-up and support expertise
 - For the training

If you decide you are ready to proceed with accounting software, and have made your choice, you will need

- Last year's accounts and balance sheet
- Details of suppliers and customers/clients
- Details of your bankers and bank accounts
- Your chart of accounts
 - Your income and expenditure analysis headings
- Your budget for the year
- Details of your employees
- Records of all receipts and all payments to be entered
 - Cross-referenced to your chart of accounts
- Help in setting up your new system
- Training
 - Either just before or just after you've started

You will also need to run your old system in parallel for at least 3 months, as insurance.

The optimum time to change is at the start of a new financial year. However, some accounting software requires that you have to enter all your previous year's end of year balances before you start to enter this year's data, which means you can't start using your new system until your previous year's accounts are available, leaving you with 3 (or more) months of transactions to post. Others aren't so fussy, and will allow you to fill in the start of year gaps as you go along, but these bring their own perils.

Whichever software you choose, full supporting paperwork filed away remains a pre-requisite.

Chapter 13

13. Paying People

This important chapter covers paying people “people who do work for you” , including

- ❖ Paying the self-employed
- ❖ Paying wages and salaries to employees
- ❖ Paying expenses
 - To employees
 - To volunteers
 - To your management committee members/trustees

important because if you employ staff,

- ❖ This will take up the lion's share of your budget – 2/3 to _ is not unusual
- ❖ The staff (along with your volunteers) are your greatest asset, and you need to manage your assets well

13.1. Introduction

Labour intensive industries, like health care and education, have always found that their costs have increased significantly faster than inflation, whereas capital-intensive ones, like manufacturing consumer goods, which have replaced people with technology have seen their costs fall (and that doesn't take account of the added reductions by exporting the work to low labour cost economies). The community sector, and especially that part of it involved with running or managing community buildings, is very labour-intensive. As more and more people come to be paid a living wage and as society's views of what constitutes a living wage and the levels of benefits payable to those who can't work mature, it is inevitable that labour costs in the voluntary sector will increase at a rate faster than inflation.

Community organisations have traditionally, consciously or unconsciously, contained their labour costs by a combination of reliance on volunteering and low wages. To a considerable degree, the reliance on volunteers and volunteering is both desirable and necessary, with community organisations gaining both benefits and credibility. However, it can't all be done by volunteering – most of us have to earn a living, and that leaves us insufficient time to do all that needs to be done in a voluntary capacity.

The reliance on low wages is more problematic. The minimum wage threshold has, since its introduction, increased at a faster rate than inflation, and looks set to continue to do so for the foreseeable future. In addition, although there will continue to be those content to earn pocket money wages in exchange for a few hours of undemanding work (such as hall sitting), there will be the need to attract and keep able staff in an increasingly competitive environment for those with the interpersonal and administrative skills that we seek. We can't and indeed shouldn't continue to rely on our staffs' commitment to the job and to our charities' objects to justify paying them less than the rate for the job. As a result, the dominance of community sector organization budgets by wage costs will continue to increase.

Pareto's principle states that we should concentrate on the vital few, rather than the trivial many, when it comes to managing. With wage costs the dominant factor in community organisation budgets, it is right and proper to concentrate on them. However, in reality, if we become involved in the financial management of any established community organisation we will find that our room to manoeuvre is limited. Existing staff will (or should) have contracts of employment, and their hours worked and rates of pay will already be laid down. If we are lucky, our predecessors will have fixed the positions, the hours worked and the rates of pay through a rational process of looking at what was needed, and what could realistically be afforded, given the state of the market-place when the positions were filled. If we are even luckier, they will have written this process down. Make no mistake - what ultimately drives the wages for any job is what you have to pay to get and keep somebody who can do it well enough to satisfy you. In any part of the country, and at any time, this is the rate for the job.

If we are unlucky, we will find that the contracts of employment, the hours worked and the rates of pay were inherited from when the local authority ran the community building and employed the staff, and that these now bear little relationship to either the local rate for the job, or what the local authority now offer for similar work. Especially in London, many community organisations tie their jobs and rates of pay to the NJC salary scales published by the NCVO/NAVCA, but ultimately determined by negotiations between the Local Government Employers Federation and the trades unions representing workers in local government. As NAVCA/NCVO make clear, the way in which these scales are used by local authorities has significantly diverged from the way it was a few years ago, though the voluntary sector by and large still sticks to the old ways. As a result, there is no longer (if there ever was, given the very different natures of the statutory and voluntary sectors) a good correlation between salaries in the statutory and voluntary sectors. It isn't just rates of pay which become problematic if the voluntary sector apes the statutory sector – many of the conditions of service, such as sick pay, non-contributory pensions, early retirement and the like, are beyond its means.

Nobody can force anybody to use our community centre and pay its charges, but local and central government can force us to pay our taxes and the community charge, so if they pay over the odds we have to pay, whereas if we pay over the odds, we will go bust. If we go bust, that is when having unlimited liability could cost us personally.

I'm not advocating the continued exploitation of the goodwill of our staff, far from it. What I am advocating is being hard-headed and realistic, and using other measures against which to evaluate what we should be paying our staff than just custom and practice and the NJC scales. For example, we should not only be looking at the NJC scales, but also the job advertisements in Wednesday's Guardian, and what other community centres in our local authority area, and in surrounding areas, are offering, and what private sector leisure facilities in our area are paying. In addition, whilst it is good practice to commit to an annual review of staff pay and conditions, and prudent to budget for (at least) an increase in line with inflation, you should never commit to having to pay an increase, whatever your group's financial circumstances. If paying an annual increment is the straw that breaks the camel's back, your staff could soon find themselves down the labour exchange, with the statutory minimum redundancy paid for out of government funds, rather than a job.

I accept that even where a new post is concerned, there may not be total freedom of room to manoeuvre. Creating differentials, favourable or unfavourable, between new and existing staff is fraught with difficulties, so you are bound to set any new post in the context of existing posts, and especially to preserving differentials resulting from skill or responsibility. Nevertheless, given that typically staff costs account for 2/3 of the budget, we must do all we can to ensure that wage rates are fair and reasonable, but not over-generous, and that staff do a fair days work in return, and where circumstances allow us to review, restructure and rationalise our rates of pay and conditions of employment, we must seize the opportunity so to do. On the other hand, if we expect the staff to share in the misery when times are tough, by foregoing cost of living increments, we should at least accept the moral case for the staff sharing in success when we have a good year (to which they will also have been major contributors) by offering a more generous settlement, or rewarding meritorious service.

On the question of compulsory redundancy, always an admission of failure on our part as financial managers if it becomes necessary, as charity trustees we have no authority to make payments to staff over and above whatever is written into their contracts of employment, or whatever the law requires, whichever is the more generous. If redundancy terms aren't set out in the staffs' terms and conditions, then whatever we can afford or feel morally obliged to pay is irrelevant. All we can pay without breaching charity law is the statutory minimum. Any payment over and above the strict legal obligations is viewed by the Charity Commissioners as an ex-gratia payment, and their express permission in advance to make such a payment would be required, their permission being predicated on our ability to convince them that such a payment was in the best interests of the charity.

13.2. Community Organisations and the Informal Economy.

Why this topic appears under "Paying People" is that most of what goes on is related, directly or indirectly to making payments to people.

The informal economy is the politically correct term for what used to be called the black economy. This covers a whole host of questionable and downright dishonest transactions designed to evade the tax man, the VAT man, the benefits agency, our creditors and Old Uncle Tom Cobbleigh and All. Those most familiar to community organisations running community buildings will be:-

- ❖ Employing people who aren't entitled to work in the UK
- ❖ Treating students who work for you during term time the same as students working for you during the vacations
- ❖ Payments to sub-contractors who are really staff
- ❖ Payments of cash in hand wages off the books,
- ❖ Payments of wages to people who are claiming benefits,
- ❖ Payments of wages to staff with other jobs, ignoring the other job for tax purposes
- ❖ Payments to volunteers over and above strict reimbursement,
- ❖ Provision of benefits in kind to staff and volunteers,
- ❖ Payments of expenses without either a dispensation being in place or a P9D returned,
- ❖ Payments in cash to trades-people in the absence of VAT invoices
- ❖ Purchase of goods
 - "Fallen off the back of a lorry"
 - "Imported for personal use (usually fags and booze)"

In principle, all are illegal and should be avoided. All could result in the organisation being "whistle-blown" to the National Criminal Intelligence Bureau under the Proceeds of Crime Act. In practice, some are very difficult to avoid.

We have all needed some relatively minor repairs made to our community building, for which we rather than our landlord are responsible. We have policies in place which oblige us

- ❖ To get three quotations for such work
- ❖ To pay by cheque,
 - After the work had been completed to our satisfaction
 - Upon presentation of a proper invoice

Try as we might, we just can't get three trades-people/companies to give us a quote, and both the two that do will only take on the job if we agree to pay cash. What do we do? In the end, we agree, reluctantly, to pay cash, and get the person doing the job to sign for the money. We know, or suspect, that the tradesperson is evading both the tax man and the VAT man.

We have a major function on in our hall which will be very profitable for our Centre. We had great difficulty in finding anybody to do the hall-sitting, since all of our management committee and other volunteers are otherwise engaged, but in the end, one of our regular hall sitters agreed to do the job, through the books, as usual. Unfortunately, they are taken ill at the last minute, and we are stuck. In the end we find somebody we trust to do the job, paying them £25 off the books (from the takings) as a sweetener. We aren't too worried, because we've heard on the grape-vine that the tax man will turn a blind eye to such payments, providing the amounts are small and the number of incidents per year is less than a hand-full.

Linked to this last situation is the vexed question of expenses paid and benefits in kind provided to volunteers, which is discussed in detail later. If, for example, we do find one of our volunteers prepared to hall sit, and slip them £5 at the end of the evening "to cover their expenses", we have in effect paid them (and below the minimum wage). If, however, they go home in a taxi (because it is late, and there aren't any buses running) and we reimburse them for the taxi fare when we next see them that is all right.

If the practice of paying volunteers unaccountable round sum expenses, (that is, a whole number of £, without evidence of expense or purchase) or providing them more than occasional free use of your computers, or giving them discounts on hall hire, is rife in your organisation, the difficulty is in stopping it: but stop it you must!

Apart from unaccountable round sum expenses paid to volunteers, a big issue for many voluntary organisations is the abuse of self-employment status. Let's look at a couple of examples, to illustrate.

We expanded the activities in our community building over the years, and the bookkeeping became too much for either the treasurer or the warden (or whatever we call the person managing the community building). We decided to employ a bookkeeper part time. Some bright spark suggested that if we get a freelance bookkeeper in we can save on employer's national insurance, and avoid all the hassle and agro of holiday pay, sick pay and all that, so that is what we decide to do, and engaged a self-employed bookkeeper who came in one day a week to do the books. This lady is now a fixture. Is she (or was she ever) self-employed?

Our community building is in an area with a high refugee and asylum seeker population. We decided that we should offer ESOL classes, and managed to get a grant to fund them. We engaged a TESOL teacher who claimed to be self employed, and we paid her, by cheque, the agreed amount per session. We supplied everything she needed, and when she was ill, the classes were cancelled.

Because she was clearly good at what she did, we have always used her to teach our on-going ESOL classes. We now know that she is on the staff at the local college of further education, and suspect that she doesn't declare what we pay her to the tax man. Is she really self-employed? Why does it matter to us?

There are two issues if somebody we use to do work and treat as self employed really ought to be treated as an employee. The first is that we should have been paying the employer's national insurance contribution on what we have paid the worker, and the second is that income tax and employees national insurance should have been deducted from what we paid the worker. If the worker, believing that they are self-employed, declared what they earned when working for us on their tax return, there could still be issues, since this income should have been taxed at source and at the time, rather than paid over months after the event and if what we paid is assumed to be after tax, and not before tax (and this is what the Inland Revenue will assume), then the amount of tax (and National Insurance) paid will be too low. If the worker didn't declare the earnings, then somebody owes the tax-man the tax and national insurance on what was paid. If the worker is judged to be an employee, rather than self-employed, it is the organisation who paid the money which owes the tax man, not the employee. And, the amount owed will be calculated assuming that what was paid was after tax, not before it.

That may be the theory, you say, but we only pay £50 per session, there's only 1 session a week, and £50 a week is below the earnings threshold for tax and NI. And that is true, as far as NI goes, but it isn't the end of the story if the worker has another job, and uses up all their personal tax allowance in the other job. They then have to pay the basic rate of tax (currently 22%) on the £50, which would have been £11 had you had them on your books as an employee. However, since they weren't, but should have been, the Inland Revenue want the tax worked out by assuming that the £50 is after tax, which works out, at the basic rate, as £14.10. That's no too bad, but look what happens if there had been 2 sessions a week and you had been paying £100. This is above the threshold for tax and NI (currently £97 per week), so both employer's and employee's NI liability comes into play. If you had deducted tax and NI at source, the bill would have been £22 in tax plus a further £1.43 in NI, but since you didn't, it becomes £29.44 in tax plus a further £9.48 in NI, on top of the £100, which is getting to be a tidy sum – over 52 weeks this would be £2,024!

The reason for harping on about this is that HM Revenue and Customs (remember, they are responsible for collecting both tax and NI contributions) are concerned about three abuses they believe are rampant in the voluntary sector:-

- ❖ Cash in hand wages

- ❖ Round sum unaccountable allowances for expenses paid to volunteers
- ❖ Paying workers as self-employed who are really employees.

With regard to the last, they have let it be known that they are on the look-out for organisations in the voluntary sector they can target and prosecute “pour encourager les autres ” You don’t want to be one of the ones they pick!

A further point to watch is that somebody could move from being, legitimately, self-employed to being your employee over a number of years, if they by custom and practice always provide you with a service, without the service ever being reviewed or competed. For example, if you always got in a local self-employed jobbing builder to do small repairs and maintenance on your premises, without providing written estimates, on a charge per hour basis, you could find that the Inland Revenue rule after several years, that this person was an employee. They may well have been paying income tax and national insurance on what you paid them gross, but the inland revenue could claim that you should have paid them net, and you could find yourself with a sizeable bill for back taxes, amounting to around 1/3 of what you paid the builder! The way to avoid this is for your management committee, at least every 3 years

- ❖ To review the service offered and the price paid
- ❖ To put the requirement out to tender
- ❖ To minute the review and the outcome

If your usual self-employed person is competitive, you can reappoint them. If not, you must appoint somebody else.

Note that it is good practice to review all your contracts with suppliers at least every three years, whether or not there are self-employment implications.

13.3. Employment or Self-employment?

In the prologue to this chapter, I chose the expression “people who do work for you” deliberately, to include

- ❖ Your employees (your paid staff)
- ❖ Your volunteers
- ❖ Consultants and other self-employed people

all of whom do work for you.

What distinguishes a volunteer is that they aren’t, indeed must not be, paid.

What distinguishes an employee from a self-employee is more difficult. In legal terms,

- ❖ An employee has, or is entitled to have, a contract for service,
- ❖ A self-employed person has or is entitled to have a contract for services.

This may seem like splitting hairs, and wouldn’t matter, except that

- ❖ Employees
 - Must be paid through the PAYE and National Insurance system, to comply with the law, and as a result have income tax and national insurance contributions deducted by their employers, who also have to pay an additional national insurance contribution
 - Are also covered by employment legislation.
- ❖ The self-employed
 - Are responsible for their own income tax and national insurance contributions, and don’t attract an additional national insurance contribution
 - Aren’t covered by employment legislation

Given that PAYE and NICs, as pointed out below, are complex, and by getting all work done by the self-employed, voluntary groups could

- ❖ Avoid this complication

- ❖ Save on the additional (employer's national Insurance) contribution
 - ❖ And avoid having to comply with employment legislation
- and that the self employed
- ❖ Have more scope for tax avoidance (which is legal, it is evasion which isn't)
 - ❖ Can offset more expenses against tax
 - ❖ Can delay payment of some tax to the year end (and beyond)
- there is a case to be made for getting as much work as possible done by the self-employed.

However, self-employment has been much abused in the past both as a way of avoiding tax, and more recently by unscrupulous employers wanting to avoid meeting their legal obligations. and as a result, the regulations and definitions have been tightened.

The onus is now on employers to assume and treat everybody who receives money for work as an employee, and to deduct tax, unless the Inland Revenue agree otherwise. Employers, and that includes voluntary groups, have to pay all the back taxes due for somebody they assumed was self-employed, but who the inland revenue subsequently decided was an employee, even if all parties had acted originally in good faith. If the inland revenue think you got it wrong, they will calculate what you owe assuming that what you paid the self-employed person was after deductions. e.g. if you paid £200, they will assume the person's gross pay was £243.32, and they will require you to pay £62.12 (the income tax and employees and employers NI due on £243.32).

Note that it is possible for somebody to be both self-employed and an employee, it all depends on the nature of the contract you have with them. If you are in any doubt, assume that anybody you take on is an employee, and treat them accordingly for tax and national insurance deduction purposes, until you have clarified their status with the inland revenue.

The self-employed are generally in business to sell their specialist services to others.

- They are responsible for paying their own income tax and national insurance contributions
- They can set off some expenses against tax
- An employer's national insurance contribution isn't required

To become self-employed, a person must

- Register with HM Revenue and Customs
 - Get a self-employed tax reference
- Fill in each year an income tax self assessment form, keeping proper records of all earnings and expenses
- For each job done, pass the inland revenue's "employed or self-employed?" test

Before you agree to treat as self employed someone who does a job for you, you need to be satisfied that they can pass the Revenue's "employed or self-employed?" test, which is as follows:-

- ❖ They are employed by you if
 - They have to do the job themselves and can't hire someone else to do the job for them
 - You can tell them at any time what the job is, how to do the job and when to do it
 - They are paid by the hour, week or month, and can get overtime pay
 - They work set hours, or a given number of hours a week or month
 - They work either at your premises, or at other premises decided by you
- ❖ They are self-employed if
 - They have the final say in how they do the job
 - They risk their own money
 - They stand any losses as well as take any profits
 - They provide all their own tools and equipment, large and small

- They can hire other people to do the job for them, paying them out of their own pocket
- They have to correct unsatisfactory work in their own time and at their own expense.

If they are self employed, they should

- Before you pay them,
 - Give you an invoice
 - Give you their self-employed tax reference
 - Sign a letter of comfort
 - A letter acknowledging that in the job
 - They pass the self employment test
 - They are responsible for paying their own income tax and national insurance contributions and will advise HM Revenue and Customs accordingly
- After you pay them,
 - Give you a receipt

If you are in any doubt,

- Pay them after deducting PAYE and NI
 - Use tax code BR (Basic Rate)

If they turn out to be genuine, they can get the tax paid back from the Revenue and Customs.

13.4. Wages and Salaries

Traditionally, wages are paid weekly, at a rate per hour, and salaries monthly, at a rate per year, but for PAYE and NIC purposes the distinctions are largely academic (though they do still have significance in minimum wage and working time calculations, which see) and will be ignored.

Where employment law is concerned, there are no opt-outs or exceptions for voluntary organisations, whether charities or otherwise. They are treated in the same way and have to follow exactly the same rules as any other business employing staff.

For community organisations running community buildings wages and salaries and the other costs associated with employing people tend to be the largest cost - 2/3 of the total is not unusual. As a result, they are dealt with in some detail. Even if you contract out the work of doing the payroll (which is recommended), and can thus leave the detail to others, you still need to be aware of the principles, and the responsibility for

- Checking the identity of everybody who works for you
- Checking that they are entitled to work in the UK
- Keeping records
- Finding and paying the money

remains yours.

Wages are what you pay people who work for you, whether regularly or occasionally, whether full-time or part-time. Paying somebody a wage makes them your employee, even though they may not have contract of employment. If you pay somebody you must

- ❖ Pay them through the PAYE (Pay As You Earn) and National Insurance Scheme. That is, with income tax and National Insurance Contributions (NICs) deducted
- ❖ Pay them at least the national minimum wage (currently £5.35 an hour)
 - There are special (lower) rates for those aged between 18 and 21 (currently £4.45 an hour) and for under 18s (currently £3.30 an hour for 16 and 17 year olds)
 - There are also rules to ensure that those paid by the session or task don't lose out
 - You cannot come to an agreement with an employee to pay them less than the minimum wage, no matter how willing they may be.
- ❖ Give full-time staff at least 4 weeks holiday with pay (pro-rata for part-time staff).
 - Since this is health and safety legislation

- You have a responsibility to ensure that your staff take their holidays
- You cannot come to an arrangement with them to pay them in lieu of taking holidays, no matter how willing they may be

The rules and regulations governing working hours, minimum terms and conditions of employment and the like are many and complex, and are dealt with in outline later.

13.4.1. PAYE and NICs

PAYE is pay-as-you-earn, NICs is national insurance contributions.

You must not pay your employees “cash in hand”. That is, paying wages in cash without

- ❖ Deducting income tax and national insurance contributions
- ❖ Recording the payment properly in your Books of Account
 - Either by diverting cash received before it has been paid into the bank
 - Or by disguising it as something else – expenses, for example

You must pay all your employees through the PAYE system, that is, after deducting income tax and national insurance contributions, which you must, whether you pay staff weekly or monthly, send monthly (quarterly for small employers) by a due date (always the 19th of the following month (22nd for those paying electronically)) to HM Revenue and Customs, together with any additional employer’s national insurance contributions, putting all transactions through your books of account.

The subject of PAYE and NICs is complex, especially where employees

- ❖ Work irregular patterns of hours
- ❖ Have more than one job
- ❖ Are students working during their vacations
- ❖ Get working families tax credits or disabled person’s tax credits
- ❖ Are entitled to receive statutory sick pay, statutory maternity/paternity pay or statutory adoption pay
- ❖ Suffer attachments of earnings
- ❖ Are repaying student loans
- ❖ Are reimbursed their expenses through the payroll

Accordingly, the general advice to voluntary and community organisations employing staff is to out-source your payroll to a payroll bureau. Commercial payroll bureau are in the business of calculating PAYE and NI, for a fee, typically £5.00 per pay slip, which works out at £60 to £70 a year per employee paid monthly. Accordingly, it is not usually cost-effective for a small organisation to train its staff up to do PAYE and keep them up to date with the annual changes.

Although there are affordable computer programs available which will calculate all the deductions and produce the returns required by the Revenue and Customs, these provide maximum benefit only when being operated by people who understand the rules and have at least basic IT skills. Unless you have this knowledge and experience, or are prepared to put in the time to learn them, they are best avoided. The difficulty isn’t when the answers come out as you expect, but when, as they will, they don’t. If you do go down the payroll software route, you must also buy into the maintenance and update options, since the PAYE rules change at least once a year, as a result of the national budget.

For community associations, there are issues around paying staff weekly in cash rather than monthly by cheque/BACS. (BACS is the system used by banks and businesses to send and receive payments, including wages, electronically). For historical reasons, and because of a desire to support local communities and employ locals, many community associations still pay wages weekly, and in cash, opting not to insist that all staff have bank accounts and are paid monthly. This may appear to be convenient for staff, but is expensive for the organisation, since it requires at least 4 times as much time and effort, and that is without taking into account the extra effort needed to make up cash wage packets and the security head-aches of having all that cash around.

The rules and regulations regarding PAYE and National Insurance are set out in the employer's annual pack, which is sent to you (these days on a CD, rather than on paper) when you first register as an employer, and every year thereafter.

If you are already employing people, or you are going to employ people in the near future, and have not registered, you should do so as soon as possible by telephoning the new employer's help line 0845 60 70 143, requesting your employer's pack. Revenue and Customs also have a very detailed web site at www.hmrc.gov.uk/employers setting out all the rules and regulations. You must still register and get your employer's pack even if you follow the recommendation and put the work out to a payroll bureau. You will also need to tell the Revenue and Customs who your payroll bureau (the Revenue and Customs calls them "payroll agents") is. At least it will enable you to understand

- ❖ What it is that you are paying the payroll bureau to do on your behalf
- ❖ What your obligations are, in terms of what payments have to be made and what information has to be sent to Revenue and Customs, and when

13.4.2. Taking somebody on as an employee

You can only legally employ someone who has the right to work in the UK. It is you, as an employer, who has to decide that

- They are who they say they are
- They are allowed to take paid employment in the UK

In the recent past, right to work checks were only routinely applied to prospective and new employees about whom there might be some concern. However, such potentially discriminatory practice is no longer permitted, and all current and future employees should be asked to provide evidence of their right to work, starting with written evidence of their National Insurance Number (NINO) in the form of

- ❖ P45
- ❖ P60
- ❖ A National Insurance Number Card
- ❖ A document from a Government agency, such as the Inland Revenue, Department for Work and Pensions, Jobcentre Plus, Employment Service, Training and Employment Agency (Northern Ireland), or the Northern Ireland Social Security Agency)
- ❖ A pay slip from a previous employer.

together with

- ❖ A full birth certificate issued in the United Kingdom, which includes the name or names of the holder's parents
- ❖ A birth certificate issued in the Channel Islands, the Isle of Man or Ireland
- ❖ A certificate of registration or naturalisation stating that the holder is a British citizen
- ❖ A letter issued by the Home Office to the holder which indicates that the person named in it can stay indefinitely in the United Kingdom, or has no time limit on their stay
- ❖ An Immigration Status Document issued by the Home Office to the holder with an endorsement indicating that the person named in it can stay indefinitely in the United Kingdom or has no time limit on their stay
- ❖ A letter issued by the Home Office to the holder which indicates that the person name in it can stay in the United Kingdom, and this allows them to do the type of work you are offering
- ❖ An Immigration Status Document issued by the Home Office to the holder with an endorsement indicating that the person named in it can stay in the United Kingdom, and this allows them to do the type of work you are offering

If they cannot provide written evidence of a permanent NINO, rather than a temporary one (i.e. a NINO beginning with TN, or ending with a letter between E and Z), then you need to see

either

- ❖ A passport showing that the holder is a British citizen
- ❖ A passport showing that the holder has a right of abode in the UK
- ❖ A national passport or national identity card showing that the holder is a national of a European Economic Area (EEA) country or Switzerland
- ❖ A residence permit issued to a national from a European Economic Area (EEA) country or Switzerland
- ❖ A passport or other document issued by the Home Office which has an endorsement stating that the holder has a current right of residence in the United Kingdom as the family member of a national from a European Economic Area (EEA) country or Switzerland who is resident in the United Kingdom
- ❖ A passport or other travel document endorsed to show that the holder is exempt from immigration control, can stay indefinitely in the United Kingdom, or has no time limit on their stay
- ❖ A passport or other travel document endorsed to show that the holder can stay in the United Kingdom - and that this endorsement allows the holder to do the type of work you are offering provided it does not require a work permit
- ❖ An Application Registration Card issued by the Home Office to an asylum seeker stating that the holder is permitted to take up employment

or

- ❖ A work permit or other approval to take employment that has been issued by Work Permits UK

Together with

- ❖ A passport or other travel document endorsed to show that the holder is able to stay in the United Kingdom and can take the work permit employment in question
- ❖ A document issued by the Home Office to the holder confirming that the person named in it is able to stay in the United Kingdom and can take the work permit employment in question

All documents provided must be originals - photocopies, printouts or other copies are not acceptable.

It is your responsibility to look carefully at the documents and ensure that they are genuine:-

- ❖ Photographs - does the person look like the photographs on their documents?
- ❖ Dates of birth - are the dates consistent with the appearance of the candidate?
- ❖ Expiry dates - all the documents will have an expiry date - are they still valid?
- ❖ Stamps and endorsements - do the passport stamps allow your potential employee to do the type of work you are offering?
- ❖ Names - is the same name used on all the documents?

You must then make a copy of the documents you used to verify your workers' right to work

- ❖ By photocopying the documents
- ❖ By scanning the documents into your computer using only WORM software

and store the copies securely with your personnel records.

If your new worker comes from one of the following countries

- ❖ Czech Republic
- ❖ Estonia
- ❖ Hungary
- ❖ Latvia
- ❖ Lithuania
- ❖ Poland
- ❖ Slovakia
- ❖ Slovenia

they also need to register with the Worker Registration Scheme.

Once you are satisfied that they are entitled to work, and have retained a copy of the documents used to verify this, the Form P45 they should have received from their previous employer shows

- ❖ their earnings in the tax year to date
- ❖ their PAYE code
- ❖ their National Insurance Number.

Once you have extracted this information you

- ❖ Fill in Part 3 of the P45 and send it to the Inland revenue
- ❖ keep Part 2 of the P45 for 3 years
- ❖ return Part 1A to the employee (if they give it to you)

If a new employee can't provide a P45, because

- ❖ They have lost or mislaid it
- ❖ They haven't worked before
- ❖ They have been unemployed for some time and haven't "signed on" (registered at the Job Centre in order to claim unemployment benefit)
 - Job Centres normally provide P45s for those who have signed on
- ❖ They will be working for you whilst still working for somebody else
 - the commonest reason
- ❖ They were self-employed

you get them to fill in Form P46 (which you can obtain from HM Revenue and Customs following the instructions in your employer's pack).

Form P46 provides tick box answers, as follows, to 3 statements:

- A. This is my first regular job since leaving full-time education. I have not claimed Jobseekers Allowance, or income support paid because of unemployment since then
- B. This is my only or main job
- C. I receive a pension as well as the income from this job

If this isn't the person's only or main job, they won't be able to tick any of the boxes, or sign the form.

What to do with the forms in all circumstances is set out in the employer's pack.

13.4.3. When an Employee Leaves

When an employee leaves you should complete a Form P45, send part 1 to the Inspector of Taxes, and give parts 2 and 3 to the employee. The details to be included on the P45 are the total pay and tax deducted to date, the tax code, the date of leaving, and the week or month no. in which the employee was last paid. Amend your permanent record and update your P11. These steps will help you to complete your end of year returns.

13.4.4. Students

A common area of confusion is when employing students (a student being anyone over 16 in full time education). If you employ students during their vacations (that is, the Christmas, Easter and summer holidays), you do not need to deduct income tax or make employer's national insurance contributions (though they may still be liable to pay an employees National Insurance Contribution). In order to do this, they need to sign Revenue and Customs form P38(S). However, if you employ them during term time, then the normal rules apply, and they are liable to PAYE and NI, and you are liable to pay employer's NI, in the same way and at the same rate as any other of your employees.

13.4.5. The PAYE and NIC Basics

During the tax year (6th April one year to 5th April the next year) you (or your payroll bureau) must

- ❖ Deduct the correct amount of PAYE from your employees pay
- ❖ Work out the correct amount of NICs you and your employees have to pay
- ❖ Keep a record of your employees pay, and PAYE and NICs due
- ❖ Make monthly payments of the total PAYE and NICs due to the Accounts Office

The Revenue and Customs expect you to use a Deductions Working Sheet, Form P11, [figure 34](#), one for each employee, on which you work out and record their pay, and the PAYE and NICs due. You can use substitutes,

provided the same information is recorded. P11s are divided into two sections, one dealing with NICs and the other with PAYE.

When you “sign on” as an employer, in addition to the Form P11s. HM Revenue and Customs also provide a booklet, Form P30BC, of monthly payslips, Form P30B, which you must fill in each month and post, to be received by a due date (always the 19th. of the month (22nd, of the month for electronic payments)) to the Accounts Office with your payment of all the PAYE and NICs you have collected in the previous month, and SAEs in which to do this. If there are no PAYE and NICs due, you still have to make a nil return (that is, send in a P30B with “NIL” in the Amount Due box). (Very small employers can arrange to make payments quarterly).

They also provide Form P32 on which you keep a record of all the payments made. Note that the Collector of Taxes has the right of access to all your records of PAYE and NICs deducted and made.

At the end of the tax year, always 5th April, you (or your payroll bureau) will need to obtain and fill in the following forms:-

P14 – End of Year Summary – one for each employee – a 3 part form

P35 – Employer’s Annual Return

P60 – Employee’s certificate of Pay, Income Tax and NICs – one for each employee. In practice, Part 3 of Form P14

You need to return the completed P35 and Parts 1 and 2 of the P14s to the Revenue and Customs by 19th May, and to distribute the P60s to your employees by 31st May.

Tax and national insurance rates and thresholds and limits are set each year in the Chancellor of the Exchequer’s budget. As a result, they tend to change annually. The rates for each year will be set out on the employer’s CD, and on CASH’s web site (www.cash-online.org.uk), where PAYE and NI are also discussed in detail and in depth.

13.4.6. Gross and net wages

For someone earning more than the earnings threshold (and that will be the majority), their take home pay, or net wages, will be their gross pay (their salary, or their hourly rate multiplied by the hours they have worked) less their PAYE and their NI contributions. These are called their deductions. What you, as their employer pay to HM Revenue and Customs each month is their deductions plus your NI contributions. So, before taking account of any pensions contributions, what it costs you to employ somebody is their take-home pay plus their PAYE and NI contributions plus your NI contribution, as their employer.

Remember, they pay the PAYE and one NI contribution (the employees share) and you pay the other NI contribution (the employer’s NI share). This does not come out of your employees wages, it is on top of it.

13.4.7. PAYE (Pay As You Earn)

Income tax is payable on total earnings in the tax year (6th April to 5th April). A calculator for working out PAYE deductions is on the CD in the employer’s pack. The tax to be deducted depends not only on this week’s or month’s gross wages but also on

- ❖ Wages paid to date
 - In this job this year
 - In previous jobs this year
- ❖ Their tax (PAYE) code

Tax codes are issued to employers by the Revenue and Customs on Form P6T, and to employees on Form P2X(T) – PAYE Coding Notice. The tax codes take into account

- ❖ Not only the personal allowances to which an individual is entitled
- ❖ But also
 - What they have earned,

- Are earning
- Or will earn

in other jobs this year (if your job isn't the employee's only job).

- ❖ Any taxable expenses or benefits in kind they receive
- ❖ What other taxable income (from savings or investments, for example) they have.

An employee who has more than one job will have a different PAYE code, and pay a different percentage in tax, in each job.

Note that an employer can only use a PAYE code that has either been taken from a P45 (for new employees) or was notified on Form P2X(T). They must ignore coding notices and any other official correspondence referring to a PAYE code sent to their employees. What the PAYE codes mean and how they are worked out is set out in Revenue and Customs leaflet P3, which is sent to employees with their PAYE Coding Notice. Full details of the PAYE scheme from an employee's point of view are given on the HM Revenue and Customs web site at:- http://www.hmrc.gov.uk/pensioners/tax_codes_index.htm

All this seems straight-forward enough, especially now that there are calculators on the employer's CD, so what is the problem with doing it yourself? Well, not only are you required to act as an (unpaid) tax collector, you also have to act as an (unpaid) benefits agent, and deal not only with PAYE and NI (both in themselves complicated enough), but also Working Tax Credits, Statutory Sick Pay, Statutory Maternity, Paternity and Adoption Pay, and Attachment of Earnings Orders and Student Loan Repayments. All are governed by rules and regulations which make the rest of PAYE look simple, so unless your finance worker is already an expert, or you are prepared to pay for them to become expert, and to keep up-to-date, you are strongly advised to go down the payroll bureau route.

13.4.8. National Insurance

In theory, national Insurance contributions pay pensions and benefits.

- If you don't pay national insurance contributions you won't get a pension.

The registered unemployed, the long term sick and disabled and people earning less than the earnings threshold but more than the lower earnings limit have contributions paid for them. In practice, National Insurance is both an additional tax on earnings, and a tax on employment.

Every worker should have a NINO – a national insurance number. This will be

- On their P45,
- On letters they have received from the Revenue and Customs
 - The Revenue and Customs use your national insurance number to identify you
- On their NINO card
 - National Insurance Numbers are usually allocated to people on or around their 16th birthday
 - By law, everyone who is
 - Over 16
 - Resident in the UK
 - In paid work
 - Claiming benefit

must have a National Insurance Number

If they don't have one because

- they haven't worked in the UK before,
- and you are satisfied that they are allowed to work,

they need to get one from the Department for Work and Pensions (their nearest Job Centre Plus, Job Centre or Social Security Office).

If they have one but have lost or forgotten it, you need to get the Revenue and Customs to trace it

- Use Revenue and Customs form CA6855

National insurance contributions due are worked out separately for each job, based on wages in the job.

- Each worker pays a %, currently 11%, of their wages, in addition to any tax due, on all wages above the Earnings Threshold (currently £420 a month)
 - On earnings between the Lower Earnings Limit (currently £364 a month) and the Earnings Threshold, earnings count towards pensions and benefits, though no contribution is payable
 - Below the Lower Earnings Limit, earnings don't count towards pensions and benefits
- In addition, for each worker earning more than the Earnings Threshold, an employer has to pay a % (currently 12.8%) of their wages (on top of their wages, that is, not deducted from their wages) as an additional national insurance contribution

A calculator for working out NI contributions, both the employee's contribution which is deducted from their wages, and the employer's contribution, which is additional, is on the CD in the employer's pack.

13.4.9. Paying people "free of tax and NI"

Some "smart alecs" will tell you that they don't pay tax and NI, yet they are earning a good wage and are on an employer's books. Are they lying? Not exactly. What this means is that they have come to an agreement with their employer to be paid "free of tax and NI".

When you take on a paid worker, you usually negotiate their wages or salary gross, that is, before deducting PAYE and NI. However, what their take-home pay will be will depend on their circumstances and what other taxable income they get. If they are hourly paid and they work irregular hours their take home pay will vary from pay day to pay day, in part because they earn different amounts in each pay period, but in part because the tax and NI they pay isn't fixed, being re-calculated for each pay period.

Some people don't like this constant varying in their take home pay and come to an agreement with their employer that the wage or salary for their post will be set net, that is after PAYE and NI. HM Revenue and Customs calls such arrangements paying "Free of Tax and NI", FOT for short. The name is a misnomer. PAYE and NI is still being paid, but by the employer. If you enter into such an arrangement with an employee that all of his or her earnings are to be paid 'free of tax', you should note that

- ❖ It is your responsibility to make sure that your employee understands and agrees with the terms under which the payment is made "free of tax"
- ❖ Payments made "free of tax" can increase your costs
- ❖ There are extra PAYE duties involved. For example, the tax due is worked out by reference to the 'true gross pay', not the amount your employee is actually paid. It is your responsibility to work out the 'true gross pay' figure

Where you have such an arrangement with any employee(s), contact your local Revenue and Customs office to obtain a package containing

- ❖ Forms P11 (*FOT*)
- ❖ Special 'free of tax' (*FOT*) Tax Tables, *Tables G*
- ❖ A leaflet *FOT1* which will help you work out the 'true gross pay' figure and show you how to complete form P11 (*FOT*).

My recommendation is that you avoid free of tax arrangements like the plague. HM Revenue and Customs bland statement that "payments made "free of tax" can increase your costs" is the tip of an iceberg.

Note that, the more somebody is paid, and the higher their tax code, the more beneficial it is to them to be paid "Free of Tax", and the more expensive it is for you. In addition, unless all your employees are in similar circumstances, and have similar tax codes, it is both inequitable and divisive, because you are in effect paying people different rates for the same job.

13.4.10. Is There No Escape From This Bureaucracy?

The only way you can pay somebody

- ❖ Without having to deduct PAYE and NICs
- ❖ Without having to pay an employer's NIC contribution
- ❖ Without having to fill in a P11 and make monthly returns to HM Revenue and Customs

is if

- ❖ You pay them less than the earnings threshold (currently £84) per week
 - Which works out at under 16 hours per week at the current minimum wage (currently £5.35 a week),
- ❖ This is their only job

You will still need to record

- ❖ Their names,
- ❖ Their addresses
- ❖ How much they were paid

and will have to return a P14 at the year end.

The disadvantage to the employee is that their work isn't given any credit for National Insurance purposes.

If you pay your employee

- ❖ More than £84 per week
- ❖ Less than £97 per week,
 - equivalent to just over 18 hours per week at the current minimum wage
- ❖ You won't have to deduct tax or national insurance, or pay an employer's contribution,
- ❖ You will have to
 - Record what you paid and who you paid it to on Form P11
 - Make monthly nil returns to the Revenue and Customs

The advantage to your employee is that their work is given credit for National Insurance purposes.

Note that:-

1. Any kind of paid work can jeopardise an individual's right to claim benefits, and they may find that their payments are docked or suspended
2. It isn't strictly your responsibility to take into account the effect of what they earn on any benefits to which your employees are entitled, it is down to your employees to do this
3. HM Revenue and Customs and the Benefits Agency regularly exchange information, with a view to preventing fraud

13.4.11. Permitted Work

There were in the past rules whereby the long term sick and disabled could supplement their benefits by taking what was called "therapeutic work". These therapeutic work rules have been replaced by permitted work rules, which apply to people getting a Severe Disablement Allowance (SDA). There are 3 situations where someone can get a SDA and do some permitted work, the third especially being relevant to the community sector:-

1. They can work and earn up to £20.00 a week for as long as they are getting SDA.
2. They can work for less than 16 hours a week (on average) and earn up to £86.00 a week for up to 26 weeks. This can be extended for another 26 weeks if the Department for Work and Pensions agrees that an extension will help them towards work of 16 hours or more a week. After their first attempt at a fixed period of permitted work, if they cannot move into work of 16 hours or more a week, they can try again after a gap of 52 weeks. These subsequent attempts at permitted work will last for 52 weeks, and must be supported by the Department for Work and Pensions. During any gap period they can still work and earn up to £20.00 a week.

3. They can work for an unlimited period and earn up to £86.00 a week if they are doing work which is supervised by someone who is employed by a public or local authority, or a voluntary organisation, and it is their job to arrange work for sick and disabled people. This could be work done in the community or in a sheltered workshop. Similarly, if you are doing work under medical supervision as part of a hospital treatment programme, either as an in-patient or a regular out-patient of a hospital or institution, you will be able to work without a time limit.

13.5. Employees' Expenses

Employees' expenses, whether paid direct or reimbursed, and any benefits in kind are, in principle, counted as part of wages, and, for employees earning £8,500 a year or more (inclusive of expenses and benefits in kind)

- ❖ Should be declared
- ❖ Should have PAYE and NICs deducted

Some types of expenses and benefits in kind are not taxable, and tax suffered on them can be recovered

- ❖ Either as a refund from the inland revenue
- ❖ Or, more usually, by an adjustment to an employees tax code.

In practice, the need to submit detailed records, and to deduct tax and NICs, can be avoided by obtaining a dispensation from the Revenue and Customs. Before you can obtain a dispensation, you will need a written procedure covering payment of employees expenses and provision of benefits in kind, setting out how claims are vetted and authorised. Once the Revenue and Customs are happy with this, and that you will stick to the rules, you should be granted a dispensation.

You apply for a dispensation by filling in Form P11DX - **How to cut down on your paperwork: dispensations**, attaching a copy of your procedure. A copy Booklet 480, Expenses and Benefits – A tax guide - giving full details of what is and isn't taxable, is on the employer's CD.

Note that:-

- ❖ Reimbursement of purchases by your employees which are for the use of your group doesn't count as expenses
- ❖ If you allow employees to use your offices and equipment – personal computers, for example - for their own use, this is a benefit in kind
 - Occasional/limited use is permitted without being counted as a benefit
- ❖ You will not be given a dispensation
 - If you pay round sum allowances
 - If the person claiming is also the person who authorises the claim

Round sum allowances are where fixed amounts are paid to employees to cover an expense which

- ❖ Aren't the true cost of the expense
- ❖ Aren't accountable. That is, where receipts are not required

For community organisations, expenses are usually for travel and subsistence. That is,

- ❖ For the use of private motor vehicles on the group's business
- ❖ For bus, rail and tube fares
- ❖ For meals
- ❖ For hotel bills

Which instances of travel and subsistence can be reimbursed tax free, and which cannot, are complex, the rules being set out, illustrated with examples, in HM Revenue & Customs Booklet 490 - Employee Travel – A Tax and NICs Guide for Employers, a copy of which is on the employer's CD.

Basically, you can reimburse reasonable actual travel and subsistence expenses,

- ❖ But not from home to work, and vice versa.
- ❖ Calling in to see a client on your way to work or on your way home isn't reimbursable
- ❖ You can pay bus, train and tube fares
- ❖ You can pay for meals taken on the journey, including refreshments (tea, coffee, soft drinks)
- ❖ You can pay hotel bills, including
 - Cost of accommodation
 - Cost of meals
 - Cost of refreshments, non-alcoholic and alcoholic
- ❖ If an overnight stay is involved, you can pay an allowance of a maximum of £5 for personal incidental expenses
- ❖ You can reimburse employees who use their private motor cars, motor-cycles or pedal cycles on your group's behalf, without having to declare it and deduct tax, if you pay no more than the current Revenue and Customs rates.

Expenses should only be reimbursed

- ❖ Against a completed and authorised expense claim
- ❖ When supported in full by receipts, or other evidence that the expense was actually incurred

If you do not obtain a dispensation, and yet you pay expenses and/or provide benefits in kind, at the end of the tax year you will have to obtain from Revenue and Customs and fill in forms

- ❖ P9D – Expenses and Benefits from Which Tax Cannot be Deducted
- ❖ P11D – Expenses and Benefits
- ❖ P11D(b) – Return of Class 1A National Insurance Contributions

and return them to Revenue and Customs by 6th July, with copies to each employee affected.

13.6. Volunteers' Expenses

Volunteers includes not only your voluntary workers but also your management committee and trustees. Claims for reimbursement of the cost of purchases made by volunteers on behalf of an organisation (for example, the treasurer using her personal credit card to buy computer equipment over the internet, or a volunteer buying milk and biscuits for the playgroup) often treated as if they were expenses, are strictly outside the scope of this section. Such reimbursements, always of the exact amount spend, as evidenced by a receipt, should be made promptly. For large items, the volunteer should have been authorised in writing in advance to make the purchase on behalf of the organisation.

13.6.1. Why reimburse?

It's not unknown for managers of organisations to query why they should reimburse expenses. Some volunteers too might feel that they shouldn't take money from a charity. The reimbursement of expenses is an equal opportunities issue. The cost of travelling and a meal eaten out is significant to someone on benefits or a low income. Any organisation serious about involving a diverse range of volunteers should reimburse expenses. Volunteer expenses should be built into any funding application. It's worth remembering too that volunteers are making a gift of their time – one that has substantial monetary value. They should not be expected to give up money as well.

13.6.2. Do's and Don'ts

By and large, what you can and can't pay in expenses to volunteers is much the same as for paid staff, with the addition of

- ❖ Travel to and from home - employees can't claim for commuting
- ❖ Child care - employees can only claim for an onsite crèche or nursery

Since you are going to have to write a procedure covering payment of expenses to your employees to get a dispensation from Revenue and Customs, you are strongly advised to include expenses payments to your volunteers in this procedure.

Do, on a reasonable actual basis, pay or reimburse volunteers for

- ❖ Provision of refreshments (meals, tea or coffee) while undertaking voluntary work
- ❖ Postage and telephone costs, if working from home
- ❖ Provision of a crèche, and reimbursement of some child care costs - if they have had to make special provision, say to attend a management committee meeting, AGM, or to do a task for you
- ❖ Protective clothing or other essential equipment or work materials
- ❖ Training solely or mainly provided for improving the voluntary worker's ability to do the work
- ❖ Travel
 - To and from the place of voluntary work
 - Undertaken in the course of voluntary work, including
 - Subsistence i.e. hotel bills and refreshments when travelling
 - Bus, tube and train fares
 - Motor and cycle expenses at the current Revenue and Customs rates.

A reasonable actual basis means that

- ❖ The expense should be reasonable in the circumstances
 - 2nd. class rail fares, rather than 1st. class
 - Tube and bus fares, rather than taxi fares
 - (Though this depends on circumstances. It would be perfectly reasonable to pay for a taxi, for example, to take a female volunteer home in the late evening, or to take a disabled volunteer home at any time)
 - Not
 - Meals in expensive restaurants
 - An occasional exception, at Christmas, for example, is permissible
 - Rooms in 5* hotels.
- ❖ It should actually have been incurred
 - With proof of purchase – a ticket, receipt, invoice or other written evidence

Volunteers' expenses should only be paid or reimbursed

- ❖ Against a completed and authorised expense claim
- ❖ When supported in full by receipts, or other evidence that the expense was actually incurred

Don't

- ❖ Pay volunteers
 - An honorarium, as a genuine one-off "thank you" payment, is just about acceptable, provided the recipient is not a trustee. If it is expected, hinted at or regularly given it would be treated as any other taxable income, and such payments are likely to affect benefits.
 - Many community organisations prefer to show their appreciation by giving volunteers a small present, rather than pay an honorarium, but the rules about expectation, hinting and regularity still apply.
- ❖ Pay round sum allowances (£5 to £7 are figures often used) to cover expenses
 - Round sum allowances are where fixed amounts are paid to volunteers to cover an expense which
 - Aren't the true cost of the expense
 - Aren't accountable. That is, where receipts are not required
- ❖ Reimburse them for personal incidental expenses
 - i.e. pay pocket money, or a daily allowance, however small
- ❖ Provide significant benefits in kind
 - This could include

- Personal use of your computers, photocopiers and other office equipment, other than occasionally
- Training not related to the tasks the volunteer does for you
- Free or reduced rate use of facilities for which you charge e.g. hire of a hall or meeting room

If you do, your volunteers will be employees in the eyes of the HM Revenue and Customs and the Contributions Agency, with the result

- ❖ To your organisation
 - That the volunteer becomes a paid worker, entitled to the minimum wage, and 4 weeks paid holiday,
 - That your organisation becomes liable to pay both employer's NICs and employees PAYE and NICs on any back pay
- ❖ To the volunteer
 - that they become employed and liable to pay PAYE and employee's NICs, and to loose benefits

If you want to know more about what you should and shouldn't do in terms of paying volunteer their expenses and providing them with benefits in kind, see CASH's information sheet on volunteer's expenses at www.cash-online.org.uk.

13.6.3. Management Committee Members'/Trustees Expenses

Remember, your management committee members (who will be your trustees, if you are a charity), are also volunteers, and should be offered their expenses. However, if you are a charity, you need to be particularly careful when reimbursing or paying the expenses of your trustees that they aren't being left in pocket. The Charity Commissioners are particularly hot on unauthorised payments to trustees (and this includes over-generous expenses), and the annual return you have to make to them includes a question on the amount in expenses paid to trustees.

13.6.4. Volunteering and State Benefits

The rules are straight-forward, and it's well worth knowing them so that you can advise volunteers if they have any queries. All benefits rulings agree that voluntary work is work for a not-for-profit organisation, or work for someone who is not a member of your family, where only reasonable expenses are paid. It is good practice for Individuals in receipt of benefits to inform their benefits advisers if they take up voluntary work, but it is entirely up to the volunteer whether they tell their adviser or not, and you have no duty to inform the benefits office of who is volunteering for you. However, bear in mind that if someone has not informed the benefits office that they are volunteering, they may be wary of their name or photograph appearing in any publicity, so do always check first before 'outing' someone as a volunteer.

- ❖ Job Seeker's Allowance. People on JSA can do as much voluntary work as they want as long as they remain available for and are actively seeking work. This will mean that they will have to show that they are looking for work and applying for jobs where appropriate. This means that as an organisation you will have to give your volunteers some flexibility, as they will need to visit the Job Centre for meetings and to sign on, and will need to go for interviews when they come up. If an individual is volunteering, then they are entitled to 48 hours' notice if they have to attend an interview, and a week's notice before starting work. These are concessions to the 24 hour notice normally allowed.
- ❖ Income Support. Volunteering should not affect someone's Income Support as long as they are not receiving any money other than reimbursement of expenses.

- ❖ Incapacity Benefit. If your volunteer is in receipt of Incapacity Benefit then they can volunteer for as long as you they want. Occasionally there is also some confusion about volunteering and 'permitted work' The permitted work rule applies only to paid work and should not affect volunteers. Claimants should be entitled to volunteer without having to have it recognised as permitted work.
- ❖ Disability Living Allowance. DLA is an allowance paid in acknowledgement of the fact that life for someone with a disability may be more expensive – for instance, someone with mobility problems may be reliant on taxis. Volunteering will not affect whether an individual receives this benefit or not.
- ❖ Advances. The Social Security Amendment (Volunteers) Regulations 2001 clarified income support, JSA, and Incapacity Benefit rules to make it clear that volunteers can receive advances to cover future expenses. Receipts and records must be kept, and the volunteer would have to repay any money that was not spent.

13.6.5. Volunteer's Expenses, Equal Opportunities and Financial Controls

There is a conflict between what is desirable for your volunteers – prompt repayment, on the same day, in cash of expenses incurred, or even advances, if your volunteers are asylum seekers in receipt of vouchers who will have very little access to cash, so will find it difficult to pay for travel or go out and buy a sandwich – and what is desirable from a financial control viewpoint - reimbursement of expenses monthly rather than daily or weekly, and always by cheque. To avoid excluding volunteers who are on low incomes, such as asylum seekers, or those in receipt of benefits, who cannot afford to wait for the money, you will need to balance their need for prompt payment of small amounts in cash against your need for strict financial controls. Do not assume that a small amount of money for you is a small amount of money for everyone else, and recognise that many people do not have bank accounts, and in any case cheques take several days to clear. Be flexible, and if you are not sure which methods of reimbursement suit people, just ask them – in some cases it may be more efficient to develop different systems for different people.

13.6.6. Volunteer Agreements

Some community organisations, with the best of intentions, treat their volunteers as if they are paid workers, albeit without paying wages, and some insist on their volunteers signing written agreements setting out what the organisation expects of them and will do their best to turn up on time and to follow the organisation's policies and procedures and so on and so forth. However, volunteers aren't paid workers, and can't be treated as such – they must be free to come and go as they please, and if they don't feel like it, they must be able not to turn up without your applying sanctions. If you treat your volunteers as if they are workers, you risk them actually becoming your workers, with all that that entails, so if you have volunteer agreements in place, you need to make it clear that these are statements of what will happen ideally and, explicitly, that they not legally binding, and thus not a contract. In addition, you must avoid doing anything which gives a volunteer anything of value, in money or money's worth, in return for volunteering, whether this is money, gift vouchers, training unrelated to their role, or boxes of chocolates, since this could be taken as evidence of a contract of employment. Remember, there is no need for contracts to be in writing, but there is need for a "consideration", and paying expenses, in cash or in kind, over and above the strict cost incurred, is a consideration, and the lower limit is a peppercorn!

Chapter 14

14. Community Organisations and Taxation

14.1. Rates

Local Government is financed by a dual system of Council Tax, levied on domestic premises, and the uniform business rate, levied, as its name implies at uniform rate throughout England and Wales, on non-domestic premises. The 'uniform business rate' is collected by the local authority on behalf of central government and the funds go into a central pool. The money is then re-distributed to local authorities on the basis of a range of social and economic indicators.

Community buildings, even though although they are not normally businesses, are non-domestic premises, and therefore are subject to this rate. The rateable value is based on the annual rent which the building might command on the open market, and is usually much higher than a community organisation would (or could) in practice pay as rent for its community building.

14.1.1. Rates Relief

Charities receive a mandatory relief of 80% of the amount otherwise due on their premises. Whilst this relief is not in principle restricted to those charities registered with the Charity Commissioners, in practice, such registration is clear proof of eligibility.

Rating Authorities have discretion to afford further relief to charities, and to grant relief to other non-profit making voluntary organisations, such as sports clubs. As might be expected, the practice of different authorities varies. A substantial number do grant discretionary relief to community organisations, often of the whole of the remaining 20%. Local Authorities must give notice of the making or revocation of decisions to grant discretionary relief and of the making or revocation of the chargeable amount. Note that rates relief for charities and other non-profit making voluntary organisations does not extend to water rates.

In deciding whether or not to grant discretionary relief, Rating Authorities are supposed to take into account such factors as:

- ❖ The active encouragement of participation by such groups as young people, those with disabilities, from ethnic minorities, the elderly, etc
- ❖ The sort of facilities provided (for example, to help develop the skills of one or more of the above mentioned groups)
- ❖ Whether such provision directly or indirectly relieves the authority of the need to make its own

The existence of a bar run by the organisation should not be a reason for refusing - the authority should look at the main purpose of the organisation.

For more detailed Information, see Community Matters Information Sheet No. 15 Rates

14.2. Fuel & Power Supplies

Fuel and power supplies to a building used entirely for domestic purposes or for non-business charitable activities ('qualifying purposes') are liable to Value Added Tax (VAT) at 5%. If at least 60% of the building is used for a qualifying purpose, then fuel and power supplies can be rated at 5%; if less, then supplies of fuel and power may be apportioned between qualifying and non-qualifying uses with the non-qualifying portion taxed at 17.5%. Beside these instances, supplies of fuel and power below certain specified low quantities will automatically be rated at 5% whatever the use of the building.

14.2.1. The Climate Change Levy (CCL)

The Climate Change Levy is a tax imposed on the use of energy by businesses and the public sector which is added to fuel bills before VAT. Fuel oil is not subject to CCL, because it is already subject to excise duties. The rules for liability to pay this tax follow existing VAT rules, so that supplies currently charged VAT at the 5% rate

will not be charged CCL, but supplies currently charged VAT at 17.5% will be liable. Hence, the levy does not apply to energy used by registered charities for non-business purposes, supplies of fuel for domestic use are excluded, and there is an exemption for business premises where only a small amount of fuel is used.

If you think you are not eligible to pay CCL but your energy supplier is charging it, you should in the first instance contact your supplier. Your supplier should also be able to give you advice and assistance on other matters related to CCL.

14.3. Water Rates

Water rates, which include a sewerage charge are payable to your private sector water company. There is no relief - either mandatory or discretionary – for charities. You have the options of either paying a flat rate based on the rateable value of the premises, or of having your water consumption metered and paying for how much you use, though you will still have to pay a standing charge, regardless of your usage. Whether or not you will save money by having your water metered depends on how much water you will use, and its cost, and you may also have to pay for installation of the meter.

For more detailed Information, see Community Matters Information Sheet No. 66 Community Buildings and Utility Charges

14.4. Value Added Tax (VAT)

Value added tax is in principle a tax on the value you add when you do work on something i.e. you make something from raw materials. In practice, it is a tax on the difference between what you paid for something, whether goods or services, your inputs in VAT jargon, and what you charge for something, your outputs, in VAT jargon.

Organisations have to register for VAT when their annual outputs, their annual income (not profit, note, but income) in other words, exceed a threshold value, currently £61,000, which is set annually by the Chancellor of the Exchequer in his budget. However, not all outputs count towards the threshold. HM Revenue and Customs, the government body which collects VAT and enforces the VAT rules, calls the goods and services your organisation provides (your outputs) 'supplies' and designates them as 'exempt' or 'taxable'. Only taxable supplies count towards the VAT threshold. Charities are not exempt from the need to register for VAT simply by virtue of their charitable status, and community organisations are treated like any other body when it comes to considering whether they have to register and therefore separately account for VAT.

There are three rates of VAT - standard rate (currently 17.5%), some supplies of fuel and power - i.e. gas and electricity and some other items - (currently, for buildings used wholly or mainly for domestic or charitable purposes, 5%) and zero-rate (currently 0%). Note that although tax is not charged on zero-rated items their value does count towards the overall value of taxable supplies.

14.4.1. What is, and What is Not, a Taxable Supply?

To determine how much of your income is taxable in VAT terms, you need to sort out all your activities and the income they bring in into three categories:

1. Outside the scope of VAT
2. Exempt;
3. Taxable, whether at 0%, 5% or 17.5%

The following list, whilst not exhaustive, categorises the most common activities of organisations running community buildings.

14.4.2. Outside the scope of VAT

These are not included in the calculation of the organisation's taxable income.

- ❖ Voluntary services given free of charge in accordance with the objects of the charity

- ❖ Supplies made for below cost for the relief of distress: these supplies must be made at least 15 % below cost and effectively funded by the charity's own resources
- ❖ Proceeds of flag days or house to house collections
- ❖ Grants and donations, provided these don't amount to contracts or sponsorship
 - Restricted grants and restricted donations if the restrictions are detailed and onerous may be in realty contracts or sponsorship, and thus count towards the threshold
- ❖ The selling of advertising space in charity brochures to private individuals (but not to commercial organisations, and only if private advertisements make up at least 50% of the advertising)
- ❖ Dividends paid on shares owned by a charity
- ❖ Membership subscriptions to charitable and similar organisations - but only if the payment of a subscription secures for its members entitlement to nothing more than the right to receive copies of accounts of and reports on their activities, and the right to vote at general meetings

14.4.3. Exempt

Items which are exempt do not count towards the threshold (and VAT cannot be charged on exempt items nor recovered on related purchases)

- ❖ Letting out a charity-run building
- ❖ Welfare services and related goods supplied by charities when made 'otherwise than for profit': this means that if a profit is made it is used entirely for the service on which it is made and not for any other charitable purpose
- ❖ Receipt of interest by charities on funds kept in building society or bank accounts
- ❖ Some fundraising events by charities or other similar non-profit-making bodies
- ❖ Subscriptions to non-profit-making youth clubs serving mainly members who are under 21. This can also include extra fees paid for facilities directly related to the club's ordinary activities, but not entertainment, goods which are sold, food, drink and purely recreational holidays
- ❖ Lotteries and bingo (but not takings from gaming machines)
- ❖ Nurseries, crèches and playgroups which are registered under the Childminding and Day Care Regulations, 1992
- ❖ Education and training, if not carried out for profit
- ❖ Sporting and physical education services supplied by non-profit-making organisations to individuals

14.4.4. Taxable

a. Zero-rated

VAT is not chargeable on zero-rated supplies. They do, however, count towards the registration threshold and have to be accounted for after registration.

- ❖ Sales of donated goods by a charity or by any VAT-taxable body donating to a charity all the profits from the sale of donated goods (such as a charity's trading subsidiary)
- ❖ Sales of donated goods to the general public, to disabled people or to people receiving means tested benefits
- ❖ The loan of donated goods if the sale would have been zero-rated
- ❖ Publications, including books and newsletters

b. Standard-rated

- ❖ Membership subscriptions, where payment confers benefit other than those mentioned above under Non-business, such as free advice, information and the organisation of social activities. Membership fees of community associations and sections are likely to be taxable
- ❖ Admission charges, except for 'one-off' fundraising events held by a charity
- ❖ Food and drink to be consumed on the premises, and hot take-away food and drink
- ❖ Certain items of cold take-away food, e.g. ice-cream, confectionery, chocolate biscuits, alcoholic drinks, soft drinks and crisps
- ❖ Sale of posters, diaries and calendars, greetings cards

❖ The selling of advertising space to commercial organisations

If you have to register for VAT, you will not only have to charge VAT on your taxable outputs but also have to keep detailed records of purchases, and can only claim input tax for those for which you have proper tax invoices - i.e., an invoice or receipt from the supplier with its VAT number printed on it. This applies to petty cash payments as well as other purchases. The inputs and outputs of all the activities of the organisation must be accounted for, including those of the different sections you may have. As the tax and the liability to register for the tax is calculated on the total amount of taxable supplies and not the profits, it is vital that if a community organisation has sections each inform the Treasurer of all their income and expenditure and not just the net surplus or deficit. You will also be subject to inspection by Revenue and Customs officials. An important consideration is the considerable time it takes to do the extra accounting, and thus best avoided.

The good news is that, unless you have restricted grants which are so driven around with conditions that they amount to contracts, your community organisation's taxable income is unlikely to exceed the registration threshold. The bad news is that even if your organisation is not liable to register for VAT, VAT will be levied on the purchases you make for your community building, just as it is on those you make for your personal use. However, if you are a charity (whether registered or not) certain goods and services which you purchase, which otherwise would be standard-rated, can be charged to you at zero rate, including:-

- ❖ Charity advertisements – including recruitment advertising - in all media (including a web site other than the charity's). Recruitment can be for paid staff or volunteers, and advertisements no longer have to include a statement of the charity's objects
- ❖ Design and production services and other closely related services, excluding a charity's overheads for producing its own adverts
- ❖ Providing, extending or adapting bathrooms for use by disabled people in day centres and other charity premises
- ❖ Talking books and radios for blind people
- ❖ Supplies of aids for disabled people to a charity for use by disabled people
- ❖ Donations by a charity of specified medical and scientific equipment to a health authority, hospital or charitable institution that provides medical care or treatment
- ❖ Catering for meals on wheels
- ❖ Construction of some new buildings
 - The definition of a 'new building' is not always clear - particularly when part of an existing building is retained, or when the new structure is joined to an existing building and you should always get professional advice before embarking on any construction project

This zero-rating is usually dependent on the charity providing the supplier with a written declaration of its eligibility for zero rating. An example of a written declaration is set out in figure 35, (zero-rating certificate). A declaration form (zero rating certificate) must be completed and given to the supplier for all goods and services on which the charity wishes to claim relief.

There are also examples of certificates in VAT Notice **701/6 (Supplement)**.

There are also some further VAT concessions. Charities and some other non-profit-making bodies are now exempt from paying VAT on up to 15 fundraising events of any kind held in any location, within a financial year. An exempt event is defined as one which is organised and promoted primarily for the purpose of raising money. There is no restriction on the number of small-scale events of any one kind, such as coffee mornings, as long as weekly gross takings for such events do not exceed £1,000. Any fundraising event that meets the criteria for VAT exemption will automatically also qualify for exemption from income tax and corporation tax.

14.4.5. Voluntary Registration

If you aren't required to register, and provided you make at least some taxable supplies, you can opt to register voluntarily, so that you can recover the VAT on your inputs. However, given all the extra paper-work involved, this is only worth-while if the amount of the input tax that you claim is more than the output tax that you charge, for example if a significant proportion of the main goods and services which you supply for payment would be zero-rated. Remember, if you register voluntarily you will have to charge VAT on all taxable supplies, and VAT cannot be recovered on purchases related to exempt supplies.

14.5. Taxation and Trading

Community organisations which are charities are exempt from income tax, corporation tax and capital gains tax on all income applied for charitable purpose, and are not liable to pay stamp duty. Those that are not charities are subject to corporation tax on the profits from their activities, just as any commercial undertaking. However, they may be able to qualify for some reliefs

In principle, all the activities of a charitable community organisation must be charitable, so it follows logically that all their income must be applied for charitable purposes, and thus that there can be no tax liability. However, in practice matters are not so straight-forward. There are particular issues associated with trading by charities, and accordingly outlined below are the types and extent of trading that may be conducted by charitable community organisations without infringing their charitable status or incurring a tax liability.

A common misconception is that charities cannot trade, and another is that charities in receipt of grants cannot trade, neither of which is true. Although charities must always act in accordance with their constitutional powers, trading which is undertaken in the course of carrying out the objects of the charities, primary purpose trading, is quite legitimate. Additionally, charities are allowed to carry on ancillary trading, e.g. a museum selling refreshments to visitors, or a charitable training organisation providing childcare. It is in non-charitable trading, in the form of activities undertaken primarily to raise funds, where the problem lies. Where mixed trading occurs, that is where a charity's trade is partly primary-purpose or ancillary and partly non-charitable, special rules apply.

14.5.1. Primary Purpose Trading

The primary purpose of a community organisation will be defined in its constitution (if it is unincorporated) or its Memorandum and Articles (if it is a company limited by guarantee). For example, for community organisations using the Community Matters Model Constitution, primary purpose trading will include hall lettings to anyone, or any organisation, and the organising of any activity which furthers leisure or recreation, provided that it is in the interests of social welfare. No amount of primary purpose trading will affect an organisation's charitable status or cause it to incur a tax liability, as long as the profits from the trade are used solely for the charitable purposes of the association.

a. Letting out premises

Income from letting out a building is the primary source of income for many organisations, whether to other charities, to non-profit-making or profit-making organisations, or individuals, either for recreational and leisure time activities for the purposes of social welfare or for some other charitable or non-charitable purpose. Regardless of to whom the lettings are made, there will be no tax liabilities for this income. However, a distinction does need to be made between charitable and non-charitable lettings, for the purposes of complying with charity law. When making non-charitable lettings, community associations should

- ❖ Maximise their income from the letting, as there is a duty on charity trustees to maximise the assets of the association
- ❖ Only make such lettings when there is no competing demand for the space from charitable lettings

Note that

- ❖ Where a community organisation lets space to one of its own sections, this is not income to the association or a charge to the association but a movement of funds within the association
- ❖ Where a letting is to a wholly owned trading subsidiary of the association to provide a bar (or an independent social club committed to covenanting all its profits to the association), the income from the letting is also not subject to tax

b. Services supplied as part of a letting

Whether any profit from the provision of services such as catering, printing, equipment hire, etc supplied as part of a letting is treated as taxable income is likely to turn on the nature and extent of the services provided by the association. For example, where an association is letting to an organisation engaged in providing leisure and recreational activities, the additional services might be justified as an ancillary trade and, therefore, free of any tax liability. However, if the letting is to an organisation engaged in non-charitable pursuits the association may find that the additional services constitute a trading activity, the profits of which may be liable to tax depending on their magnitude. In practice, most community associations will not pay any tax on the profits from such trading because of a range of concessions and exemptions.

14.5.2. Ancillary Trading

Ancillary trading is treated in the same way as primary purpose trading by both the Charity Commission and Revenue and Customs. Ancillary trading occurs where the trade carried out is not of itself a primary purpose trade but where it is conducted in the course of the carrying out of a primary purpose activity. Much of any trading conducted by community associations is likely to fall into the category of ancillary trading. An example would be the profits of a café for people using the building, which would not matter as long as the café was used solely by people taking part in the charitable activities of the association. However, a café set up to serve people other than charitable users of the building, would be engaged in 'non-charitable trading'.

Before undertaking any ancillary trading, community associations should check that they have the powers in their constitution to do so. If they have, then they can undertake ancillary trading knowing that it will be treated in exactly the same way as primary purpose trading. This means that it will not incur a tax liability or affect an association's charitable status, providing that the proceeds are used to support the association's charitable work. If an association does not have the appropriate power to conduct an ancillary trade, but wants to, it will need to amend its constitution in consultation with the Charity Commission.

14.5.3. Mixed Trading

Mixed trading is where the trade being carried out is partly but not wholly a primary purpose trade. In the case of a mixed trade the Revenue and Customs will treat the profits as being exempt from tax as long as the turnover of the non-primary purpose element is less than £50,000 and less than 10% of the turnover of the whole trade. This is known as a de minimis allowance. If either one of these requirements is not met the whole of the profits of the trade will be subject to tax. To take the café example, if it is partly for the benefit of people using the building and partly for passers-by dropping in off the street, it would be conducting a mixed trade. If the total turnover was £15,000, as long as the turnover from sales to passers by was less than £1,500 (i.e. less than 10% of the total turnover), Revenue and Customs would disregard the profits, and no tax would be payable.

14.5.4. Non-charitable Trading for Fundraising Purposes

In principle, where a charitable community association wishes to engage in trading for fundraising purposes, it will be necessary to set up a separate non-charitable trading organisation. However, there are four important exemptions or concessions for non-charitable trading relating to:

- ❖ Lawful lotteries
- ❖ Small scale trading;
- ❖ Frequent small-scale events
- ❖ Major fundraising events

which mean that in practice a charity can undertake some limited non-charitable trading without incurring tax liabilities or jeopardising their charitable status. When assessing the extent of allowable non-charitable trading, an association should calculate the extent of any trading which might be relieved from tax under the fundraising events concessions first. The 'small scale trading' exemption can then be applied to the remaining trading which does not benefit from any of the other exemptions or concessions.

a. Lawful Lotteries

Charitable community organisations may run small lotteries incidental to an exempt entertainment, private lotteries and society lotteries (see the notes on lotteries on the Gaming Board of Great Britain's web site for the definitions of what these are and what the rules are for running these), provided the lottery profits are applied solely to the purposes of the charity.

b. Small Scale Trading

This exemption is in addition to all other exemptions for charity trading profits and applies to the profits of all trading activities, and most other incidental fundraising activities, that are not otherwise exempt from tax, where –

- ❖ All the profits of the trade are used solely for the purposes of the charity
- ❖ The trading turnover in the relevant chargeable period for tax purposes is no greater than -
 - Either £5,000;
 - Or the lesser of either £50,000 or 25 per cent of the charity's total gross incoming resources;
 - Or the charity had a reasonable expectation, at the start of that period, that the turnover would not exceed this threshold.

c. Frequent Small Scale Events

The profits from frequent small-scale events can be ignored, as long as the aggregate gross takings (that is, before expenses are deducted) of one type in one location do not exceed £1,000 in a week. This means that jumble sales and coffee mornings are not included when counting up the number of events which count towards the 15 large-scale events permitted in a year. If any of the small-scale events breaches the £1000 limit, it will become one of the 15 large-scale events. Note that the people attending the small-scale events must realise that the event is intended primarily for fundraising purposes.

d. Major Fundraising Events

The exemption for large-scale fundraising events is restricted to 15 events in a year at any one location, where the people attending the event must realise that the event is intended primarily for fundraising purposes. In addition, any event which creates a distortion of competition and places a commercial enterprise at a disadvantage will not be exempt. Location refers to the geographical area within which the fundraising activity takes place. Similar kinds of event held in different locations will not be added together for the purposes of the 15-event rule. However, where an event such as a concert is repeated on successive evenings, each performance is a separate event and counts toward the 15. Activities of a semi-regular or continuous nature such as the frequent operation of a shop or bar cannot be an event. Social events which 'incidentally make a profit' do not fall within the exemption, neither do events that form part of a social calendar for members.

To show that the main purpose of the event was to raise fund, minutes of meetings, costs, examples of publicity and other paperwork should be kept. Listed below are some of the events which would qualify:-

- ❖ Ball, dinner dance, disco or barn dance
- ❖ Performances: for example concerts, stage productions, and other events which have a paying audience
- ❖ Film showing, Fireworks displays, Exhibition - including art, history, science etc
- ❖ Fête, fair, festival, horticultural show
- ❖ Bazaar, jumble sale, car boot sale
- ❖ Sporting performance, sporting participation (including spectators), endurance participation

- ❖ Games of skill / contests / quiz
- ❖ Dinner, lunch, barbecue
- ❖ Auction, raffle, lottery

Car boot sales and events where an entrance fee is charged to people selling their own goods fall within the concession, provided the other conditions are satisfied. Joint events with other charities can be organised, but only if all the charities (including their trading subsidiaries) involved have organised, individually or collectively, less than 15 events of that type, in that location, in the year. Events arranged by a professional fundraiser/fundraisers may qualify for exemption if the association or its trading subsidiary is the principal partner and the professional fundraiser merely an agent.

A word of caution is appropriate. Although a major fundraising event may qualify for exemption and not put either the tax exempt or charitable status of a community organisation, it may still expose the assets of the organisation to considerable risk, if the event is unsuccessful. For example, large scale events such as celebrity concerts, sporting events, etc, can be valuable ways of raising funds, but face large costs and risk heavy losses if attendance is less than forecast. Running such risky events, especially where losses are incurred, would constitute a breach of trust by the charity's trustees (i.e. its management committee), leading, if the organisation is unincorporated, to the trustees being required to make good any losses from their own pockets, and charitable community organisations are strongly advised to run such events only through a separate trading company.

e. Requirement to Separate Trading Activities

Where a charitable community organisation wishes to engage in trading for fundraising which falls outside the exemptions/concessionary reliefs, it will have to set up a separate trading subsidiary or independent trading organisation. Such trading could include the regular sale of second hand goods in a charity shop (except where the goods are wholly donated), the running of a café for public use on a regular basis and, commonly, the sale of alcoholic beverages from a permanent bar on the premises. The separate trading subsidiary or independent trading organisation then gift aids its profits to the charitable community organisation, thereby avoiding corporation tax.

Many voluntary and community groups, especially sports and social clubs and community centres, rely on the profits from their bar to keep them afloat, and carefully managed bars attracting a large clientele can make substantial profits, so it is not surprising that community organisations who currently don't have licensed bars on their premises are attracted to the idea. However, they can just as easily become a poisoned chalice. At the heart of the difficulties lies in the need to separate the operation of the bar from the main activities of the community organisation, which can lead to the need to find two competent management committees, not just one, in circumstances where getting one competent management committee is problematic enough, and can ensure instant conflicts of loyalty and interest, with typically one party seeking to maximise profits and the other to minimise prices. For more information about this complex area, see Community Matters Information Sheet No. 37, Alcohol in Community Buildings.

The separation of trading activities is definitely an area where specialist knowledge and advice is vital. Community Matters can assist in this area, and it is sensible to seek their advice.

14.6. Gift Aid

Organisations or businesses that owe corporation tax on their profits can donate some or all of the profit and the tax due on it to a charity, the only requirement being that the donation or donations must come out of their UK pre-tax profits. Charities are also able to recover the basic rate tax paid by individuals on donations made under gift aid. There is no minimum or maximum amount, except that individual donors must ensure that they will pay as much income or capital gains tax during the tax year as the aided charity (or charities, if they donate to more than one) will recover. There is also no limit on the number of donations a donor can make in any year.

Individual donors are required to make a gift aid declaration covering the donation, which may be made in writing, by fax, e-mail or the internet, or orally. All declarations must include:

- ❖ The donor's name and full address including post code
- ❖ The charity's name or acronym
- ❖ A description of the donations covered by the declarations; and
- ❖ A statement that the donations are to be treated as gift aid declarations

There is no need for the declaration to be signed or dated, but the inclusion of at least a date is sensible for administration purposes. Where a declaration is made orally (including by telephone), the charity must make a written record and send a copy to the donor. The record must contain the same information as in a written declaration, and must also include:

- ❖ The date when the oral declaration was made
- ❖ The date the record is being sent to the donor; and
- ❖ A statement that the declaration will not take effect if the donor cancels it within 30 days

To claim the tax refunds, the charity must keep records identifying which donations are and which are not covered by a gift aid declaration. These must show the donations received, the link to the gift aid declaration (e.g. by a code number), and tax recovered, together with copies of the declaration itself and any correspondence relating to it, and records should be retained for six years after the end of the accounting period to which they relate. Forms for claiming repayment of the tax, and other information, are available from Revenue and Customs.

A specimen form for a gift aid declaration is set out in the appendix to Community Matters Information Sheet no.62, Community Buildings and Taxation.

14.7. Income Tax on Investments Taxed at Source

Charities fortunate enough to have money to invest, whether in a deposit account or in stocks and shares, are not liable to pay income tax on the interest received on the investment. However, the interest on many investments is taxed at source - in other words you receive the interest after the tax has been deducted. Registered charities can claim this back by writing to the Inland Revenue. Banks and building societies, will pay interest gross, that is without deducting tax, to registered charities as long as you give them your charity number. If you invest your money either in a National Savings Investment Account or with the Charities Official Investment Fund your interest will be paid without the deduction of tax.

14.8. Business Sponsorship

Community organisations may enter into sponsorship arrangements with businesses in order to raise funds. Sponsors may fund the general work of the organisation, or, more likely, a particular project. Sponsors often seek to link the name of the organisation or its project with their business, to suggest an affinity between the business and the organisation, and this has important implications for the trustees, if the organisation is a charity. In particular, the trustees must consider whether such a link is in the best interests of the charity, bearing in mind both the objects of their charity and the nature of their business, and the probable impact on the general public and other funders.

The tax treatment of payments received under sponsorship arrangements will depend on the nature of the arrangements. If the payments are not for goods or services, they will normally be treated as charitable donations, but if the community organisation agrees to provide some goods or services in return for the sponsorship payments, they may be treated as trading income. This is a complex area, and if your organisation is considering sponsorship, it is advisable to seek professional advice.

14.9. Corporation Tax Self Assessment

Although charities are generally exempt from corporation tax, HM Revenue and Customs will issue Corporation Tax Self Assessment Returns to a selection of charities each year on a random basis, to check that all of their

income is exempt. If your charitable organisation are asked to make a Return, even if all of your income is exempt and you have applied the charity's income correctly, you must still complete the Return, even if there is no tax to pay. The Return must be made by the latest of the following dates:-

- ❖ 12 months after the return period
- ❖ 12 months after the accounting date (when accounting date and return date don't match)
- ❖ 3 months after receipt of the notice to file

If you are late sending the return back, you will be charged penalties, even if there is nothing to pay.

The Return you will receive is Form CT600. This applies only to non-exempt income, and there will be very little on it you need to complete. However, to claim exemption, you need to obtain and complete a supplementary Return specifically for charities, Form CT600E. Unfortunately, even though HM Revenue and Customs will be well aware of your charitable status, they will not send you one automatically, and you will have to either order one by telephoning their order line on 0845 300 6555 and asking for CT600E, or download the pages from the HM Revenue and Customs website. When you send back the completed Returns, both CT600 and CT600E, you will need to include a copy of your charity accounts. Unless you receive a return, you don't have to send your accounts each year to HM Revenue and Customs.

If a return is received for the wrong accounting period, alter the Forms to the correct dates and complete it for that period.

If you have taxable income or gains but haven't received a return, you must inform HM Revenue and Customs. Charities have the same obligations as any other taxpayer to notify HM Revenue and Customs of any liability they may have.

Even if there is nothing to pay, charities may still receive a payment demand, and the demand should be returned to the Collector of Taxes showing amount due as "Nil".

Note:- If your charity is a trust (i.e., its governing document is a trust deed, you will be sent and need to send back different forms, and there are different return date requirements. See HM Revenue and Customs website under IR Charities for further details.

14.10. Taxation Position of Non-Charitable Not-For Profit Organisations

Not-for-profit community organisations that are not registered as charities in England and Wales are *prima facie* subject to corporation tax on the profits from their activities, just as any commercial undertaking. However, there may be some reliefs that can be agreed with Revenue and Customs.

14.10.1. Donations

Grant income and other donated income or goods do not count as trading income and so are not taxed.

14.10.2. Mutual Trading

Where the members are entitled to share the profits and they pay for goods and services from the organisation in their capacity as members, then this would be exempt from tax as mutual trading. This can apply to sports clubs and associations, where there is a bar and social club. Sales to non-members are taxable.

14.10.3. Trading Income

Trading with non-members for a club and sales of goods and services for other organisations will be subject to corporation tax. A computation has to be prepared to show the turnover, but deducting all related expenses. A fair share of the general overheads may be attributed to the trading activity and volunteer time may be included at a notional cost. The hourly rate to be used in this calculation can be obtained from Revenue and Customs.

14.10.4. Capital Gains Tax

There is no exemption from capital gains tax in a non-charitable body, although the exact position would depend on ownership and the provisions in the rules for the disposal of property in the event of a winding up.

14.10.5. Tax Effective Transfers

A non-charitable body can make transfers to a charity by means of Gift Aid, which are then allowable in its tax computation. Care should be taken that the transactions are not "linked" – in other words there should be no reciprocal arrangements and gift aid donations must be pure gifts.

It is, however, quite common to operate a structure whereby there is a trading organisation and a sister charity receiving the profits. The charity must then apply all funds for its charitable purposes.

14.10.6. Investment Income

Interest earned on bank accounts and other investment income will be subject to corporation tax.

14.11. Further Information

Community Matters Information Sheets:-

No. 15 Rates

No 37 Alcohol in Community Buildings

No. 62 Community Buildings and Taxation

No. 66 Community Buildings and Utility Charges

No. 86 Trading and Community Associations

HM Revenue and Customs VAT publications:

For detailed Information, see :-

701/1 Charities

701/58 Charity advertising and goods connected with collecting donations

317 Imports by charities free of duty and VAT

701/6 Charity funded equipment for veterinary etc uses

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700/1 Should I be registered for VAT?

[701/30 Education and vocational training](#)[706 Partial exemption](#)

CWL4 Exemption for fund-raising events held by charities and other qualifying bodies

All available for download from:-

www.hmrc.gov.uk/charities/vat-notices.htm

ISBN 1 900360 62 4 A Practical Guide to VAT for Charities and voluntary organisations , published by the Directory of Social Change

Other HM Revenue and Customs Publications:-

IR 46 - Clubs, societies and voluntary organisations

Charity Commission publication: CC35 - Trading by Charities www.charity-commission.gov.uk.

All their publications can be down-loaded from the website.

Chapter 15

15. Social Enterprises and Trading for Fundraising

The primary purpose of companies in the private sector is to trade with a view to profit. Conventional wisdom is that all the profits made in the private sector are distributed to the owners of the company – the shareholders, where the company is limited by shares, the partners if the company is a partnership, the workers, if the company is a workers cooperative. As usual, conventional wisdom is wrong. Most of the profits of private sector companies are reinvested in the business, but it is true that there are pressures on the directors to increase shareholder value by doing things to keep their share price high (since it is by buying and selling shares that the shareholders make money, rather than by taking dividends), and to get out of unprofitable activities.

Conventional wisdom also assumes that organisations, whether unincorporated associations or companies limited by guarantee, in the voluntary sector are not for profit. It is true that their motivation is service rather than profit, but if they are to survive and grow, they need to make profits, although these are called surpluses, and these surpluses should all either be reinvested in improved services or put into reserves, for the inevitable rainy day. What voluntary sector organisations are is not profit distributing. Indeed, this is usually forbidden by their governing documents.

Social enterprises are a concept rather than a legal form. What are taken to be social enterprises can vary at one extreme from charities which get all, or at least a substantial portion of their income from primary purpose trading to at the other extreme private sector companies with a social conscience or philanthropic bent. Consider the following example. Many people will view their local peripatetic music teacher, legally a sole trader, as being a social enterprise, but what is the real difference between this and the local green-grocer, also a sole trader, who aims to provide quality fruit and vegetables at affordable prices? In summary, therefore, a social enterprise is any organisation which provides goods or services in exchange for payment – it trades, in other words – but its objects are not primarily or exclusively to make profits and to distribute these profits to the owners.

When they start, all organisations, be they voluntary, private or public, need working capital. Private sector businesses usually raise this working capital either by selling shares, or borrowing the money from partners or banks. Public sector organisations usually borrow the money from central government. Voluntary sector organisations usually rely on grants for working capital, (and by begging or borrowing it from the founders and their friends and family) but these are limited in amount and availability, and grant-givers are generally risk averse, and don't like taking chances. One of the concepts behind social enterprises is that they should be able, if required, to attract investors by selling shares, with limits placed on the degree that these shareholders can control the enterprise or secure their investments against the enterprises assets.

Social enterprises are not new. There have been companies with a social conscience which by the standards of the day treated their employees well and invested heavily in the community for a couple of hundred years – the Quaker businesses of 18th and 19th centuries being a case in point, and the Co-operative Societies (of which more anon) would still claim to be such, as were the traditional mutual insurance and building societies. If they are so minded, there is nothing to stop the founders of a social enterprise registering it with Companies House as a company limited by guarantee or shares, and writing its values into its memorandum and articles, and in the past, this was in fact the norm. However, as the “carpet-baggers” who managed to bring about the de-mutualisation of many insurance and building societies discovered, there is little to stop the members of such organisations, and this includes not-for-profit and social enterprises registered with companies house as well as mutual societies registered with the Registrar of Friendly Societies (now absorbed into the Financial Services Authority), resolving to change their status from not-for-profit or social enterprise to a profit-distributing trading company, and then selling the assets for gain.

Registering such a company as a charity is one way to ensure that community assets are safeguarded, and another, though more problematic, is to write the necessary checks and balances constraining the members powers to change them into the company's memorandum and articles. (The problem is the difficulty of making such constraints water-tight in all conceivable circumstances without providing a hostage to fortune to the lawyers.) Recognising that there were issues about allowing investors to take a stake in a company without them ultimately gaining control, and about the need to constrain the directors of the company from putting community assets at risk by borrowing against their value, the government has recently created a new legal form for social enterprises called the Community Interest Company, to be regulated by and registered with the Financial Services Authority. Investment by shareholders in exchange for dividends and some degree of control is permitted, and a lock on community assets can be put in place, so these are not put at undue risk. Community Interest Companies are new and there is limited experience of how they work in practice.

Another traditional model for social enterprises is the co-operative. When people start talking about co-operatives, the models they call up in their mind are many and varied. Most are concepts, rather than legally identifiable entities. At the risk of over-simplification, the Financial Services Authority (FSA) permits only one sort of co-operative, the Bona Fide Co-operative, which operate primarily to benefit their members, to register under the Industrial and Provident Societies Acts. Who the members are is not specified, and hence there can be producer co-operatives, consumer co-operatives and workers co-operatives, to name but a few. The FSA will also permit Community Benefit Societies, which operate not only to benefit their members but also the community at large, to register as Industrial and Provident Societies. On the face of it, the Community Benefit Society model would seem to be specifically designed for community-based social enterprises, but in practice isn't yet much used, perhaps because

- ❖ Before the FSA allows Community Benefit Societies to register, it requires them to argue successfully why they shouldn't register with Companies House as companies
- ❖ Registering with the FSA rather than Companies House is a more expensive, complex and regulated route
- ❖ Compared to the Charity Commission and Companies House, dealing with the FSA is opaque rather than transparent (hardly surprising in an organisation whose primary purpose is to regulate the financial services sector)
- ❖ They can't become registered charities (they are exempt charities)
- ❖ Model Rules (constitutions) are not available, the FSA assuming that organisations wanting to register under the Industrial and Provident Societies Acts will be sponsored by a recognised body, who will provide an appropriate set of Rules

Where does all this leave a charitable unincorporated association running a community building wanting to engage in trade beyond the scope permitted by primary purpose trading? Setting aside the complex issues surrounding what to do if the trade is to run or permit a licensed bar or bars for the sale of alcohol, as the law currently stands, with setting up a separate, independent, organisation, usually a limited company, whose objects are to trade with a view to profit, and which Gift Aids its profits to the charitable unincorporated association. In principle, this is straight-forward, whether the company is limited by shares or by guarantee, but in practice, is more complex.

The Charity Commission take the view that it is inappropriate for a charity to invest money in any new trading venture, either directly, by taking a stake in the company, or indirectly by lending it money, especially at favourable rates of interest, since this involves an unacceptable degree of risk to the charity's funds. So, where does the trading company get its working capital, and how can the charity exercise control over the company, so that best serves the charity's interest and not the company's? (For those of you involved with bars in community buildings, you should now be recognising the tensions at the heart of the relationship between the traditional social club model for running bars in community buildings and the community association, with the former wanting to minimise prices to members and the latter wanting to maximise its share of the profits.)

Taking the latter first, either by ensuring that the company's guarantors are all members of the charity (though this is no guarantee – in the traditional model, social club members were members of the charity, but often march to a different drummer than the charity's management committee) or by controlling the transfer of shares, both through appropriate clauses written into the company's memorandum and articles. You'll need to go to a specialist solicitor (or to Community Matters) for this, and it will cost.

For example, assuming that all the company's founder shareholders are all committed members of the charity (even the trustees, in a private capacity), you could write into the memorandum and articles that any transfer of shares could only be made with, and to someone who had, the approval of the charity. Once the company is established, the plan is to persuade the shareholders individually and collectively to donate all their shares in the company to the charity, leaving the charity as the owners of the trading company. If the number of shares is very limited, then the monetary value of each shareholders' donation will be nominal.

Raising the working capital is more of an issue. In fact, it is the issue, especially if the charity can't (or at least shouldn't) either invest in or lend money to the company. Although there are issues about interest rates, which shouldn't be lower than could be obtained by lending the equivalent sum to a solid financial institution, the real problem is the risk of default – that is, the company being unable to repay the loan.

Companies limited by shares usually raise working capital by selling shares, but if your trading company does this, then the investors will have much more than a nominal sum locked up in the company, which they can only recover by selling their shares, and to donate their share to the charity involves a significant sacrifice. Borrowing either from financial institutions, who will almost certainly require a business plan (and possibly personal guarantees), or from the charity's supporters, looks the only course. To minimise lenders' exposure if things go wrong, the company will need to start small and expand slowly, by reinvesting its profits, thus limiting the amounts which can be drawn down by the charity. Indeed, it is essential to permit the company to retain profits as an alternative to gift aiding them to the charity by writing such a provision into its Memorandum and Articles. In any event, obliging a charity's trading company to gift aid all its profits to the charity is an almost certain guarantee that the trading company will be a continuing drain on the charity's resources rather than a contributor to them!

When starting a trading company, a cash flow forecast is crucial, It will reveal both how much money needs to be invested at the start (to buy stock, to pay for the rent of premises, and other expenses, and to pay for staff) and how long it will be before cash inflow exceeds cash outflow on a regular basis. Remember, suppliers are unlikely to offer new companies credit, and you will have to stock and staff "the shop" before you open for business. You will also need to take the long view – it takes on average 3 years for those who start small businesses to be able to start to recover their initial investment!

Chapter 16

16. External Scrutiny of End of Year Accounts

External scrutiny is the proper name for having your end of year accounts looked at by somebody outside your organisation. This is commonly, but erroneously, referred to as having your accounts audited. Erroneously, because in accountancy audit has a precise meaning, which is the detailed examination of the end of year accounts against requirements laid down by the Companies Acts and/or the Charities Acts by a fully qualified accountant licensed to audit, with the auditor's conclusion that the accounts are (or are not) "True and Fair."

For community organisations which are not limited companies, there are three types of external scrutiny:-

1. Informal audit
2. Independent Examination
3. Audit

Informal audit is only available to community organisations which are not charities. As with the accounts of such organisations, there are no legal requirements or definitions, but custom and practice generally dictates that the "auditor" be independent of the organisation, checks that the end of accounts correctly summarise the books of account and are free of serious errors and omissions. Custom and practice also dictates that the "auditor" receives no payment, though a suitable gift (e.g. a bottle of whisky) in appreciation of the work done is also customary.

Independent examination and audit are the options open to charities, though only to charities with an annual income or expenditure of less than £250,000 currently, but £500,000 from early 2007. Above that limit, there are no options, an audit (to the requirements of the Charities Act 1993) is mandatory. Below that limit, charities may still have to have their end of year accounts audited if

- ❖ This is required by their constitution
- ❖ This is a requirement imposed by funders

Additionally, the trustees may choose to have the accounts audited.

Since they have to be carried out by registered auditors, who don't come cheap, take many hours, and usually have to be paid for, audits are expensive, and should be avoided, where possible. If you are required by your constitution to have an audit, consider amending the constitution. The Charity Commissioners will usually look on this with favour, unless your constitution post-dates the 1993 Act. There are only 2 other reasons why in practice unincorporated charities below the £250,000 limit opt for audit, and these are

1. The external funders require it. In which case, argue with them, pointing out how much it costs. Often, they don't know what they mean when they talk about an audit, and will accept, once explained, independent examination
2. The trustees have had their arms twisted by dissent in their own ranks, or in the membership about their stewardship of the charity. Having an audit will do nothing towards building bridges and healing rifts

There is one set of circumstances where trustees should, indeed must, call for an audit, and this is where they suspect, or have evidence of financial malpractice, fraud or theft, be it by trustees, members of staff or volunteers.

Note that, for charitable community organisations with an annual income or expenditure of less than £10,000, there is no requirement for audit or independent examination, though it is good practice to have an independent examination.

For charitable companies, the audit threshold is also £250,000 (also to go to £500,000 from early 2007), though the requirements are primarily those of the Companies Acts 1985 and 1989. Below the £250,000 threshold, the less onerous form of scrutiny is an audit exemption report by a reporting accountant, rather than independent

examination, and the lower limit for this is £90,000, rather than £10,000 (for no very good reason, but that is English bureaucracy for you.) Whilst there are much stricter requirements, in terms of accountancy qualifications, for being a reporting accountant than for being an independent examiner, the work leading up to preparing the report itself is much less rigorous than in carrying out an independent examination and the report itself says little and implies less. Again, as for unincorporated organisations, there will be circumstances in which charitable companies with income and expenditure below the £250,000 or even the £90,000 limit will need to opt for an audit, and the circumstances are much the same.

If this wasn't already both complicated and confusing enough, there is worse to come, because friendly societies and industrial and provident societies all have their own rules and regulations about external scrutiny. These are set out by the Financial Services Authority in their on-line Handbook, at <http://www.fsa.gov.uk/Pages/handbook/>, which see. For Industrial and Provident Societies and Friendly Societies, the general rules are as follows, but there are special rules covering societies

- ❖ Which are Housing Associations
 - ❖ Being or having subsidiaries
 - ❖ Which are subject to the Insurance Accounts Directive (Miscellaneous Provisions Undertakings) Regulations 1993
 - ❖ Which take or hold deposits within the meaning of the Banking Act 1987
1. Societies with a turnover of more than £350,000 (£250,000 if the objects are charitable) or total assets of more than £1,400,000 must have a full professional audit by a qualified auditor
 2. Societies with a turnover of more than £90,000 but less than £350,000 (£250,000 if its objects are charitable) or total assets of less than £1,400,000 can opt for the less onerous audit exemption report by a qualified auditor, provided their Rules allow it and the membership have voted in favour of this option at a general meeting
 3. Below the £90,000 limit, where the Societies Rules allow it, and the membership have voted for it, no external scrutiny is required
 4. For very small societies, with an annual turn-over and assets of less than £5,000, and a membership under 500 there is the option of a lay audit, where the Rules allow for this and the members have voted for it. That is, an informal audit by 2 of the members who are not committee members or employees

Since the majority of community organisations running community buildings will fall into the independent examination required group, this will be dealt with in some depth.

Figure 36 is a table summarising the current eligibility requirements for independent examination (which will change early in 2007).

16.1. What is an Independent Examination?

Independent examination is a less onerous form of external scrutiny than an audit, providing less assurance both in terms of the depth of work required and the qualifications necessary. For example, the examiner will not be in a position to give an opinion on whether or not the accounts show a "true and fair view". An examination involves

- ❖ A review of the accounting records kept by the charity and a comparison of the accounts presented with those records.
- ❖ A review of the accounts and consideration of any unusual items or disclosures identified.

The independent examiner also has to be satisfied that the money raised and spent by the organisation is within the aims and objectives of the organisation's constitution.

The examiner will only carry out a detailed comparison of the records with the supporting paperwork where concerns or doubts have arisen during the course of the examination, and where satisfactory explanations cannot be obtained from the trustees.

16.2. What does an independent examiner do?

The majority of community organisations running community buildings are unincorporated charitable associations, and will need to have their annual accounts independently examined. What your independent examiner should do is to follow the directions of the Charity Commissioners set out in their publication CC63 - Independent Examination of Charity Accounts - Directions and Guidance Notes. There are 12 directions, eight of these apply to all accounts and four apply only when accounts are prepared on an accruals basis (i.e. under section 42(1) of the 1993 Act).

All Accounts

1. Carry out such specific procedures as are considered necessary to provide a reasonable basis on which to conclude that an examination is required under section 43(3) (of the Charities Act) and that section 43(2) (audit) (of that Act) does not apply to the charity, and where accounts are prepared under section 42(3) (of that Act), that the charity trustees may properly elect to prepare accounts under this sub-section
2. Obtain an understanding of the charity's constitution, organisation, accounting systems, activities and nature of its assets, liabilities, incoming resources and application of resources in order to plan the specific examination procedures appropriate to the circumstances of the charity
3. Record the examination procedures carried out and any matters which are important to support conclusions reached or statement provided in the examiner's report
4. Compare the accounts of the charity with the charity's accounting records in sufficient detail to provide a reasonable basis on which to decide whether the accounts are in accordance with such accounting records
 - ❖ Whilst the charity trustees are responsible for the preparation of accounts, on occasions the examiner may also prepare accounts on behalf of the trustees. The preparation of accounts will not generally impinge on independence provided the examiner ensures that the requirements of the Directions are met and avoids involvement in the management or administration of the charity
5. Review the accounting records maintained in accordance with section 41 (of the charities Act) in order to provide a reasonable basis for the identification of any material failure to maintain such records

Guidance

- ❖ The accounting records should:
 - Be up to date
 - Be readily available; and
 - Provide the basic information from which the financial position can be ascertained, not only at the year end, but also on any selected date
 - Contain:
 - Details of all money received and expended, the date, and the nature of the receipt or expenditure; and
 - Details of assets and liabilities.
6. Carry out analytical procedures to identify unusual items or disclosures in the accounts. Where concerns arise from these procedures, the examiner must seek explanation from the charity trustees. If, after following such procedures, the examiner has reason to believe that in any respect the accounts may be materially mis-stated then additional procedures, including verification of the asset, liability, incoming resource or application, must be carried out.

Accruals Accounts Only

7. Carry out such detailed procedures as the examiner considers necessary to provide a reasonable basis on which to decide whether or not the accounts comply with the requirements of the Charities (Accounts and Reports) Regulations 1995 and 2000

8. Review the accounting policies adopted and consider their conformity with fundamental accounting concepts, consistency of application and their appropriateness to the activities of the charity. The examiner must also consider and review any significant estimate or judgement that has been made in preparing the accounts
9. Enquire of the charity trustees as to material events subsequent to the year end of the accounts examined which may require adjustments or disclosure in the accounts
10. Compare the accounts to any financial references in the charity trustees' annual report (if any); identifying any major inconsistencies and consider the significance such matters will have on a proper and accurate understanding of the charity's accounts

All Accounts

11. Review and assess all conclusions drawn from the evidence obtained from the examination and consider the implications on the report to be made under The Charities (Accounts and Reports) Regulations 1995 and 2000. If the examiner has cause to make a positive statement, or to make a statement on any matter arising from the provisions of the Regulations, then the examiner must ensure so far as practicable that the report so made gives a clear explanation of the matter and of its financial effects on the accounts presented.
 - ❖ Any failure to be provided with information and explanations may seriously hamper an examination. If information and explanations requested are not provided this matter must be included in the examiner's report.
 - ❖ In the case of accounts prepared on an accruals basis any major inconsistency between the accounts and the trustees' annual report may give rise to misunderstanding. This should be brought to the attention of the charity trustees with a view to the amendment of the discrepancy. Where concerns still exist this must be stated in the examiner's report
12. Inform the Charity Commissioners in writing if, whilst acting in the capacity of the examiner of a charity, information or evidence is obtained which gives the examiner reasonable cause to believe that any one or more of the charity trustees has been responsible for deliberate or reckless misconduct in the administration of the charity

By implication, at least, the independent examination should be of not only the annual accounts but also the annual report. Where your independent examiner also prepares your annual accounts, you may not be in a position to complete your annual report until you have had sight of your annual accounts. In such circumstances, your examiner should send you a draft copy of the annual accounts, and you should approve these and send them back to the examiner, together with a copy of your annual report, for the formal independent examiner's report to be prepared. If your accounts have to be qualified (that is, shown to be wanting in some important respect), you may be able to blunt the criticism, and thus limit the damage to your organisation's reputation, by describing in your report what you are doing to put your house in order in the current year. As is covered more fully later, much of your annual report will be dealing with history, but there should be some mention of future (that is, current) plans, and it is here that you can and should respond to input from your examiner.

16.3. The Independent Examiner's Report

Following the examination, the independent examiner is required to produce a report. The specific reporting duties of the independent examiner are detailed in paragraph 7 of the 1995 Regulations, as modified by the 2000 Regulations. In the report, the examiner must state whether or not any matter has come to their attention in connection with the examination which gives reasonable cause to believe that:

- ❖ Proper accounting records have not been kept;
- ❖ The accounts do not accord with such records; or
- ❖ The accounts fail to comply with relevant Regulations.

A statement is also required as to whether or not any matter has been identified, in connection with the examination, to which attention should be drawn to enable a proper understanding of the accounts to be reached. The report should also include details of the following matters where they have become apparent:

- ❖ Material (i.e. significant) expenditure or action contrary to the trusts of the charity;

- ❖ Failure to provide information and explanations to which the examiner is entitled
- ❖ Evidence that accounts prepared on an accruals basis are materially inconsistent with the trustees' annual report.

Figure 37 illustrates the form provided by the Charity Commissioners, which incorporates the precise wording required by the Act and the Regulations.

The examiner's report must be signed by the examiner in his or her own name. Whilst the name of a partnership or company may be added, the appointment of an examiner relates to the individual rather than the partnership or company.

An unqualified report is one in which no faults are reported, whereas a qualified report is one in which faults are noted and reported. Note that an unqualified report does not mean that no faults were found, just that they weren't sufficient (large enough or occurring often enough) to require qualification. Any examiner worth his or her salt will supplement and support the formal Report with a written statement setting out their detailed findings, comments and recommendations. This "management letter" and the advice contained within it is what your group is actually paying for. Where a report has been qualified, because there are many and significant gaps in the supporting paperwork, for example, or "netting off" has occurred, or track has been lost of some income and/or expenditure, or it is impossible to distinguish restricted items from unrestricted items, the management letter is even more important, since it should point the way to avoid getting qualified reports in future years. That said, given that charities have 10 months in which to submit their accounts for the previous year, by the time the independent examiner has made their recommendations, it may be too late to put your house in order in the 2 months remaining of the current year, resulting in the almost automatic qualification of these accounts as well. This is another good reason not to leave it to the last minute before submitting your accounts for independent examination.

Carrying out an independent examination is not an exact science, and there is room for differences of judgement about what is significant, and therefore the point at which a set of accounts should be qualified. The temptation is if you have had your accounts qualified and think your examiner has marked you hard to seek a second opinion from an examiner who marks easy, and conveniently ignore the first opinion. Failure to tell the second examiner about the first examiner would itself be reason enough to get this mentioned by the second examiner, if this came to light. More usually, a group seeks a new, more lenient, examiner for this year's accounts, having had last year's accounts qualified, but a competent examiner will always ask why a group has switched, and should either contact the previous examiner or request sight of the management letter if there is any doubt about the reason. Clearly, there are legitimate reasons for changing examiners, including

- ❖ Legitimate dissatisfaction with the previous examiner (not simply you didn't like the answers or advice you were given)
- ❖ The previous examiner being unwilling to continue
- ❖ Your obtaining a better price/service
- ❖ Your finding a more competent/more experienced examiner

What you must not do is simply ignore any advice/recommendations given by your independent examiner, since this would lay you, as a trustee, open to a charge of breach of trust, by failing to take professional advice.

16.4. Selection of examiners

Whilst examiners do not have to hold a professional accountancy qualification, the trustees must appoint a person suitable for the circumstances of the charity. Experience of charity administration and accounting is desirable. Where a charity has gross assets in excess of £1,000,000, or gross income of more than £100,000, the Charity Commissioners recommend that the independent examiner should be either a qualified accountant or have similar qualifications in charity finance. Where accruals accounts are prepared, a knowledge and understanding of accountancy principles and accounting standards will be needed. From early 2007,

independent examiners examining the accounts of charities with gross incomes between £250,000 and £500,000 will require formal qualifications.

Although there is nothing to stop you, as charity trustees, from obtaining the services of a competent examiner on a voluntary basis, most of you will in practice be unable to do so, and should be prepared to pay reasonable fees to your examiner, which will be a proper charge on the assets of the charity. What is reasonable depends on the work involved, but now that you have seen what an examiner is required to do, you will realise that this can be a task of days rather than hours, especially if your accounts are a mess and all the supporting paperwork is out of order, and you expect your examiner to sort out the mess before they can start the examination. You need to put a realistic figure in your budget to cover the examiner's fees.

I'll let you into a trade secret – where they can, independent examiners overcharge their larger clients whose books are in good order so that they can undercharge their smaller clients whose books are often in a mess! Charges are often based on what the examiner thinks the group can afford, rather than on the work actually required. In other words, independent examination is treated as a variable cost, whereas it is in reality either a fixed cost, or a mixed cost, with a large fixed element.

An independent examiner is “an independent person who is reasonable believed by the charity trustees to have the requisite ability and practical experience to carry out a competent examination of the accounts”.

For an examiner to be independent that individual should have no connection with the charity trustees which might inhibit the impartial conduct of the examination. The following are considered to have a connection barring them from becoming your independent examiner.

- ❖ The charity trustees or anyone else who is closely involved in the administration of the charity;
- ❖ A major donor to or major beneficiary of the charity,
- ❖ A close relative, spouse, partner, business partner or employee of a trustee, major donor or major beneficiary

To have the requisite ability, your independent examiner must be familiar with accounting methods, but need not be a practising accountant. Bank or building society managers, local authority treasurers or retired accountants would all be suitable. The quality of evidence of ability which is required will depend upon the size and nature of the charity's transactions.

The practical experience must be relevant to the charity in question, by virtue of having:

- ❖ Had an involvement in the financial administration of a charity of a similar nature; or
- ❖ Acted successfully as an independent examiner on previous occasions for such charities
- ❖ Relevant practical experience in accountancy or commerce

Providing your independent examiner with written terms of engagement is good practice, and should prevent misunderstandings on both sides. Such written terms of engagement must recognise and not limit the examiner's statutory duties.

16.5. Getting Ready for Independent Examination (or Audit)

You can save your organisation time and trouble and minimise the size of the bill if you get all your paperwork in order and hand it all over to your independent examiner or auditor. You will need to provide the following:-

- ❖ The Analysis Books fully written up, correctly analysed, totalled and cross-cast for the whole year
- ❖ Bank reconciliation statements for each bank account clearly showing how the balance shown by the analysis book reconciles with that shown in the bank statement
- ❖ Bank Statements for each bank account for the whole year
- ❖ Bank paying-in books
- ❖ All documents relating to bank receipts and including letters from funders who pay by credit transfers
- ❖ Cheque book stubs
- ❖ Invoices/vouchers to support all banks payments in cheque number order
- ❖ The Petty Cash Analysis book fully written up, correctly analysed, totalled and cross-cast
- ❖ Written confirmation that, at the end of the year, the amount of cash in the box agrees with the balance of cash in hand shown in the Petty Cash Analysis book
- ❖ All the Petty Cash vouchers and receipts filled in order
- ❖ Salary records including a form P11 for each employee
- ❖ Records of any Statutory Sick or Maternity Pay
- ❖ Any changes to tax codes notified by the tax office
- ❖ Any P45 forms given by new employees
- ❖ A copy of the Employer's Annual Statement form P35
- ❖ A record all PAYE and NI paid to the Inland Revenue
- ❖ Any subsidiary records for sub-committees or projects that come under the group's umbrella
- ❖ An up-to-date register of fixed assets, with estimated values
- ❖ Minutes of all the committee meetings (and AGM) held during the year
- ❖ A copy of the constitution or other ruling document
- ❖ A copy of previous year's audited accounts
- ❖ A list of debtors (i.e. people who owed the group money at the end of the year), with the amounts owed
- ❖ A list of creditors (i.e. people to whom the group owed money at the end of the year) with the amounts owed
- ❖ The names of the Chairperson, Secretary and Treasurer

Note that the independent examiner or auditor has a legal right of access to this information, and the right to seek face-to-face answers to any relevant questions not only from your trustees/management committee members, whether officers, or otherwise but also from your staff, both present and former, from your volunteers and from your previous independent examiner/auditor. Failure to provide information, or access, must be declared by the examiner/auditor.

Sources of further information

1. Publications

Accounting and Reporting by Charities: Statement of Recommended Practice (SORP 2005)

Also known as SORP 2005, this is available free on the Charity Commission's web site

Example Reports and Accounts are available on the Charity Commission's web site at:-

www.charitycommission.gov.uk/investigations/sorp/sorp05exraa.asp

Other relevant guidance in the CC range:

CC61(a) Charity Accounts: The framework (2005)

CC16 Receipts and Payments Accounts Pack

CC 17 Accruals Accounts Pack

2. Contacts

The Association of Charity Independent Examiners brings together both professional accountants specialising in this field and others acting as independent examiners. Itself a registered charity, it may be of assistance to trustees looking to appoint an independent examiner.

The association may be contacted at:

Association of Charity Independent Examiners

Bentley Resource Centre

High Street

Bentley

Doncaster DN5 0AA

Tel: 01302 828338

<http://www.acie.org.uk>

Chapter 17

17. Annual Accounts and Reports

17.1. Annual Reports

Your management committee accounts and reports are primarily for internal use. Your annual accounts and report are primarily for external use by

- ❖ Your members
- ❖ Your supporters
- ❖ Your funders
- ❖ Your clients
- ❖ Your volunteers

And, if you are a charity,

- ❖ The general public
- ❖ Your regulators (the charity commission)

If your group is a charity, the annual accounts and report I'm writing about here is the one to send to the Charity Commissioners to meet the statutory requirements set out in the Charities (Accounts and Reports) Regulations 1995 and 2000 and the Charities SORP 2005 - Statement of Recommended Practice (on accounting and reporting by charities. In principle, this needn't be any different to the report presented at the AGM, or vice versa, provided the report to the AGM meets the statutory requirements. Because these requirements are complex and written around large organisations, the Charity Commissioners have made available free forms, with guidance notes, for smaller charities either to fill in or to use as templates.

The forms come in one of 2 packs – CC16 – Receipts and Payments Accounts Pack, or CC17 – Accruals Accounts Pack. CC16 can only be used by charities with an annual income or expenditure of less than £100,000 who have opted to prepare their accounts on a receipts and payments basis, and won't be considered further in this publication. If, as I'm assuming in this publication, you have an annual income or expenditure which is less than £250,000, and you keep your books of account on a receipts and payments basis, but opt to prepare your annual accounts basis, you are strongly recommended to obtain a copy of CC17 (either by ordering a paper copy from the Charity Commissioners' order line, or by down-loading the forms from the Charity Commissioner's web site at www.charitycommission.gov.uk) and fill in the forms, following the given instructions. This publication assumes that this is what you are going to do, and what is written below is based around the various forms and sections which make up CC17. You aren't obliged to use all or any of the forms in CC17, but where you choose to do your own thing, you should still use CC17 as a template, to ensure that the end result will comply with the requirements.

If you are a charitable company, you cannot use CC17 directly (though you could still use it as a template), because it isn't designed to meet the additional requirements imposed by Companies House. For these, you will need to refer to both the Charities SORP and to Companies House publication GBA3 Accounts and Accounting Reference Dates, especially Chapter 4.

To return to CC17, this comprises: the Independent Examiner's Report on the Accounts, the Trustees Annual Report, a set of completion notes for the trustees annual report, the Accruals Accounts form CC17a and a set of completion notes for the accruals accounts form CC17b. , , and .

If you follow the recommendations and use the pack, you will end up with

17.1.1. CC17a) Your Accruals Accounting Statement, comprising

- ❖ A SOFA (Statement of Financial Activities) for the year, and the previous year
- ❖ A Balance Sheet at the year end, and the previous year end, broken down into

4. Unrestricted Funds
 5. Restricted Funds
 6. Endowment Funds
- ❖ A comprehensive set of Notes to the Accounts
 - ❖ Your Accounting Policies

To remind you of what some of these terms mean:-

- ❖ A Statement of Financial Activities is a report peculiar to charities, combining elements from both an Income and Expenditure Account and a Statement of Movement of Funds, complying with the requirements of the Charity Commission's Statement of Recommended Practice: Accounting and Reporting by Charities (Current issue: 2005)
 - Its purpose is to show the source of a charity's funds and explain how they have been applied
- ❖ Unrestricted funds are those which come without strings attached, and can be spent as the managing trustees see fit
- ❖ Restricted funds are those that come with strings attached
 - They can only be spent in accordance with the wishes of the donor
 - Most grants are restricted funds
 - Street collections for a specific project will also be restricted funds
- ❖ Endowment funds are donated assets which the charity holds for its own use
 - Either permanent endowments, which cannot be converted into income
 - Or expendable endowments, which can

The Notes to the Accounts pages look, and indeed are, daunting. However, they are designed to cope with most eventualities, and most won't apply, so if they don't apply, you either don't need to fill in the form or just need to write "not applicable" in the relevant box. The Notes are also a useful reminder of the sorts of things you should be able to dig out of your books of account, and can serve as a useful health check on your book-keeping and record-keeping.

All accounts should set out what the organisation's policies are. In CC17a you have a comprehensive set already set out.

17.1.2. an Independent Examiner's Report on the Accounts

- ❖ An independent examiner's report is a report prepared by somebody with financial knowledge who is independent of your group, in accordance with the Charity Commission's free Guidance Note CC63 Independent Examination of Charity Accounts .
 - In principle, anybody with financial knowledge can be your independent examiner, and you don't have to pay them, if they will do it for free
 - In practice, however, unless you are a micro group, you should be prepared to pay an accountant
 - An independent examination is less thorough than an audit, the report stating only that no fault was found
 - You cannot choose an independent examination if your constitution requires an audit.
 - ❖ If you need an audit,
 - Because your constitution requires it
 - Or your funders require it as a condition of grant
 - Or you want the assurance that your accounts do indeed present a "true and fair view" of your financial affairs

this must be done by a fully qualified accountant who is registered with their professional body to audit limited companies.

This will cost you accordingly, which is why, if you can get away with it constitutionally and your funders will allow it, you should opt for independent examination.

17.1.3. The Trustees Annual Report, comprising

- ❖ Reference and administrative information
 - The financial year to which the report relates
 - The name, address, and registered number of your charity
 -
 - The names of all your charity's trustees, with the dates of their election or appointment
 - The names and addresses of accountants, solicitors, investment and other professional advisers, if your charity has these
- ❖ Structure, governance and management
 -
 - Details of your constitution, trust deed or memorandum and articles,
 - The details of the method used to elect or appoint trustees
 - Optionally, additional information, where relevant, about:
 - Policies and procedures adopted for the induction and training of trustees.
 - The charity's organisational structure and any wider network with which the charity works.
 - Relationship with any related parties.
 - Trustees' consideration of major risks and the system and procedures to manage them.
 - As a small charity (i.e. with an income or expenditure less than £250,000), you are not obliged to review your major risks, but it is good practice
 - Risks are discussed in detail later in this document
- ❖ Objectives and Activities
 - Summary of the objects of the charity set out in its governing document
 - Summary of the main activities in relation to these objects
 - Optionally,
 - Policy on grantmaking
 - Policy programme related investment
 - Contribution made by Volunteers
- ❖ Achievements and Performance
 - In the past, the Trustees Annual Report was treated as an incidental adjunct to the accounts, and was often written by the organisation's financial advisers. However, the Trustees Annual Report overall, and in particular the activities and achievements section, is now at least as important as the accounts. Accordingly, given its importance, which is increasing year by year, the Trustees Annual Report on Activities and Achievements is discussed in detail below.
- ❖ Financial Review
 - Brief Statement of Reserves Policy
 - The trustee's annual report should state the level of reserves on the last day of the financial year and for what future needs, opportunities, contingencies and risks for which the reserves is being held. If a charity does not hold a reserve, a statement is required in the trustee's report explaining why. It also enables trustees to consider why they

- are holding funds; where actual reserves exceed what are needed trustees will need to show how they intend to use the surplus for the charity's benefit.
- Reserves are discussed in detail later in this document.
- **Details of any funds materially in deficit**
 - If any funds are in deficit an explanation must be given of why this has occurred and what will be done to correct the situation.
 - This situation comes about because an organization, having inadequate unrestricted funds, effectively “borrows” from one restricted fund either to cover costs on another (overspent) restricted fund, or to pay for its (unrestricted) overheads. Funders are, understandably, not amused by such a situation.
- **Optionally,**
 - The charity’s principal sources of funds (including any fundraising).
 - How expenditure has supported the key objectives of the charity.
 - Investment policy and objectives including any ethical investment policy adopted.
-
- ❖ Signature and Declaration
- Signed by two trustees on behalf of all trustees

If your group is not a charity, and is unincorporated (that is, not a registered company), there are no specific legal requirements spelling out what your annual report and accounts should look like or cover. Nor are there any legal requirements covering independent examination or audit. However, it is general practice for such groups to prepare

either

- ❖ A Summary Receipts and Payments Account for the year
- ❖ A Statement of Assets and Liabilities at the year end
- ❖ A Report by the Management Committee

or

- ❖ An Income and Expenditure Account for the year
- ❖ A Balance Sheet for the year end
- ❖ A Report by the Management Committee

and to have these accounts “audited” by someone with financial knowledge independent of the group, usually for an honorarium (a nominal sum, not related to the work involved, or an equivalent gift in kind (a bottle of whisky, for example)). The first of these are prepared on a Receipts and Payments basis, and the second on an Accruals basis.

The lack of a legal straight-jacket does give one advantage over charity accounts, and that is the freedom to make the accounts and reports meaningful to readers, especially to those outside the organisation. You can, within reason,

- ❖ Present the data in the format that best suits your readers
- ❖ Breakdown the figures anyway you choose
- ❖ Summarise the results graphically, using pie charts, bar charts and the like, as appropriate

17.2. Charity’s Annual Return

If your charity has an annual turn-over of greater than £10,000, in addition to sending a copy of your formal Annual Report and Accounts to the Charity Commission, not later than 10 months after the end of your financial year, you will also have to make an annual return to them. They should send you a form to fill in automatically. If they don’t, you should request one by telephone (or download it from the Charity Commission’s web site at <http://www.charitycommission.gov.uk>). You will find that much of the information required duplicates that in your

annual report and accounts, especially the legal and administrative details. Unfortunately, they still require both, completed in full, even if you send them in together (as is usual).

Chapter 18

18. The Trustees' Annual Report on Activities and Achievements

Community organisations, especially if they are charities, often produce two annual reports, one of which they present at their Annual General Meeting (AGM) and the other they send to the Charity Commissioners with their annual accounts. Strictly, the annual report I'm writing about here is the one to send to the Charity Commissioners to meet the statutory requirements set out in the Charities (Accounts and Reports) Regulations 1995 and 2000 and the Charities SORP 2005 - Statement of Recommended Practice (on accounting and reporting by charities), but in principle, this needn't be any different to the report presented at the AGM, or vice versa, provided the report to the AGM meets the statutory requirements.

There are many reasons why community organisations end up writing 2 annual reports, but here are two:-

1. The report to the AGM consists of a series of informal reports from the officers (the chair, secretary and treasurer), the centre manager/warden and the user groups/sections on what they have been up to in the year, or how the year has gone from their point of view, the year running from last year's AGM to this year's. As a result, it isn't seen as suitable or appropriate to send to the Charity Commissioners
2. The trustees annual report is primarily the statutory accounts, with any narrative covering activities and achievements, written by the organisation's treasurer or even their accountants, being in the same terminally turgid style as the legal and administrative information, and could relate to any one of hundreds of similar community organisations anywhere in the country in any year in the past half century. Also, the year referred to is the organisation's financial year, not the year from AGM to AGM. As a result, it isn't seen as suitable or appropriate to put to the members (at best, they won't understand it, and at worst, it would bore them to death)

Provided the annual report meets the legal requirements when it comes to the presentation of the accounts, and the requirements for the legal and administrative information is included, the Charity Commissioners would far rather receive what you presented at your AGM rather than the bureaucratic bulls**t that is in your trustees annual report – at least it says something of substance!

In practice, there are two complications, neither insoluble. The first, and simplest to solve, is to collect together all the reports presented at the AGM, under a covering note signed by a management committee member on behalf of all the committee acknowledging that all the reports have been accepted by them. The second, and more difficult, is to get all those who present reports to match them to your financial year, and not to the year from AGM to AGM. The only down-side to using the AGM reports as the trustees annual report is that you trade off a uniform style and language for colour, interest and information, the risk being that you end up with a camel rather than a horse (a camel being a horse designed by a committee). In the end, it doesn't actually matter who writes the annual report, providing the end product is endorsed by all the members of the management committee.

An interesting point to note is that there is often no requirement in an organisation's governing document for the trustees' annual accounts and reports to be put to an AGM, though it is both common courtesy and good practice to do so, and also that whatever resolutions are passed at the AGM concerning the annual account and report are not usually binding on the trustees.

If you follow the recommendation made earlier to use Charity Commission publication CC17 as the template for your annual accounts and report, you will soon come across its one deficiency, and that is the lack of prominence it gives to the report on the organisation's activities and achievements. The Trustees Annual Report, is a 4 page form, yet the space set aside for the report on your activities and achievements is a bare half page, and the text requires only a **"Summary of the main achievements of the charity during the year"** The completion notes go on to suggest that you should

“include in this section a brief summary of the charity's main achievements for the year that resulted from the charitable activities undertaken. This may be a brief narrative describing the results of the charity's work or give details of the outputs achieved, for example, 'ran 150 playgroup sessions of 3 hours each reaching 89 children and 60 families'.

And that “Charity trustees **may choose** to provide more detailed information in this section about their main achievement. Such information may include:

- ❖ Qualitative and quantitative information that helps explain performance.
- ❖ A comparison of performance achieved with objectives set for:
- ❖ Charitable activities.
- ❖ Fundraising.
- ❖ Investments.
- ❖ A commentary on any factors within and outside the charity's control relevant to the achievement of its objectives.
- ❖ Details of any future plans and any other matters which the trustees believe should be brought to readers' notice.”

However, if you do only precisely “what it says on the tin” you will not satisfy any of the stake-holders who have an interest in your annual report, be they

- ❖ Your members
- ❖ Your supporters
- ❖ Your funders
- ❖ Your clients
- ❖ Your volunteers
- ❖ The general public
- ❖ The Charity Commissioners

In addition to commenting on the subjects commended in CC17's Completion Notes to the Trustees Annual Report , especially the contribution of your volunteers, a good annual report needs to do 6 things

1. To set your objectives for the year
2. To outline your plan of work for the year
3. To detail the work you did
4. To measure how well you met your objectives
5. To explain your plans for the next year.
6. To help readers understand your accounts

To set your objectives for the year. What was it that you set out to achieve in the year? What were your outputs - how many people used your community building in the year – and outcomes - what difference have you made to people's lives? How did these outputs and outcomes relate to your objects - what your organisation is legally permitted to do – and your long-term goals? The objectives need to be **SMART**, that is Specific, Measurable, Achievable, Realistic, and Time-bounded.

To outline your plan of work for the year. How did you plan to meet the objectives? What activities did you plan, and what resources, both personnel (staff and volunteers) and materiel (everything else) did you expect to use? How did you propose to measure your progress (where you got to in the year), your outputs and your outcomes. What the reader is wanting to see is that “We had a plan, and not just any old plan, but a cunning plan”

To detail the work you did. What you did in the year, in terms of activities for beneficiaries (your users) and services to beneficiaries, expressed as statistics, showing number of users, rooms let, courses run, sessions held, services delivered and so on and so forth - the traditional “how, what, who, when, where, why” we all learned at school, in other words.

Use graphs (what Microsoft Excel (and other spread-sheet programs) call charts) to illustrate the statistics, and bring them to life by giving them a human face – remember, community organisations are about helping people,

and it is the people who you've helped who should spring out of your annual report. A good way to do this is to put photographs of your activities in the report. However, be sensitive and sensible - most people don't mind having their photograph taken most of the time, but if you photograph the AIDS clinic your community building is hosting, are you sure their clients want their attendance to be public knowledge?

To measure how well you met your objectives. Compare your actual outputs and outcomes to your planned outputs and outcomes. In explaining any significant differences, be honest. However, whilst your explanations should be the truth and nothing but the truth, they don't have to be the whole truth! Celebrate success as well as acknowledging failures. Management committees often manage by exception, which is all well and good, but if you only ever deal with problems (because these are the exception), your view of your successes and failures will be skewed towards your failures. Finally, soften the hard evidence with anecdotes (an anecdote is a short, true story, which brings your achievements to life).

To explain your plans for the next year. What are your plans for the next year? This needs to be another cunning plan, with SMART (Specific, Measurable, Achievable, Realistic, and Time-bounded) objectives. Always promise less than you can deliver – overachieving a modest target always looks better than under-achieving an ambitious target, even if the numbers are identical. Remember – by the time people get to read the report, this year may already be half gone, so base your plan on the world as it is, not as you hoped it might be.

To help readers understand your accounts. Try and put yourselves in your readers shoes. If you, as the management committee, don't understand the accounts, how can you expect your readers to? It is your collective responsibility, not your accountant's, or even your treasurer's, to make the accounts understandable. Apply Pareto's principle, and concentrate on your vital few activities and not your trivial many - the difficult trick is to sort out which is which! (Pareto was an Italian engineer who first realised that typically 30% of work accounts for 70% of achievement (and expense)). Don't be afraid to use numbers, not just in this bit, but throughout the report.

If your statutory accounts are at all complicated, it is a good idea to put a summary, with charts and graphs, of your accounts in the report. However, if you do, you must

- ❖ Get your auditor/independent examiner to endorse the summary
- ❖ State that a full set of accounts is available, upon request
- ❖ Provide details of how and where the full set can be obtained

18.1. General comments, hints and tips

Your report needs not only to cover the 6 points but also needs to do so in as lively and as colourful a way as possible, so try and make it a good read. To do this,

- ❖ Use the KISS principle (keep it short and sweet)
- ❖ Write in English rather than “officialese”
 - Eschew words like eschew
- ❖ Don't try either to “blind them with science, or baffle them with bulls**t”
- ❖ Use interesting and informative illustrations - a good picture is worth 1000 words
 - It takes (unfortunately) more effort than 1000 words

For charities which are also companies, there are some additional requirements, around the directors publicly acknowledging their responsibilities. These additional requirements are set out in the Charities SORP and more specifically in the Companies House publication covering Annual Accounts (available on the Companies House web site).

For community groups who aren't charities or companies, there are no specific legal requirements, but following the rules for charities is good practice. Note that, whatever the legal requirement, many funders will demand that you prepare and publish an annual report, as a condition of getting their grant.

The report is history. By the time anybody comes to read it, it will be dealing with events anything between 3 months and 9 months old, perhaps even more. There is an important exception. If there is a significant change in your organisation's circumstances between the end of the financial year and the time the report is written, this change must be covered in the report. For example, if your community organisation has run out of money and thus has had to stop work, you must cover this.

Charities have by law to give a copy of their annual report (and accounts) to anyone who asks. So, if your annual report isn't fit to be seen, by the members of the public, it isn't fit for purpose. Requests are rare, so if you get one, seize it as an opportunity to "sell" the good work you are doing (and to enlist their support and their money).

A good annual report is an important marketing tool. It may be that "if you build a better mouse-trap, the world will beat a path to your door", but the world will only know this if you tell them. Your annual report is your one major opportunity to tell the world about your better mouse-trap.

Chapter 19

19. Reserves

19.1. Money Set Aside for a Rainy Day

All voluntary groups ought to have spare money tucked away for when things go wrong (we call this spare money “reserves”). Experience tells us that, sooner or later, things will go wrong. How much should be tucked away is difficult to answer – it depends on the risks of an unexpected reduction in income or increase in expenditure, and varies from group to group. “Rule of thumb” suggests that 3 to 4 months income or expenditure is the minimum.

19.2. What are Reserves?

In simple terms, reserves are the amount that would be left in your bank account at the end of the year when all bills have been paid and all planned expenditure met. However, any monies left over in your restricted funds aren't available for general use, and so don't count as reserves.

In drawing up your accounts, you should explain how your bank account or accumulated fund balances are made up, distinguishing between

- ❖ Endowment fund balances (i.e. donated assets which the charity holds for its own use)
 - Either permanent endowments, which cannot be converted into income
 - Or expendable endowments, which can
- ❖ Restricted fund balances
- ❖ Unrestricted fund balances, made up of
 - Funds required to pay outstanding bills
 - Funds set aside (designated) to meet future needs, such as repairs to buildings or replacement of equipment
 - The rest = the reserves.

Most charitable community organisations don't have endowment funds.

19.3. Building up Reserves

Budgets generally come in three flavours-

- ❖ A deficit budget, in which what you plan to pay out is greater than you plan to receive in. Deficit budgets are a bad idea, unless your reserves (that is, uncommitted cash in the bank) are large.
- ❖ A balanced budget, in which what you plan to pay out is just balanced by what you plan to receive in. Balanced budgets are usually, but wrongly, what voluntary groups aim for
- ❖ A surplus budget, in which what you plan to pay out is less than you plan to receive in. Surplus budgets, which is what you should aim for, are often regarded as wrong for voluntary groups - wrong, because surplus is associated with profit

However, if your group is to

- ❖ Grow
- ❖ Be able to survive sticky patches
- ❖ Be able to do more than live hand-to-mouth

it needs to build up a reserve of cash in the bank.

This reserve can only come from surpluses of receipts over payments. Groups which don't have any reserves now can only realistically build these up by planning for a surplus, and building the plan into their budgets, over several years. For example, It takes 5 years at 5% surplus a year to arrive at the suggested minimum of 25%. Once your reserves have built up to the planned level you can, indeed must, revert to balanced, or even, deficit budgets. Sitting on cash in the bank which you don't need and can't justify is depriving your group and its beneficiaries of its use, and letting down your donors, who have a right to expect you to spend their cash on good causes, not hoarding it in the bank.

In setting your budget, in addition to aiming for a modest surplus, to build up the reserves, you should also have a contingency fund, shown as an item of expenditure. This is to take care of small errors and omissions in the budget, and to allow for the reality that you won't be able to be spot on with all your budget items, no matter how hard you try. Note that, by increasing the size of the contingency, a surplus budget can easily be turned in to a balanced budget, if your funders object to surplus budgets.

19.4. Attitude of Grant-givers

Some of the reasons why groups don't have reserves are

- ❖ What income they can get isn't sufficient. They'll have to work harder at fundraising
- ❖ They have got used to spending all they can get. They need to learn to live within their means
- ❖ They can't get funding if they have reserves.

In fixing the size of your reserves, you will need to take into account the likely attitude of funders. Some will expect you to use part of your reserves, however small, to contribute to the project. Others will take the size of your reserves into account when fixing the size of your grant. Unfortunately, their idea of what is a realistic reserve (typically 1/10 of your annual expenditure) is usually much less than you will arrive at from looking at the risks (typically 1/3 or more of your annual expenditure). However, many grant-givers have softened their attitude in recent years, the London Borough of Ealing being an example who now disregard reserves which are less than 25% of expenditure. If the size of your reserves are a problem for a grant-giver, you can reduce them by designating (setting aside) monies for future work, but doing this is only allowed if:-

- ❖ You can prove you will carry out the work, when circumstances or funds permit
- ❖ You include them in your work plans or business plans
- ❖ The sums set aside are reasonable and in proportion to the work

One of the vexed issues which complicates the relationship between charities and their funders is the question of restricted funds and redundancy. When creating a reserve we are trying to build up a pot of money to cover costs like redundancy payments to staff. However, restricted funds, which can't be included in the reserves, often specifically exclude redundancy, and this seems unfair because if a grant funds someone's post then a redundancy liability starts to build up when they have been with the organisation for two years, even if the post is for a fixed term. All is not lost, however, and you may be able to get the funders permission. If a line for contingent liabilities, such as redundancy, was included in the budget submitted to the funder when the grant application was made, you (and your auditor/independent examiner) can assume that the funder has given their permission. Alternatively, you will have to write to them seeking their written permission to apply part of their restricted grant to cover unrestricted expenditure (such as redundancy payments). There is an example of such a letter to a funder in the facts sheet on reserves on CASH's website: www.cash-online.org.uk.

19.5. Charities' Reserves

Unless this is expressly forbidden by their governing document (constitution, trust deed or memorandum and articles) charities can build up reserves. It is good practice for them to have a reserves policy explaining how the amount of money held in the reserves has been arrived at, and what risks the reserves are intended to cover. Charities are not legally obliged to have a reserves policy, but if they do have one, it must be set out in the trustees' annual report. The size of a charity's reserves, indeed whether it has any reserves at all, and its policy regarding reserves, should all be informed by and related to the risks it runs. Risk management, for this is what having reserves (and indeed insurance), is all about, is a topic in its own right, discussed elsewhere in this document.

19.6. Reserves and Risks

If your group is a registered charity, one of the things you are expected to do is to look at the risks facing your organisation, and to make allowance for these risks in your accounts by having a rainy day fund – a reserve – whose size is matched to the risks. When looking at the level of reserves that it would be prudent for your organisation to hold, you should take into account

- ❖ How secure is the present funding?
- ❖ How long would it take to find alternative sources of funding?
- ❖ What risks and opportunities might arise which could not be met out of income? Consider staff sickness, maternity leave, staff leaving and recruitment costs and the security of your property lease etc
- ❖ If the charity had to close, how long would it take to transfer clients to other organisations and wind up in an orderly manner causing least hardship to users? For example
 - Redundancy costs
 - Legal and accountancy costs
 - The time to the expiry of leases on property and office equipment

19.7. Reserves Policy

A good reserves policy doesn't have to be complicated or lengthy, as the following example shows:-

"The trustees have reviewed the charity's needs for reserves in line with the guidance issued by the Charity Commissioners. These amount to £xx,xxx which approximates to three months running costs. The trustees believe that, taking into account the need to safeguard the charity's services in the event of delays in receipt of grants, reserves should be at least at this level to ensure the charity can run efficiently and meet the needs of the beneficiaries".

Provided the reasons are written down, and agreed by the trustees, a community group's reserves policy could be not to have reserves. However, having such a policy could call into question the services provided and the survival of the group when as inevitable things go wrong.

Any policy should allow the organisation to draw on the reserve in emergencies and to take advantage of unexpected opportunities. The trustees would then seek to rebuild the fund.

19.8. Excessive Reserves

Whilst having little or no reserves is a bad thing, so is having excessive reserves. In some ways, it is worse, since the money should be funding activities, not sitting in a bank gathering interest. What is excessive is another difficult question to answer, but for community organisations, anything much over 1 year's income or expenditure is hard to justify. Note that if your charity has large reserves, but no reserves policy, your trustees could be accused of a serious breach of trust.

Funders and the general public are rightly sceptical about charities reserves. Although many charitable community organisations have little or no reserves, charities in general, large and small have very significant reserves, ranging from on average 2 years income for large charities up to 8 years on average for small charities, as revealed by research published in two Charity Commission reports, RS3 – Charity Reserves and RS5 – Small Charities and Reserves. These are well worth reading, containing wise words on reserves and reserves policies and making recommendations for action to

- ❖ Charities and their trustees
- ❖ Grant-making bodies
- ❖ Donors
- ❖ Charity Commissioners

19.9. When Things go Wrong

For community groups intent on living hand to mouth, the Charity Commissioners publish useful guidance in CC21, Managing Financial Difficulties and Insolvency in Charities. This points out that one way to avoid getting into financial difficulties in the first place is to have reserves! The other way is to have proper financial procedures, which is a subject dealt with elsewhere in this publication.

19.10. Guidance

Detailed guidance on reserves and reserves policies are contained in Charity Commissioner's publications

❖ CC19 Charities' Reserves

<http://www.charitycommission.gov.uk/Library/publications/pdfs/cc19text.pdf>

❖ OG 43 Charity Income Reserves

<http://www.charitycommission.gov.uk/supportingcharities/ogs/index043.asp>

both available to download for free on their web site at the locations shown

Chapter 20

20. Risk Management

20.1. Introduction

Risk management is one of those topics which is on one level extremely simple and on another level enormously complex. On the simple level, it is something we do every day, often without thinking, because living our everyday lives is a risk. Risk is a direct consequence of uncertainty, and the only things which are certain about life are, to quote Benjamin Franklin, death and taxes. Although we generally live our lives by a combination of expecting tomorrow to be like today and planning ahead for major events (like our annual holidays) we know that some things we don't expect will happen, and our plans will sometimes go astray, often for reasons outside our control. We call these unexpected and unplanned occurrences risks, and often take conscious steps to minimise their bad consequences, by taking out insurance, or allowing extra time, or having a spare tyre and basic tools in our car (or joining the AA or RAC) or taking our mobile phone, or even our umbrella, with us.

On the complex level, it can seem like rocket science, as indeed it is, since it is from rocket science that we get many of the formal techniques and most of the terminology. That is, words like "probability", "impact", "assessment" and "mitigate". However, since we aren't actually dealing with the sort of complex projects, like putting a man on the moon, which the rocket scientists were doing when they devised the techniques and the terminology, we can steal their clothes without needing to have their brains.

In outline, before we can manage risks, we need to work out what they are, and if and why we need to worry about them.

First of all, what is a risk? The formal definition is a future event which may or may not happen but if it does will have an effect on our activities. The important ideas to pick up are uncertainty, it may, or may not, happen, and effect, which may be good, or more usually, bad. In risk management terms, we talk about probability – how likely it is that something will happen – and impact – the seriousness of the effect if it does. We could, and the rocket scientists do, spend a lot of time trying to work out the odds of something happening to the same levels as a book-maker, for example, what are the odds of my getting a puncture the next time I drive to the supermarket, but we don't need to, and won't.

We could also, and again the rocket scientists will, spend a lot of time trying to work out precisely what the impact will be when the event happens, which could range in the case of my puncture from my having to spend a few minutes in the supermarket car park changing to my spare, on the one hand, or to my car going to the wreckers and myself to the mortuary, following a blow-out and crash on the motorway (since the supermarket is a couple of junctions up from me on the A1(M), on the other. Again, we don't need to, and won't. What we do is firstly to simplify our task by looking only for or at events which have bad consequences (the events with good consequences are called opportunities), secondly, we put the chance or likelihood of the event happening into one of three categories - low, (i.e. long odds, unlikely), medium (moderate odds, possible) or high (i.e. short odds, probable) and thirdly we do something similar with impact, the damage the event does, fitting it into one of three categories – low (i.e. not much damage), medium (i.e. moderate damage) or high (i.e. severe damage).

Since this is a publication about managing money, we will measure the impact – the damage - in terms of what it will cost us. This brings out another important point – risk is relative – something which happens and as a result a small charity is bankrupted, e.g. losing a dispute at an industrial tribunal, which is of clearly high impact for them might only be graded as low impact by a large national charity with generous reserves. What we can then do is to insert our event into a probability-impact matrix (more rocket science), which is a box of 9 squares, (well, actually 16, but 6 are headings, and one isn't used): see [Figure 38](#)

| | | | |
|---------------|----------------------------|------------------------------|------------------------------------|
| High Impact | <i>Industrial Tribunal</i> | | |
| Medium Impact | | <i>Loss of computer data</i> | |
| Low Impact | | | <i>Late delivery of newsletter</i> |
| | Likelihood Low | Likelihood Medium | Likelihood High |

Figure 38 – Probability/Impact matrix

However, we are getting ahead of ourselves, because what we need to do before we start filling in the matrix is to identify what the risks we run actually are. In principle, we should go through all our current and future planned activities, identifying everything that might go wrong. If we were actually to try and do this, we'd have an enormous list, and we'd never finish, since the list would change as time went on. In practice, what we need to do, as in so many other fields of management, and apply Pareto's principle, by identifying the 20% or 30% of risks worth worrying about and ignoring the rest. If we were trying to do something that has never been done before, which is what the rocket scientists are trying to do, this would be a job and a half in itself. Fortunately, we aren't in that position, and have lots of experience, both of our own and other people's to draw on.

20.2. Identifying risks

Do not be overwhelmed by minor risks. Limit yourselves to the major risks that would prevent your community organisation from achieving its objectives. Consult widely both within and outside your organisation, especially with other community associations, because people in different situations will know about different risks faced by the organisation. Talk to your management committee, all staff, volunteers, users and funders. Use "brainstorming" sessions and market analysis tools, such as

- ❖ SWOT looks at present Strengths and Weaknesses and future Opportunities and Threats
- ❖ STEEPLE considers the Social, Technical, Economic, Environmental, Political, Legal and Ethical issues facing the organisation

Go through the index of one of the voluntary sector management hand-books, such as Just About Managing by Sandy Adirondack. Quality assurance systems like PQASSO can also help you identify and reduce risk.

Consider internal factors:

- ❖ Governance, management committee policies and practice
- ❖ Employment policies and practice
- ❖ Volunteer policies and practice
- ❖ Financial systems and controls
- ❖ Health and safety
- ❖ Insurance
- ❖ Services: quality and delivery systems

Consider external factors:

- ❖ Funding
- ❖ Laws: general like data protection or ones specific to your work e.g. the Children's Act
- ❖ Public awareness and sympathy: people are becoming less sympathetic to the homeless, for instance, and that could affect funding
- ❖ Taxation: is your PAYE system adequate?

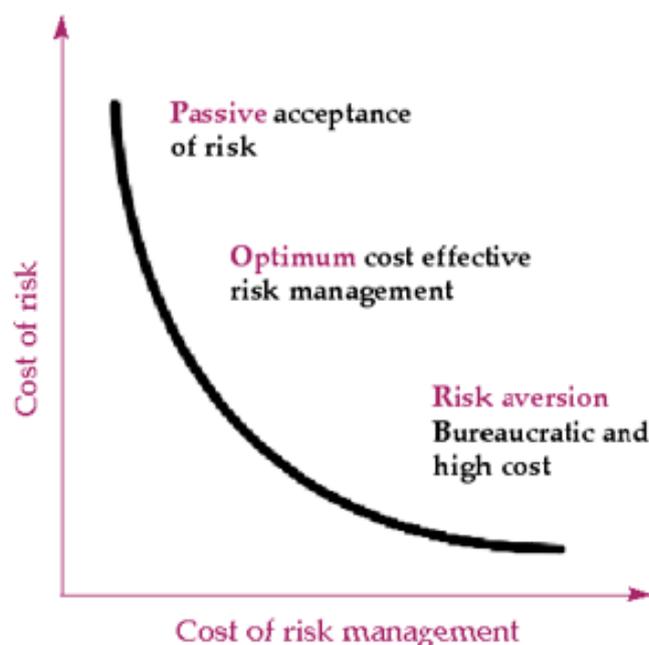
- ❖ Demand: under community care demand for some services has risen. Can you cope?
- ❖ Labour market: can you recruit and train the staff that you need?
- ❖ Technology: will other organisations adopt methods that are more competitive than yours?

Recognise these statistics:-

- ❖ People who work for small organisations are twice as likely to be hurt in an accident at work than people who work for larger organisations
- ❖ Of victims of “acquaintance violence”, 23% were assaulted by their organisation’s customers or clients
- ❖ Voluntary sector workers are twice as likely to take their employers to an industrial tribunal as private sector workers
- ❖ Three out of ten employees in the UK experience mental health problems at some stage in their working lives. Five percent are suffering from major depression at this moment
- ❖ One hundred charities in London are likely to close through insolvency this year
- ❖ There are 25,000 trustee groups in London. Sixty of these groups will pay from their own resources towards damages awarded in industrial tribunals and debts associated with their charity. This failure rate compares favourably with the private sector, but still needs attention

It is very important that you consider your own organisation and its particular services, its uniqueness and the risks that are associated with it. It isn't possible to produce a list of all the risks that would cover every organisation, so what are outlined above are just a few pointers. Also, whilst we need to learn from history and not repeat our previous mistakes, we also need to recognise that some of the risks which tripped us up in the past were in fact no more likely than some of the risks that didn't. As a result, we need to make sure that we evaluate each future risk on its own merit, and not be unduly influenced by the past. We've all heard of the saying that armies are always equipped to fight the last war and not the next - make sure you don't all into the same trap.

Once you have identified the risks and assessed their impact, you need to decide what to do, if anything, about them. The [Figure 39](#) shows the trade-off between spending too little on risk management when the cost impact of a risk is high, and too much when the impact is low.



[Figure 39](#) – Risk Management Trade-off

However, if you aren't a rocket scientist, how do you interpret it? The answer is, you don't, directly, you use the matrix, [figure 38](#), into which you should by now have put all the risks worth worrying about you have identified.

Indirectly, the figure provides clues about where to put your efforts. You should concentrate your efforts on events in the high impact, medium impact and high likelihood boxes. These you need to look at in detail. Since we should put these into a formal document, the risk register, we'll call them our risk register risks, and it is these, and only these, which we need to manage.

20.3. Mitigate the risks

Mitigation is another of those rocket science words which in principle means reduce the impact of a risk if it happens but has come to mean anything we do to respond to a risk. There are 6 main ways of responding to a risk:-

- ❖ Avoid it. This is the only rational response to a risk which has both high probability and high impact. Walk away from a contract or grant with onerous conditions. Don't take on work you know you can't finish
- ❖ Reduce it. Where you can't avoid a risk, because it is inherent in what you do or want to do, for example, working with violent clients, take positive steps to move it from say high likelihood, high impact to at least medium likelihood, medium impact. You will have to put in extra time and effort, so part of the response should be to increase the charges to your funders to cover additional insurance, staffing and equipment
- ❖ Minimise it. In effect, try to reduce its probability, or its impact, or both. This is what your policies, procedures and training are supposed to do. What distinguishes this category from the previous one is that we don't need to make a special effort, and should be able to manage these risks in the normal course of events
- ❖ Transfer it. In other words, make it somebody else's problem (usually, in exchange for money). This is what we do when we take out insurance, or contract out some activities, such as putting out payroll out to a bureau
- ❖ Accept it. This is, in effect, what we do about all the risks we identified with low or medium likelihood and low impact. We may also choose to manage a risk in our risk register in the same way. For example, a charity taking on a short-life license on office premise is accepting that it will have to leave the building sooner rather than later
- ❖ Let it run, but monitor it. Where you aren't certain what the likelihood or impact of a risk might be, but you don't feel happy just to ignore it, we monitor it, that is we keep an eye on it, and review our assessment of its likelihood and impact regularly

The text-books refer to a seventh category, which is related to those risks whose impact is or could be made positive – referred to earlier as opportunities.

- ❖ Exploit it. You can try and turn a risk to your advantage - a charity rescuing child slaves could exploit the risk factor it's volunteers face in its fundraising. This is much talked about by academics and management consultants, but is one of those aspects of risk management best left to the rocket scientists, and how often do they manage to get anything done on time and within budget? (Trust me – I know what I'm talking about – I used to be a rocket scientist!).

20.4. Risk register

You've identified those risks that you need to worry about, and have decided what to do with each, so the next step is to list them and the action to be taken in a risk register. Before you do this, make sure that a named person is responsible for managing and monitoring each identified risk. Unless you are a large organisation with several departments or major projects, when each department or project should have its own register, you shouldn't have more than 10 or a dozen risks in the register, which should have the following column headings:- Risk, likelihood, impact, mitigation strategy (i.e. reduce, minimise, etc), Action to be taken, Person responsible (by name, not office), Review period (the length of time between reviews).

Risks don't remain static, and neither should your register. Old risks will turn out to be less of a problem, or just never happen, and new risks will emerge, so you need to monitor and review the risks in your register, quarterly is appropriate for most risks, but some might need to be done monthly, and some, like the ones you insure against, annually. The register and the risks in it should also be reviewed by your management committee at their quarterly meetings, to ensure that those responsible are managing the risks assigned to them.

Every year, as part of setting the annual budget, all existing risks need to be reassessed and all new risks identified and, where appropriate, mitigation strategies agreed. It follows that you will need to compile a new risk register each year (though in practice, many risks will remain from the previous issue).

20.5. Reserves

The main justification for having reserves are to cover the extra costs resulting from risks, if and when they happen. So, implicit in setting the level of reserves is costing the impact of the risks in our register. Note that this is the extra cost of the risk if it arises, not the cost of transferring a risk, or reducing it, since these should be built into our budgets already. However, no matter how careful we are, or how thorough, we won't be able to cost the impact of all the risks accurately, and some of the risks we foresaw won't happen, and others which we didn't foresee will, so this isn't an exact science. Prudence, one of the accounting principles, therefore dictates that our reserves should be larger than the figure arrived at by calculating the impact of the risks in our register, by how much is debatable, but 20% to 25% is what the rocket scientists suggest.

20.6. Annual report

If you follow the recommendation that you use the Trustees Annual Report Form in CC17 as the template or model for your annual report, you will find that you should "confirm that the trustee body has undertaken a review of the major risks to which the charity is exposed and that systems designed to mitigate those risks have been considered." Whilst not mandatory for charities whose turn-over is less than £250,000, it is good practice, and if you adopt a risk register your annual report could (indeed should) say: "The trustees have drawn-up a risk register which provides dates and details of actions to be taken to reduce risk. The charity also purchases a range of insurance policies".

Chapter 21

21. Financial Controls

21.1. Introduction

In an ideal world, we wouldn't need controls, we would rely only on trust. In the real world, we can never be sure that we can trust everybody, and we need to substitute controls for trust. There are two fundamental Laws of Accountancy: the first law is: trust nobody, least of all yourself, and the second law is: see the first law

What the controls do is show our stake-holders – members, funders, regulators and, importantly, our beneficiaries that

- ❖ Their money is safe in our hands
- ❖ We spend it wisely and well
- ❖ We spend it as the funders would wish
- ❖ We spend it in the best interest of our beneficiaries

They also

- ❖ Prevent fraud and theft
- ❖ Defend staff and volunteers from unjustified accusations of fraud and theft

What we need to control is the flow of money into, out of and within our organisation. We do this

- ❖ By having staff, committee members and volunteers who have the required level of knowledge and experience
- ❖ By having procedures (written instructions) setting out who is to do what, and when, and how
- ❖ By following the procedures without exception

We can divide our controls into four:-

1. Basic controls
2. Control of incomings
3. Control of outgoings
4. Control of assets

21.2. Basic Controls

Basic controls need to address

- ❖ Providing for segregation of duties
- ❖ Having staff, committee members and volunteers with the required level of knowledge and experience
- ❖ Setting budgets
- ❖ Managing bank accounts
- ❖ Carrying out regular bank reconciliation
- ❖ Producing paper trails
- ❖ Measures to mitigate the risks of getting involved in money laundering and the proceeds of crime

The principle behind segregation of duties, which is a fundamental of financial control, is to divide up any task involving the management of money between people, to prevent any one person in your organisation both recording and processing a complete transaction. For example, you shouldn't let the person who records cash received also check the bank statements, and the person who keeps the books shouldn't also do the bank reconciliations. In large organisations with lots of staff splitting responsibilities between different staff members is straight-forward. For small organisations, and most community organisations are small, with limited numbers of staff and volunteers who may themselves have limited financial skills, this is the most difficult control to put in place. What you must do, at least, is avoid concentrating all money management in the hands of only one or two people – the treasurer and the warden/centre manager, typically, and is yet another of the many good reasons for not leaving it all to the treasurer. It is also worth considering adding additional controls, such as spot-checks or audits, to compensate.

Having staff, committee members and volunteers with the required level of knowledge and experience of managing money is the best control of all, but often the one furthest from our grasp. You need to ask yourself 2 main, and one supplementary question

- ❖ Are our staff, committee members and volunteers up to the jobs you expect them to do?
- ❖ Do they have the knowledge, skills and experience needed?
 - Do you know what these are?

You answer these questions by carrying out a financial health check of your organisation. How you do this is discussed in section 21.8 below. If the answer is, as it will be, hopefully to a lesser but realistically to a greater extent, that they don't, what are you going to do about it? Well, you can and should offer training, provide support and undertake supervision. Training courses in managing money for voluntary organisations are widely available – contact your local CVS, community accountancy project or Community Matters to see what is available locally. You can provide support by getting an experienced hand to mentor an inexperienced one, or just allow time to sit with someone – two heads are better than one. You may be able to provide technical supervision through the treasurer or another experienced committee member, or just rely on good line management.

Forensic accountants (that is, the people who investigate fraud) tell us that there are clear warnings for all to see before any serious fraud in voluntary groups, and that the fraud invariably results from a breach of trust. These signs, which you need to watch out for, especially when carrying out a financial health check are:-

- ❖ A dominant individual, who treats the organisation as his or hers, who is trusted implicitly by other staff members, the management committee and volunteers, and who has come to feel that the group “owes” him or her, perhaps through years of carrying the committee or working unpaid overtime
- ❖ A management committee whose members are weak and ineffective
- ❖ All the procedures under the sun, but none of them being followed
- ❖ A significant amount of the annual expenditure in cash

If you recognise any of these symptoms in your organisation, start taking remedial action immediately, before it is too late.

How to set a budget is dealt with elsewhere, but from a control point of view the critical factors are that

- ❖ The budget is based on proper and realistic estimates of income and expenditure for the year
- ❖ It is approved in advance of the year by the management committee
- ❖ All income is received and expenditure is made within the framework of this budget
- ❖ It is reviewed regularly (at least quarterly) by the management committee to make sure it still applies

Your organisation should have two bank accounts in the organisation's name, a current account with a cheque book, and a savings account, both requiring two signatures (from a pool of 4, ideally all committee members). All monies received should be paid untouched into your bank account, and all payments made only from your bank account. Never, ever, permit a blank cheque to be signed by one of the signatories. The charity commissioners consider such an action to be a serious breach of trust, and if your charitable community organisation is unincorporated, this is one of those occasions when the management committee become individually and collectively liable.

A bank reconciliation is when you compare your accounting records with the bank's, and explain any differences. How to do this is discussed elsewhere. Doing a bank reconciliation is a basic and fundamental control, widely neglected. It can be a fiddly job requiring attention to detail, but rocket science it isn't! A reconciliation should be done every time you receive a bank statement, and to enforce separation of duties, the reconciliations should at least be checked by a different person from the one making up the books.

Establishing a paper trail is crucial. All movements of money into, out of and within your organisation need to be explained and justified by a piece of paper, cross-referenced to the movement and to your books, neatly filed away. Ideally, the paper should be from outside your organisation, which should be easy for outgoings, in the

form of invoices received, shop receipts, tickets, and the like. For incomings, this is less easy, but you should be able to file away grant letters, the invoices you sent out, and the receipts you gave out in exchange for any cash and cheques you received.

Why should my community organisation running a community building bother about money laundering and the proceeds of crime? Well, the first may not be too much of an issue, unless your community organisation supports a community with its roots overseas and who send money back home, but the second certainly could be, given that many community organisations flirt regularly, willingly or unwillingly, with the informal (black) economy.

Money laundering occurs where money earned from or intended for criminal activity is passed through a legitimate organisation (like a voluntary group) to disguise its origins and/or purpose. For example, a criminal gang selling drugs in the UK make large donations to a legitimate UK-based relief organisation which then makes large donations for relief work in the drug's countries of origin, which the gang's associates in those countries use (unbeknown to the relief organisation) to purchase more drugs. There are really only two controls you need to put in place :-

1. Don't accept large donations in cash, insisting that such sums are passed through a bank account and paid to you by cheque. This makes checking the legitimacy of the donor the bank's problem, not yours!
2. Use only high street banks or other reputable agencies (who will provide a paper trail) if you need to send money overseas.

Proceeds of crime is a broad term covering all money earned by dishonest means. The definition covers not just direct theft and fraud but also indirect theft and fraud (e.g. tax and VAT evasion) and those who aid and abet both direct and indirect theft and fraud. This matters to community groups because you could be liable if you

- ❖ Pay cash in hand wages (direct evasion of PAYE and NI)
- ❖ Pay workers as if they are self-employed (indirect evasion of PAYE and NI)
- ❖ Pay cash to suppliers off their books (aiding and abetting evasion of VAT)

You could take the attitude that we won't tell, so why should this matter? Unfortunately for you, your independent examiners, auditors, bankers and other professional advisers have a legal duty to "whistle-blow" – to report all instances of money obtained dishonestly by any group they have professional dealings with to the National Criminal Intelligence Service. There is no "de minimus" limit. i.e. there is no minimum amount, so in theory, obtaining 1p dishonestly is a reportable offence! In practice, trivial amounts will be ignored. If they do "blow the whistle", for those of you who are trustees of unincorporated charities, this is when you could become personally liable, and for those of you feeling relieved because you are hiding behind limited liability status as directors of a charitable company, there is bad news - this is when you could lose that limited liability.

The simple answer is don't get involved in the informal economy.

21.3 Controls of Incomings

Controls of Incomings covers

- ❖ Incomings in cash
- ❖ Incomings by cheque
- ❖ Direct credits
- ❖ Fundraising events
- ❖ Banking and custody
- ❖ Checks of records

Incomings in cash are always a set of problems waiting to happen, so where you can, don't accept cash. Where you can't avoid cash, (ideally) have two people present when cash is received, get different people doing the job, always give a receipt from a duplicate book and always pay the total amount received into the bank. Where

you can, don't keep cash overnight. Where you can't avoid this, get a safe, pay the cash into the bank as soon as possible and take out insurance. Don't forget to get, keep and file the supporting paperwork.

For Incomings by cheque, record the cheque details (by making a photocopy), and relate it to the supporting paperwork (e.g. the grant letter, your invoice or the membership form). Pay the cheques into the bank promptly, using only numbered slips from your paying in book (and if the bank doesn't number the slips, you must), noting the cheque details on the paying in slip.

Increasingly, grants are paid and even invoices are settled by direct credits, which are electronic payments direct to your bank account. You need to check the amount of the in-payment against the grant letter or your invoice, recording the details on the paperwork, and filing the paperwork away.

For each fund raising event, you need to identify both gross incomings, and how these have arisen, and all costs incurred. Never net off, i.e. show only the profit/loss on the event. If you are a charity, this is not just bad practice, it is a breach of duty. Where tickets are sold, pre-number all tickets, record who has been given which tickets to sell and which have been sold, and reconcile income from ticket sales against tickets sold. If these events involve bingo or raffles (lotteries), run these strictly in accordance with the legal requirements (which are set out on the Gaming Board of Great Britain's web site, or refer to the relevant Community Matters information leaflet).

Banking and custody controls inevitably overlap with other controls, covering such routines as receipts always being exchanged for cash, cash and cheques being banked promptly, intact, and using only pre-printed paying in slips. Custody controls look at the security and safety of cash and cheques both when they are in your community building, when they should be kept locked in a safe, and on the way to the bank, and of your receipt books and paying in books. If you lose control of your receipt books, how do you know that somebody isn't diverting cash intended for your organisation?

You need to check your records, so that the details of cash and cheques received agree with the paying in slips and the paying in slips reconcile with the bank statements. You need also to check that you have identified all direct credits and verified them against the relevant paperwork, and any of your invoices which remain unpaid, following up those which are overdue. The checking needs to extend to both identifying any restricted income funds and that the restrictions are known and are being complied with. Finally, if you allow credit, you need to confirm that your credit terms aren't being abused, and that credit hasn't been granted without your knowledge and agreement.

21.4. Controls on Outgoings

When people talk about financial controls, assuming that they do, it is controls on expenditure, that is controls on outgoings, that they mean. What needs to be controlled are:-

- ❖ Wages and salaries
- ❖ Purchases
- ❖ Payment by cheque
- ❖ Payment in cash
- ❖ Payment by direct debit/standing order
- ❖ Debit and credit cards
- ❖ Electronic banking

All supported and backed up by

1. Checks of records

Since expenditure on wages and salaries can account for 2 / 3 to 3 / 4 of total outgoings for a community organisation, it warrants extra care. All employees, full-time, part-time permanent, temporary or casual, should

be on the books. Do all the employees on your books actually exist, are they doing the work they are paid to do, receiving only authorised rates of pay/salaries, and have they all got contracts of employment?

Are all employees having PAYE & NI deducted, with proper records – P11s or equivalent – being kept? Check that there are no cash-in-hand wages – that is, cash payments made from cash income, usually before being entered in the books, to compound the felony. You can save yourself a lot of work if you contract out your wages administration to a payroll bureau, but remember, it is still your responsibility.

If you pay all wages by cheque or through BACS (Banks Automated Clearing System), you don't have the bother of cash wages, which avoids having to have cash on your premises and making up pay packets, not to mention dealing with pay packets which have got lost or been stolen. However, this does mean that all your employees have to have bank accounts, and this, though logical, may not be reasonable in your organisation's circumstances.

Are your consultants, trainers, aerobics instructors, dance teachers and the like genuinely self-employed? Can they pass the Inland Revenue's "employed or self employed?" test? Do they provide you with invoices, letters of comfort and their Revenue and Customs Self Employment Reference Nos.? Abuse of self employment in the voluntary sector is a concern to Revenue and Customs, discussed in depth elsewhere in this document, so controls to prevent your organisation falling foul of the Revenue and Customs are a must.

For purchases, you need to ensure that orders for goods and services have been properly authorised, with the levels of authority defined and documented. Invoices should be checked against the relevant orders placed, and records of orders placed but not yet fulfilled should be maintained. The quality and quantity of goods and services delivered should be checked against both orders and invoice, and regular stock-taking undertaken. Payments should only ever be made against original invoices. Where you can, implement separation of duties, so that those who order goods aren't those who pay for them (else how do you prevent them ordering goods for their own use, which your organisation's funds pay for?). If this is not possible (due to too few staff/volunteers), consider putting in additional checks and controls.

Payment by cheque is another of those areas already partly covered by management of bank accounts, but a little repetition and overlap is no bad thing, starting with each cheque requiring 2 signatories from a pool of 4, ideally all members of your management committee, but not connected (that is, not spouse, partner, parent, sibling, or offspring), and never, ever, getting blank cheques signed by one signatory. Cheque books need to be kept in custody when not in use, that is to say in a safe and secure place, like the office safe. All cheques should be prepared and signed only against paperwork – an invoice, a shop receipt, or similar, with the cheque details recorded either on the paperwork or by attaching a photocopy of the cheque.

Wherever possible, avoid making payment in cash. One way to do this is to reimburse expenses by cheque, with claims being submitted weekly/monthly. Where you can't avoid cash, use an imprest petty cash system (what this is and how to do it is explained elsewhere in this publication), and keep the amount of the imprest (float) as small as possible. Don't ever use cash income to top up petty cash, and always keep the petty cash in a safe place (a locked cash box in a locked cabinet, for example. Pay out, and then only small sums (less than £5) only against authorised petty cash vouchers supported by receipts, tickets, etc., and always get the claimant to sign the voucher or a receipt. Check the petty cash regularly, ensuring that cash in the tin + vouchers/receipts in the tin = the imprest..

Payments by direct debit/standing order are increasingly common. A direct debit is where you give a supplier access to your bank account to take out such amounts and at such times as the supplier sees fit. If things go wrong, your argument is primarily with the supplier, and only secondarily with your bankers. For obvious reasons, suppliers like direct debits. With a standing order, you instruct your bankers to make regular payments of fixed amounts to a supplier. If things go wrong, your argument is only with your bankers, never with the

supplier. In either case, control is exercised only through the mandate, which is the written instruction to your bankers to set up a direct debit arrangement or a standing order, so the first thing to check is that your mandates have been properly authorised, that is, signed by 2 of your 4 people authorised to sign cheques. Since direct debits and standing orders are electronic payments direct from your bank account, you need to check the amount of each payment against both the relevant mandate and the supplier's invoice, recording the details on the paperwork and filing the paperwork away

The simple way to control corporate debit and credit cards is not to have them.

- ❖ They by-pass the two signature control system
- ❖ They allow ready access to cash, goods and services
- ❖ It is all too easy to run up unauthorised and unpayable debts

Using corporate debit and credit cards in this way is another of those things which the Charity Commissioners treat as "a serious breach of trust". If they are such a problem, why do voluntary organisations have them? For two reasons:-

1. Because they allow the group to access cash, goods and services without going through the controls. This is never acceptable
2. Because they enable the group to purchase goods and services over the internet/telephone

If the second reason is legitimate, what are the alternatives?

Firstly, have accounts with suppliers, trading-off price versus control, if necessary. Secondly, and this is common-place in community organisations, use a personal credit card (for example, the treasurer's, the chair's, the warden's/centre manager's), and claim back the money. For items purchased on a personal credit card for your organisation's use, the purchase should be authorised in advance (in writing, preferably in the minutes of a management committee meeting, with reimbursement against a supplier's receipted invoice, not just a credit card slip, by a cheque made payable to the credit card company, not the individual. Reimbursement must be prompt.

If after all this your organisation must have a corporate credit or debit card, you need to arrange for its safe-keeping when not in use, to control its issue and use, specifying who can use it, and for what, and when, and for how much money, and so on and so forth, with each use authorised in advance in writing. All instances of use must be checked against the card account, the supplier's receipted invoices and the card slips.

Is Electronic Banking the way of the future, or a new opportunity to evade controls and commit fraud/theft? It is a bit of both. Since the fundamental control on all expenditure is by requiring two independent authorisations, the issue becomes how to do this with electronic banking, when many banks don't provide for it. The answer is simple, if your bank is one that doesn't, don't use electronic banking to authorise payments, and switch to a bank that does, e.g. Unity Trust Bank. If you are thinking of going down the electronic banking route, before you do, read the Charity Commission's guidance, published on their web site (www.charitycommission.gov.uk).

The checks of records of outgoings parallel those for incomings, as follows:-

- ❖ Records of cash paid out agree with petty cash vouchers
- ❖ Cash payments reconcile with the imprest
- ❖ Records of cheques paid out agree with cheque stubs and supporting paperwork (invoices, receipts, etc.)
- ❖ Cheques reconcile with the bank statements
- ❖ Standing orders and direct debits are identified and verified against paperwork
- ❖ Debit and credit card use is identified and verified against mandates and supporting paperwork
- ❖ Restricted funds are identified, the restrictions are known and all payments made from the funds comply with the restrictions
- ❖ Suppliers invoices which are unpaid are checked and any that are overdue are followed up
- ❖ Check that supplier's credit terms aren't being abused, and that credit hasn't been taken without authority

21.5. Control of Assets.

Community organisations, especially those occupying community premises, have lots of assets (if you don't believe me, just tot up what all the stuff cluttering up every room and overflowing from every storage space will cost to replace), yet control of assets is often poor or non-existent, even though it is a statutory duty of charity trustees. The assets you need to control are:-

- ❖ Current Assets
- ❖ Fixed Assets
- ❖ Loans
- ❖ Investments

Since liabilities are the inverse of assets, control of these is also included and covered

Current Assets is made up of stock, debtors and creditors, and cash at bank and in hand. Strictly, stock is items for sale, which usually in community organisations means bar stock, but it could include consumables. Control of stock, in the context of a bar in a community building, is dealt with elsewhere in this publication, but the essentials for any type of stock boil down to controlling the levels of stock, the ordering of stock, taking stock, valuing it (always the lesser of purchase price or sale price) and storing it. In the context of storing stock, what are you going to do about those cupboards full of stationery and left-overs from your last publicity drive or fundraiser?

Debtors and creditors are those who owe you money, and those you owe money to. When it comes to debtors, are your terms of business set out (e.g. cash only, in advance, or 30 days to pay), are they reasonable (if a significant proportion of your users don't have bank accounts, is it reasonable to insist on receiving only cheques) and are they being adhered to? If not, what do you intend to do about it?. Similarly, with creditors, have you negotiated the best terms you can with your suppliers, and are you sticking to your supplier's terms of business? If you aren't, what do you intend to do about it? At this point, the issue of bad debts always comes up. In the context of community organisations and community buildings, this almost always means either from room hire or from play-group parents, and these are dealt with elsewhere in this document.

Control of cash at bank and in hand divides neatly into control of cash in hand, which breaks down into the level of the imprest float together with the control of petty cash, and control of cash received in transit to the bank, which topics are adequately covered elsewhere in this document, and control of cash at the bank. These need to take into account the levels of current account balances, and what to do if they get too large or too small. For the latter, overdraft arrangements, and the risks associated with running an overdraft, and for the former, what to do with any surplus, such as transferring it to a savings account, and if so, what are the interest rates on offer, and are there any limitations and penalties on withdrawal. Is it worth making a sweep arrangement, that is, an arrangement whereby once the current account balance reaches a pre-determined level, any surplus is transferred to the savings account, with the reverse happening if the balance falls below a set threshold. How are transfers to be authorised, bearing in mind that banks often accept a lower standard of authorisation for transfers than for withdrawals. Last, but not least, do you get regular bank statements, and if not, why not? Who in your organisation receives these, and who reviews them?

Fixed Assets covers land, buildings, vehicles, fixtures and fittings, and equipment (including computers and the data in them). Do you have (as, if you are a charity you must have by law) an asset register, in which all the fixed assets you use, whether purchased, leased or donated, are identified and listed. Is the list kept up-to-date, and are all the assets listed regularly checked, to verify both that they exist and that their whereabouts is known, not forgetting laptops, mobile phones, etc. which may be off your premises, and that they are in working order. Also, are they still in use, appropriate and needed, and appropriately insured, if necessary under the all risks section of your policy?

Loans covers both those made and those taken. Where loans are made (and assuming that this is permitted by your governing document), have these been properly authorised? This usually means being discussed and agreed by the management committee and recorded in the minutes, and there should always be a written agreement setting out the terms and conditions. What about informal loans, such as advances to cover expenses, advances of wages, and even advances of petty cash? You will need to put in place special controls where a loan is made

- ❖ To a member of your management committee. This is never good practice, and if your organisation is a charity, not normally permitted
- ❖ To your associated or subsidiary trading arm. Such loans used to be common-place, but where community organisations are charities, have increasingly troubled the Charity Commissioners, who are concerned that charity funds are being risked in ventures with both a poor rate of return and poor chances of success. If you do decide that providing such a loan is in the best interests of the charity, you need to ensure that the risks are proportionate and the interest rates extortionate

Where loans are taken, whether these are commercial loans from financial institutions or local authorities, or from management committee members, as for loans made, the decision to take the loan should be discussed by the management committee and minuted, and especially where the loan is from a committee member, there must be in place a written agreement, specifying both the rate of interest and the repayment terms.

If your community organisation is lucky enough to have money to make investments, pre-requisites are that you have a policy in place, you seek and follow professional advice, and that you spread the risks by having a diversified portfolio (i.e. not putting all your eggs in one basket). You aren't obliged to chase maximum returns willy-nilly, and can take into account ethical and community development concerns in your investment policy, but these should bear some logical relationship to your organisation's objects. The management committee should regularly monitor the performance of your investments, and authorise, by minuted discussion, all acquisitions and disposals. Full records of all investments must be kept, in a secure place, and checks put in place to ensure that dividends and interest are received when due.

21.6. Implementing Controls

Having identified what we need to control, how do we actually go about implementing controls?. At the risk of repeating what was set at the beginning of this chapter, we do this

- ❖ By having staff, committee members and volunteers who have the required level of knowledge and experience
- ❖ By having procedures (written instructions) setting out who is to do what, and when, and how
- ❖ By following the procedures without exception

If we need staff, committee members and volunteers with the required level of knowledge and experience, how do we do this? Initially, through recruiting only the knowledgeable and experienced.

In practice, most community organisations get the volunteers/committee members they are given, or the staff they can afford, and need to make the best of it. Also, if groups can't or won't take on the untrained and inexperienced, how do they get the experience? The solution is through training, so be prepared to offer and pay for training for your staff and volunteers. Good training doesn't come cheap, so you need to make realistic provision in your budget, and don't forget your treasurer and other committee members. You identify what training you need to provide through carrying out both a training needs analysis and financial health checks.

Once we've recruited and/or trained the staff and volunteers, not forgetting that our committee members are volunteers, we need procedures setting out who is to do what, and when, and how. In principle, procedures don't have to be in writing, but, if they aren't in writing,

- ❖ How do you demonstrate a procedure?
- ❖ How does everybody know what it is?

❖ How does everybody follow it?
and critically, how can you tell?

When writing a procedures, apply the KISS principle - keep it short and simple – and don't try to cover every eventuality, concentrating on the control of the vital few activities, not the trivial many. Steal with glee, by basing your procedures on somebody else's, but adapt it to suit your circumstances. Starting points for this can be provided by

- ❖ CASH's model Financial Policy and Procedure, which is available on the website www.cash-online.org.uk
- ❖ NCVO's models, which cover:-
 - Controls on expenditure
 - Controls on income and debtors
 - Petty cash
 - Stock control
 - Cash flow management
 - Working capital managementAll these are available on their website
- ❖ VolResource sample document: financial procedures
- ❖ Civicus toolkit – financial control and accountability

If the controls are to work, we must follow the procedures without exception. There is a common saying "rules are for the obedience of fools and the guidance of the wise". We all think we are wise, when all the objective evidence shows that we are all fools. How we check that the controls are working is by carrying out our regular internal audits. An internal audit is a check that

- ❖ You have rules (these are what are written down in the procedures)
- ❖ The rules work
- ❖ You are following the rules

Carrying out the internal audits is a job for three of the non-executive members (i.e. not portfolio holders, especially not the chair, treasurer or secretary) of your management committee. Make not following the rules a serious breach of discipline, writing this into your codes of practice and conduct. That may be all right for staff and even volunteers, but what about members of the management committee – they, especially the chair, are often the worst offenders? Don't allow any exceptions, even for the treasurer and chair. If they won't tow the line, withdraw their authority, by removing them from the list of authorised signatories, and by refusing to reimburse them for purchasing goods and services where these were not authorised in advance.

21.7. Stock Control and Bars

Stock is the items of value we keep by us, primarily to sell or use. This could include the beer, wine, spirits and soft drinks for sale in the bar, the cigarettes for the vending machine, the pre-packaged snacks, tea, coffee, soft drinks, and the uncooked and processed food, fresh and frozen, for the coffee bar and lunch club, the publications we have for sale and all the stuff not only in our stationery cupboard but also in the cleaners cubby-hole. Although this section is primarily about bar stock, since this is usually both the most valuable and the most subject to getting lost, stolen or strayed, you also need to keep some control of both stationery and cleaners' consumables, else you will end up supplying the neighbourhood's children with pens and paper and the neighbourhood's households with toilet rolls, all at your expense!

There are many reasons why we should exercise control over the stock of alcoholic and non-alcoholic beverages we sell in our bar, not least that they are worth a tidy sum, but one of the primary reasons is so that we can work out what we have sold, and whether what we got for it was what we planned. We won't know how much we made on the bar unless we take into account the change in the levels of stock before and after. In principle, we should take stock, that is to measure our levels of stock by counting bottles, gauging spirits and weighing barrels, before and after each session. Whether we can do this in practice depends on the frequency

of the sessions, the quantity and variety of the stock, where it is kept, and the time and effort we are prepared to put in, or pay someone to put in, to do it. We also need to make sure that we rotate the stock, that is, to make sure we sell older items before newer items, and that we are selling all our stock before it goes out of date.

Another critical aspect of stock control is ordering. You need in the first instance to set what levels of stock you carry, and then to decide at what level you re-order. When fixing stock levels, you need to strike a balance between carrying too much stock which ties up your organisation's money and takes up space (which also costs you) and too little, when you run the risk of running out during a session. When re-ordering, the most straightforward way is to treat the stock like petty cash, and order what you've used since the last delivery, to top up the stock to the agreed level. Unfortunately, you don't (usually) sell in the units you buy, with orders by the barrel, (of beer) bottle(of spirits) and, crate or box, and you will have to round up or down orders, as appropriate.

If you are able to take stock before and after each session (between sessions, in practice) you will have the best foundation for both stock management and analysis of sales. You will know not only how much you sell, and how much you did and should get for it, but also what sells and what doesn't. If you have an electronic till, this will in principle give you the same information, based on what the bar staff enter at the tills, but the only way you can keep such a system (and the bar staff) honest is to have both regular and random stock checks - the tills aren't physically counting stock; even swiping a bottle past a bar code reader is no guarantee that there was anything in the bottle, and it is commonplace to have a board of bar codes by the till, to cover sales of draft beers and soft drinks and shots of spirits.

Whatever you do, don't stock take just once a year, to establish the stock at the year end. If you can't do it between sessions, do it once a week (traditionally, on a Sunday, but in practice, any quiet day will do, and take into account your day for the brewer's dray and the lead-time for ordering). As hinted at above, you should also aim to carry out additional stock checks, unannounced and at irregular intervals, especially if you rely on your electronic tills for stock data.

Who does the stock taking is as important as when they are done. All need to be done by 2 people, not always the same pair, and ideally they should not be responsible for the day to day running of the bar. The random checks in particular should always be done by 2 members of your management committee, again not involved in running the bar. In practice, these ideals may be difficult to attain, due to the limited number of available people, and you may need to add additional controls or cross-checks to keep the stock-takes honest. Some groups prefer to get in external stock-takers, but these cost money, and aren't essential, unless your whole bar operation is turning over serious money.

Although specialist bar management software is available which can turn your stock-taking figures into comparisons of expected sales with actual sales, forecast and actual profits, values of stock held, patterns of consumption, stock order amounts and so on and so forth, in practice there is little that can't be achieved using a computer spread-sheet, such as Excel. The mathematics involved is straight-forward.

21.8. Financial Health Check

Voluntary organisations need good financial systems to avoid running out of money and to avoid allegations of fraud. Good financial systems enable the charity to spot problems quickly and adjust activities to maximise the effectiveness of their funding.

Poor financial systems can exist for a number of reasons. In small organisations it may be that this area has never received any real attention. The volunteers who run the charity may have focused their efforts on the main task of the charity - such as arranging summer holidays for disadvantaged children – and no one has ever had the energy to sort out the bookkeeping on a regular basis. Financial papers are given to the Independent Examiner every year who "sorts it all out".

This type of approach is fraught with risk. It is easy for money to be misappropriated. Twelve months after the event pieces of paper are often missing and verbal explanations have to be given which are frequently little more than guesses. Funders, understandably, would be unhappy if they knew that there was very little control over the finances – and they could withdraw their funding. People with grievances can make allegations to funders - true or false - about poor financial management and fraud.

21.8.1. Large organisations

In larger organisations financial health checks are useful because staff may not have relevant training or may not be aware of the specialist accountancy needs of voluntary organisations. The charity might have expanded over time with no one focusing on whether the financial systems have been strengthened to reflect the greater demands being placed on them.

21.8.2. Check ups

An occasional check is a very good way of ensuring that staff are working well. Lax conditions often arise when no one appears to be interested in a particular area of the organisation. Anybody with common sense could be asked by the committee or manager to undertake a financial health check. We have detailed below the main topics that should be covered.

21.8.3. Objects

Read the objects of the charity in the constitution and check that the activities and fundraising applications fall within the stated objects. If there is a problem it may be necessary to revise the constitution or change the activities of the charity.

21.8.4. Achieving outputs

Is the charity doing what it is being paid to do? Ask for copies of all the funding agreement application forms and letters applying for funding. Make a list of the services that the charity has agreed to provide and a list of what has been provided. What do you still have to provide? Can it be done within the time provided for in the funding agreements?

21.8.5. Budgets

A budget should be drawn up before the start of each financial year and approved by the management committee. If events are significantly different from those forecast then the budget may need revising during the year.

21.8.6. Management committee

The committee needs a report ideally monthly, but at least once every three months, comparing income and expenditure with the budget. This helps to ensure that the charity does not overspend and run out of money during the year.

21.8.7. Trustees

The organisation should have a competent active treasurer and trustees should be aware of their financial responsibilities as detailed in Charity Commission leaflets CC3/CC3a.

<http://www.charitycommission.gov.uk/publications/cc3.asp> and
<http://www.charitycommission.gov.uk/publications/cc3a.asp>

21.8.8. Cash expenditure

Cash income - coins and pound notes - and cash expenditure are the areas where voluntary organisations have the most difficulty. Months after an event organisations can be totally baffled as to how money was spent, or what the total amount of income and expenditure was. Payments by cheque are much simpler because copies of cheques can always be obtained from the bank. Cash expenditure should be kept to a minimum. If it exceeds

£100 a month in an organisation with a turnover of less than £30,000 consideration should be given to what payments could be made by cheque in future.

21.8.9. Petty cash

There should be a lockable cash tin and an account book (or separate page in the bank analysis book) in which details of all cash transactions are recorded. An imprest system should be used. This means the organisation has a float of cash - say £100. When the majority of the money has been spent, say £78.27, the float is topped up again to the original float of £100 by cashing a cheque for £78.27. CASH recommends this system because errors are easily spotted and people can be asked to find missing receipts – bus tickets etc. - or explain why the tin is short of money.

For each payment there should be a voucher signed by the person receiving the money and by the person authorising the expenditure. Check that the vouchers and the cash in the tin add up to the level of the float. If they do not, ask those who have access to the cash tin for explanations. The petty cash book should be balanced with the tin and signed at least once a week. If an imprest system is not used check that the cash paid into the tin equals the expenditure plus the remaining cash in the tin. Start from when the petty cash was last balanced or from the start of the financial year. As with the imprest system there should be a receipt when ever possible and signed vouchers for all expenditure. If checking is a long job or it does not balance consider whether an imprest system would be better. How many people have access to the petty cash tin? If this is more than three people consider if this is really necessary or whether there should be more than one float?

21.8.10. PAYE & Self Employment

If the organisation pays staff then they should receive a pay slip with tax and national insurance deducted. The main form for calculating deductions is the P11. A small sample of these forms should be checked. People who are not paying tax or national insurance must either be below the national insurance threshold and have signed an Inland Revenue form P46 indicating that the work is their only job, or have given the organisation a Self Employed Tax Reference number to prove that they are registered with the Inland Revenue as self employed.

21.8.11. Reserves

The Charity Commission advises charities to have a written reserves policy (See CASHFACTS: Reserves policy). This should cover the funding required to bridge the gap to a new source of funding or allow for an orderly winding up of the charities affairs should this become necessary. Typically a charity might plan to have reserves of between 15% and 25% of annual expenditure.

21.8.12. VAT and corporation tax

Is the charity liable to pay these taxes? The HM Revenue and Customs website at www.hmrc.gov.uk provides full information.

21.8.13 Fundraising strategy

Has the organisation identified adequate sources of income for the next twelve months and does it have a fundraising strategy covering the next three years? Are there enough current fundraising applications taking into account that they will not all be successful and typically it will take four months for a application to be approved or longer for the monies to be drawn down?

21.8.14. Financial controls

Is there a written set of rules covering who can sign cheques etc. (See CASHFACTS: Financial Controls). Do they need to be revised?

21.8.15. Computerised accounts

Is the system functioning well and better than a manual system? Are regular backups made of data?

21.8.16. Insurance

Does the charity have public liability - and if relevant - office contents, employer's liability and vehicle insurance . Consider what other insurances might be needed and whether the amounts covered are high enough. (See CASHFACTS: Insurance Policies)

21.8.17. Pensions

Is there a staff pension scheme, or should fund raising budgets be designed to include the introduction of a pension scheme? (See CASHFACTS: Pensions).

21.8.18. Staff loans

Ask if there are any loans outstanding to individuals. Generally this is not good practice, but loans are sometimes made for annual season tickets. There should always be a written agreement allowing the loan to be repaid through deductions from salary.

21.8.19. SORP

Is the organisation able to produce estimates of expenditure on:

- ❖ Direct Charitable Activities
- ❖ Management and Administration
- ❖ Fundraising.

Can the organisation identify restricted income and charge relevant expenditure to that income? You need to be able to identify expenditure against projects. This can be a simple mechanism – such as photocopies of payslips, invoices etc in the appropriate funder's file.

21.8.20. Stock control

Does the organisation hold significant stocks of items for resale such as books, or are there large amounts of office stationary etc? Bearing in the mind the cost of administration, would it be wise to introduce a stock control system?

21.8.21. Fixed-asset register

Is there a list of the assets owned by the charity with details of cost, depreciation policy, serial numbers and where stored? Typically this list would cover items valued at £100 or more. Is it accurate?

21.8.22. Action plan

Now write a plan with a timetable for rectifying any weaknesses.

21.8.23 Further Information

For further details and examples of other suitable financial health checks, see

a. Charity Commission publication CC8 - Internal Financial Controls for Charities

www.charitycommission.gov.uk/publications/cc8asp

b. Mango's Financial Management Health Check

<http://www.mango.org.uk/resources/healthcheck.asp>

c. Civicus Toolkit – Financial Control and Accountability

<http://www.civicus.org/new/media/Financial%20Control%20and%20Accountability.pdf>

Chapter 22

22. Employment Law and Employing People

22.1. Contract of Employment

22.1.1. Introduction

After its volunteers, a community organisation's employees are its greatest asset: they can complement the work of volunteers at all levels and can provide a degree of stability to the way in which the organisation is managed. The taking on of employees, especially for a community organisation that has not employed anyone before, can seem a daunting proposition particularly when one learns of the length and complexity of employment law, which is constantly changing.

Whether or not the community organisation is incorporated (and if not, it is strictly the members of the management committee who are the employers) management committees need to be aware of the basis of employment law and the potential problem areas. In addition, voluntary organisations are much more likely to be taken to an employment tribunal by disgruntled employees than either the public or private sectors, usually as a result of the voluntary sector employers not following best practice. Even if you win, the legal costs involved can bankrupt your organisation.

22.1.2. Contract of Employment

Once a job applicant has accepted your offer of a job with your community organisation, a contract of employment comes into existence. A contract of employment is a legally binding agreement between you and the employee. The actual terms and conditions of employment may include:

- ❖ Express terms - these are terms that are discussed and agreed between you and the employee
- ❖ Implied terms - these are terms which may include
 - Terms that are too obvious to mention, e.g.
 - That the employee must accept reasonable instructions from the employer
 - Not to steal from the employer
 - Those necessary to make the contract workable (e.g. a person employed to drive must have a current driving licence) although it is better for such terms to be put in writing, and
 - Those that are custom and practice of the community sector, e.g. that the employee is entitled to take part in community activities, or to represent the organisation at external events
- ❖ Terms incorporated by reference - these are terms that exist in other documents (e.g. agreements with trade unions) which are referred to in the contract and to which the employee has access, e.g. on a notice board.

In addition, all contracts of employment are covered by relevant statute law which gives minimum rights to employees, such as the right not to be discriminated against on grounds of age, race, sex or religion.

Note that a contract can exist even though nothing is put in writing and signed.

22.1.3. The Written Statement of Terms and Conditions of Employment

All employees taken on for one month or more are entitled by law to be given, within two months of the date the employment starts, a written statement setting out the main particulars. This statement will not necessarily cover every aspect of the contract, but will constitute important evidence of the principal terms and conditions. The written statement must cover:

- ❖ The names of the employer and the employee
- ❖ The date when the employment (and the period of continuous employment) began
- ❖ Remuneration and the intervals at which it is to be paid
- ❖ Hours of work
- ❖ Holiday entitlement
- ❖ Entitlement to sick leave, including any entitlement to sick pay
- ❖ Pensions and pension schemes

- ❖ The entitlement of employer and employee to notice of termination
- ❖ Job title or a brief job description
- ❖ Where it is not permanent, the period for which the employment is expected to continue or, if it is for a fixed term, the date when it is to end
- ❖ Either the place of work or, if the employee is required or allowed to work in more than one location, an indication of this and of the employer's address; and
- ❖ Details of the existence of any relevant collective agreements which directly affect the terms and conditions of the employee's employment - including, where the employer is not a party, the persons by whom they were made

Where there are no particulars to be given for one of the items required to be covered in the statement (for example, where there is no pension entitlement), this must be indicated.

The statement must also include a note giving certain details of the employer's disciplinary and grievance procedures, and stating whether or not a pensions contracting-out certificate (where the employer has opted out of the government scheme) is in force for the employment in question.

Any documents referred to must be readily accessible during working hours, perhaps kept in the administration office or in a staff handbook.

22.1.4. Who should get contracts of employment?

You should provide a contract of employment no matter what the job or the number of hours involved. Part-time workers are entitled by law to the same rights as full-time workers, and there is proportionate entitlement to the same sickness, holiday terms and pay as fulltime employees. The exception is genuine casual workers, that is, those people who work for you on an occasional basis to whom you offer work but aren't bound to accept it. Typical examples of casual workers are bar staff used on an occasional basis from a pool, who can choose whether to accept work or not, and hall sitters paid to oversee a private function in a community centre on a Saturday night, again subject to their availability.

22.1.5. Casual Workers

Whenever a casual worker works for a community organisation he or she will be an employee and will have some employment rights as follows:-

- ❖ Protection against deductions from wages
- ❖ Protection from discrimination on the grounds of race, sex, disability and religion
- ❖ Protection from discrimination on the grounds of part-time status
- ❖ Rights to be paid at least the national minimum wage, and the right to equal pay
- ❖ Rights regarding working times
- ❖ The right to be accompanied at disciplinary and grievance hearings

In the normal course, once they cease to work for the community organisation they cease to be an employee.

The issue for a community organisation is under what circumstances can a casual worker can gain the same statutory employment rights as regular employees. There are two:-

1. Where there is a global contract covering breaks in work
2. Where any periods of inactivity are classed as temporary cessations of work

A. Global contract

A global contract exists when there is

- ❖ An obligation on the employer to supply work and an obligation on the worker to take it
- ❖ Evidence of an intention on the part of both the employer and the employee to create an employment relationship when the employee was not actually working

B. Temporary cessations of work

In order to determine if a cessation of work by the employee is 'temporary', the whole relationship between the employer and the employee needs to be taken into account. If a casual worker happens to work on an irregular basis (perhaps with long time gaps between work) but is regarded as available at any time to work and expected to turn up when asked, then s/he may become an employee having continuity of employment. If, on the other hand, there is a recognised custom and practice for casual workers to be engaged by a community organisation for particular types of work but without any obligation to do the work, then even a long period of casual working may not result in a continuous employment relationship.

The risk for community organisations if you employ casual workers is that they can drift into a situation when they are working continuously for the organisation or expectations arise on both sides that work will be offered and that it will be accepted when offered. Accordingly, you must keep the employment of casual workers under regular review.

22.1.6. Seconded Workers

Where an outside organisation (e.g. a Local Authority) seconds (i.e. loans) one of their employees to a community organisation, the individual concerned remains an employee of the outside organisation. Such arrangements should always be covered by a written agreement setting out what rights and responsibilities your organisation has in relation to the individual.

22.1.7. Workers whose pay and terms and conditions are handled by another Organisation

Many voluntary organisations already do, and more should, ease the burden of dealing with employed staff by getting an outside body (i.e. a payroll bureau) to handle all the salary payments and other administration arrangements. If you pay for the service, then the staff are your employees, and you are still responsible. If you don't pay, then matters are much less clear-cut, and you need to seek professional advice from a solicitor experienced in employment law.

22.1.8. Length of contract of employment

A contract of employment can be for a fixed term, e.g. for a month or a year, or it can be open-ended, i.e. the employment lasts until such time as notice to quit is given. What is offered depends on the circumstances. For example, where the job is funded by a grant, a community organisation might offer a fixed term contract.

However, note that

- ❖ It is no longer possible to include in a fixed term contract of employment a waiver by the employee of his or her rights to redundancy
- ❖ Many Funders still do not pay for any redundancy payments

22.2. Pensions

There is no requirement for an employer to operate a pensions scheme, or to make any contributions towards an employee's private or personal pension plan, though it is good practice, and perfectly feasible, for community organisations to do the latter. One of the most straight-forward ways to do this is through making contributions towards an employee's stakeholder pension. If you do not make a pension provision, you must say so in the written statement.

22.2.1. Stakeholder Pensions

- ❖ Are low cost, affordable personal pensions aimed particularly at the people who do not have other options available to save for their retirement
- ❖ Are a good option for those currently earning between £10,000 and £20,000 a year, although they may also apply to those earning both more and less than this range
- ❖ Have to meet a number of minimum standards to ensure they offer value for money, flexibility and security
 - Management charges must be limited to no more than 1.5% per annum

- No extra charges can be made if the member stops paying in, or wishes to transfer to another scheme
- Any extra services, and any extra charges not allowed for by law, must be optional. Extra services must be offered under a separate contract with clearly defined charges
- Schemes must provide information and explanatory material to potential members, but will not be required to offer individual financial advice within the 1.5% management charge. Schemes may provide individual advice within the charge limit if they wish, or charge a separate fee
- Existing rebate rates for contracted-out money purchase schemes and appropriate personal pensions apply to stakeholder pensions

All employers must provide access to a stakeholder pension scheme, unless they are exempt.

Exemptions include:

- ❖ Employers with fewer than five employees
- ❖ Employers who offer to contribute at least 3% of basic pay to their relevant employees' qualifying personal pension schemes
- ❖ All employees earn below the national insurance lower earnings limit; or
- ❖ Employers who offers to all employees aged 18 or older (except those within five years of retirement) an occupational pension scheme

An employer who is exempt can still voluntarily provide access, and for community organisations, this is good practice.

Employers have to:

- ❖ Designate (formally choose) a stakeholder scheme
- ❖ Provide employees with information about the scheme; and
- ❖ Make deductions from an employee's salary for their pension contributions to the designated scheme if they want it
 - Employees are not compelled to join stakeholder schemes

Employers are not required to comply from the first day of employment although they will be free to do so if they wish. The requirement becomes mandatory after an employee has been working for an employer for three months.

You are not compelled to contribute into stakeholder schemes on behalf of your employees, but it is good practice to do so. For community organisations, employer's contributions are typically 3% of an employee's earnings.

22.2.2. Further information

For more information on pensions in general and stakeholder pensions in particular see

a. The Pensions Regulator - Pensions choice in the workplace – 2005

- ❖ Frequently asked questions - What you need to know about stakeholder pensions
- ❖ A quick guide for employers about contributions to personal pension and stakeholder pension schemes

<http://www.thepensionsregulator.gov.uk/onlinePublications/guidance.aspx>

b. The Pensions Service (Department for Work and Pensions)

- ❖ A Guide for Employers - Stakeholder Pensions

<http://www.thepensionservice.gov.uk/employer/stakeholder-introduction.asp>

22.3. Changing the Contract of Employment

A contract of employment is binding on both parties, and it is unlawful for one party to vary the terms and conditions in the contract without the agreement of the other. Changing (varying) a contract can have complex

legal implications if not handled properly. Terms in individual employment contracts can be changed validly in the following ways:

- ❖ The employer and employee may agree on the change
- ❖ The contract may provide for changes
 - For example, a contractual mobility clause will allow an employer to move an employee from one workplace to another as long as the employer acts reasonably in doing so
- ❖ Individual contracts may be varied by a union agreement which is binding on individual employees
- ❖ The employer may, by giving the proper period of notice, terminate the existing contract and substitute a new one
 - However, although it is in principle possible to enforce a change without the employee's consent, legal advice should be taken before attempting to do this, as an employee could make a claim of unfair dismissal to an Industrial Tribunal
 - If an employee finds a variation of contract unsatisfactory but nevertheless continues to work under the new terms and conditions without making his or her objections known to the employer, he or she could after a time be deemed to have implicitly accepted it and it would then become incorporated into the contract

If a variation of contract affects one or more of the terms and conditions required by law to be covered in the employee's written statement of employment particulars, then the employee must be given written notification of this not later than one month after the variation is made.

22.4. Disciplinary and Grievance Procedure

There is now a legal requirement on all employees

- ❖ To have in place procedures covering discipline and grievance
- ❖ For these procedures to comply with minimum standards

The minimum standards are set out in DTI publication DISCIPLINARY, DISMISSAL AND GRIEVANCE PROCEDURES - Guidance for employers, aimed at small employers, which is what most community organizations are. If you go beyond these minimum standards, you must ensure that your procedures

- ❖ Follow the codes of good practice set out by the Advisory Conciliation and Arbitration Service (ACAS)
- ❖ Do not reduce your employees rights

It is important that the procedures do not form part of the contract of employment, so that, in the future if your community organisation wishes to make changes it doesn't have to seek your employees' consent (at it would have to do if discipline and grievance procedures formed part of their contract).

22.4.1. Employment Tribunals

(second highest risk to a charities survival)

<http://www.employmenttribunals.gov.uk/default.asp>

The Employment Tribunals are judicial bodies established to resolve disputes between employers and employees over employment rights. These include unfair dismissal, redundancy payments and discrimination. Employment Tribunals also deal with a range of claims relating to wages and other payments. An Employment Tribunal is like a court but it is not as formal; for example, nobody wears a wig or gown. However, like a court it must act independently and cannot give legal advice.

Voluntary organisations are, unfortunately, more likely than either private or public sector organisations to be taken to a Tribunal by a disgruntled or aggrieved employee. Principal reasons for this are their failure either to have discipline and grievance procedures or, more commonly, to have them but not follow them, which is why the topic is introduced in the section on discipline and grievance. Having good discipline and grievance procedures, especially the latter, and following them to the letter are your first line of defence against being taken to an industrial tribunal.

The grounds on which an employee can take an employer to court are many and various, as can be seen from the list below.

a. Grounds for appealing to an Employment Tribunal

- ❖ Suffer a detriment, discrimination, dismissal and/or redundancy
 - Resulting from a failure to allow an employee to be accompanied or to accompany a fellow employee at a disciplinary/grievance hearing
 - On grounds of disability or failure of employer to make reasonable adjustments
 - Resulting from requiring time off for other (non-work but not Health and Safety) duties, study, training or seeking work
 - For claiming under the flexible working regulations or be subject to a breach of procedure
 - For health and safety reasons
 - On grounds of pregnancy, child birth or maternity
 - Related to failure to pay the minimum wage or allow access to records
 - Due to exercising rights under the Tax Credits Act
 - Relating to being, not being or proposing to become a trade union member
 - Due to requesting or taking paternity or adoption leave or time off to assist a dependant
 - Due to exercising rights under the Public Interest Disclosure Act
 - For refusing to work on a Sunday
- ❖ Application
 - For a declaration that the inclusion of discriminatory terms/rules within certain agreements or rules causes the aforesaid to be invalid
 - By an employee, their representative or trade union for a protective award as a result of an employer's failure to consult over a redundancy situation
 - By the Secretary of State for Trade & Industry to prohibit a person from running an Employment Agency
 - By an employee that an employer has failed to pay a protected award as ordered by a tribunal
 - For interim relief
- ❖ Breach of Contract
- ❖ Failure of the employer
 - To consult with an employee representative or trade union about a proposed contracting out of a pension scheme
 - To provide equal pay for equal value work
 - To consult with an employee rep. or trade union about a proposed transfer
 - To allow time off for trade union activities or duties, for ante-natal care or for public duties
 - To provide a guarantee payment
 - To pay remuneration whilst suspended for medical reasons
 - To allow time off to seek work during a redundancy situation
 - To comply with an award by a tribunal following a finding that the employer had previously failed to consult about a proposed transfer of an undertaking
 - To provide a written pay statement or an adequate pay statement
 - To provide a written statement of reasons for dismissal or the contents of the statement are disputed
 - To pay for or allow time off to carry out Safety Rep duties or undertake training
 - To pay remuneration whilst suspended from work for health and safety reasons whilst pregnant or on maternity leave
 - To provide a written statement of terms and conditions and any subsequent changes to those terms

- To prevent unauthorised or excessive deductions in the form of union subscriptions
- To pay a redundancy payment
- To pay, or unauthorised deductions have been made
- To limit weekly or night working time, or to ensure rest breaks or annual leave entitlement
- ❖ Failure by the Secretary of State for Trade and Industry
 - To make an insolvency payment in lieu of wages and/or redundancy
 - To pay a redundancy payment following an application to the National Insurance fund
- ❖ Discrimination or victimisation on grounds of
 - Religion or belief
 - Sexual orientation
 - Race or ethnic origin
 - Sex, marriage or transgender
- ❖ Loss of office as a result of the reorganisation of a statutory body
- ❖ Appeals against
 - The levy assessment of an Industrial Training Board
 - An enforcement, improvement or prohibition notice imposed by the HSE or Environmental Health Inspector, or by the Environment Agency
 - An enforcement or penalty notice issued by the Revenue and Customs
 - A non-discrimination notice issued by either the CRE, DRC or EOC
- ❖ Suffered less favourable treatment and/or dismissal
 - As a fixed term employee, than a full time employee
 - As a result of being a part time employee by comparison to a full time employee
 - As a temporary employee than a full time employee
- ❖ Suffer discrimination in obtaining
 - Employment due to membership or non-membership of a trade union
 - The services of an employment agency due to membership or non-membership of a trade union
- ❖ Unfair dismissal
 - After exercising or claiming a statutory right
 - On grounds of capability, conduct or some other general reason including the result of a transfer of an undertaking
 - In connection to a lock out, strike or other industrial action

If you employ people, and both they and you are not always models of sweet reasonableness, and you don't have on your management committee and staff a human resources expert, sooner or later you could end up before an industrial tribunal. If you do, the procedure to follow, from an industrial tribunal viewpoint, is set out at: http://www.employmenttribunals.gov.uk/pdfs/english/Responding_to_a_Claim-1479.pdf. Being taken to an industrial tribunal is therefore a significant risk for any community organisation, and needs to be managed. For most community organisations, this will involve taking out legal expenses insurance, which is discussed more fully in the section on insurance. Your insurers legal advisers will expect you to involve them at every stage of an issue potentially leading to an industrial tribunal, and to take their advice, even if unpalatable. It is, unfortunately, often cheaper to buy off a trouble-maker rather than face an industrial tribunal, where even when you win your legal fees will be considerable. Having principles may be something you cannot afford.

That said, the threat of an industrial tribunal should never be used as an excuse not to manage, or to tolerate ill discipline or poor performance. The Advisory Conciliation and Arbitration Service web site at www.acas.org.uk contains a wealth of information and advice on how small employers should manage staff where there are discipline and performance issues, and they have e-learning courses covering many of the topics outlined in this chapter, not just discipline and grievance.

22.5. Minimum wage

With certain specified exceptions, employers, and that includes all charitable, voluntary and community organisations, have to pay all their workers, whether full time, part time or casual, at least the National Minimum Wage (NMW), expressed at a rate of pay per hour, The rates are:-

- ❖ For 'adult' workers (aged 22 and over)
 -
 -
 - £5.35 per hour, from October 2006
- ❖ For 18 - 21 year olds
 -
 - £4.45 per hour, from October 2006
- ❖ For 16 and 17 year olds (above compulsory school age, the precise definitions of which vary according to whether the person is in England and Wales, Scotland or Northern Ireland)
 - £3.30 an hour Full-time workers, part-time workers, casual workers, freelance workers, temporary workers, agency workers, retired people and pensioners (if working) are all eligible.

22.5.1. The specified exceptions are:-

- ❖ Modern Apprentices who are either
 - over 19 and are within the first 12 months of starting work with the employer, or
 - Under 19.
- ❖ Those participating in a scheme designed to provide them with training, work experience or temporary work, or to assist them in obtaining work which is either
 - A Government scheme (other than a Modern Apprenticeship) or
 - Funded in whole or in part under the European Social Fund
- ❖ Those attending higher education courses (up to first degree level) who are required as part of such course to do work experience of up to one year.
- ❖ Homeless persons or those residing in hostels for homeless people who do work for a charity or other non-profit organisation in return for shelter and other benefits.
- ❖ Independent contractors and self employed people who do not work under a contract of employment
- ❖ True volunteers

Employers cannot seek to avoid paying the minimum wage either by using workers without entering into a contract of employment or by claiming that they are volunteers, and therefore that what they are paid aren't wages. Either they are volunteers, and receive no remuneration, or they are workers, and receive at least the minimum wage. Also, employees cannot voluntarily agree to accept less than the minimum wage, even where they work for a charity or community organisation.

As with all matters to do with employment law, the rules and regulations are exceedingly complex, none more so than when it comes to working out whether or not you are paying the national minimum wage. In outline, all wages payments have to be determined with reference to a 'pay reference period'. If a worker is paid weekly, the pay reference period is a week; if a worker is paid monthly, the pay reference period is a month. The worker does not have to be paid the NMW for each hour worked but must be paid the NMW on average for the time worked in the pay reference period.

22.5.2. Calculating pay for minimum wage purposes

When calculating pay, you must include

- ❖ PAYE and employee's NI deductions
- ❖ Incentive payments and bonuses,
- ❖ Deductions to repay advances for travel and wages and recover accidental overpayment of wages

- ❖ Union subscriptions, Save As You Earn , Court attachment of earnings, all of which aren't for the employer's benefit.
- ❖ Deductions for accommodation (but special rules apply).

and exclude

- ❖ A loan to the worker
- ❖ An advance of wages
- ❖ A pension payment
- ❖ A lump sum on retirement
- ❖ A redundancy payment
- ❖ A reward under a staff suggestions scheme
- ❖ Overtime and shift premiums, and other special allowances paid over and above normal pay e.g. for working unsocial hours or in a particular area
- ❖ Refund of expenses
- ❖ Uniform or tools provided by the employer for the job
- ❖ Meals provided by the employer and other benefits in kind

Where a community organisation provides accommodation for worker, typically a caretaker, it may make a specific deduction for accommodation from the worker's pay; or charge a specific amount once the worker has received his or her pay, or even provide accommodation on an uncharged basis as part of a remuneration package. However, when taking into account these deductions, or the value of the accommodation, if provided without charge, the maximum amounts which can be counted are:-

- ❖ Daily rate - £ 4.15 for every day accommodation is provided in the pay reference period
- ❖ Maximum offset - £29.05 a week

There is nothing to prevent a community organisation deducting or charging more than this, but any higher amounts cannot be counted towards the NMW.

As a result, it is no longer possible for a community organisation to provide "accommodation for duty", or "accommodation for duty plus pocket money" (that is paying no wages or a small wage but allowing the worker, to occupy rent-free, or perhaps for a small rent). For example, if a caretaker is paid £50 a week for working 16 hours a week, with accommodation (including heating and lighting) provided rent-free, the caretaker is being underpaid, since £5.35 an hour times 16 hours = £85.60, and £85.60 minus £29.05 (the maximum offset) = £56.55. If, however, the caretaker is paid £6 an hour, but has £50 a week deducted for rent, her or she is still being underpaid, since £6 times 16 less £50 is £46, to which must be added the £29.05 maximum offset, giving a wage for NMW purposes of £75.05, still less the permitted £85.60 minimum.

22.5.4. What are Hours of Work for NMW purposes?

As with deductions and admissions, the rules regarding what constitutes hours of work are complex and confusing. For a start, it depends on whether the worker is doing time work, salaried hours work; output work or unmeasured work.

Output work (i.e. 'piece work') is unlikely to apply to community organisations, and isn't discussed further here.

Time Work is work that is paid for according to set or varying hours or periods of time – waged as opposed to salaried employment. It makes no difference whether the worker is part-time, full-time, casual or permanent.

A time worker must be paid at least the NMW for the times when:

- ❖ He/she is at work and required to be at work. It makes no difference whether or not work is actually provided for that time, or if he or she are unable to work because equipment or machinery has broken down.
 - Time when a worker is absent from work (for example, rest breaks, tea breaks, lunch breaks, sick leave and holiday) does not count as hours of time work.

- ❖ He/she is on standby or on-call at or near the place of work, unless
 - His/her home is at or near the place of work and the time is time he/she is entitled to spend at home (i.e. during periods of rest)
 - He or she is permitted to sleep, and is asleep

Employees on call, on stand-by, and especially asleep at work in accommodation provided for that purpose, constitute a particularly complex area, and specialist advice should be sought if this becomes necessary

- ❖ He/she is travelling in connection with his or her work during normal working hours or the normal range of their hours, unless
 - The travelling is incidental to a worker's duties
 - The travelling is between the worker's home and his/her place of work
 - e.g. Travel from work to a place of training counts as time when the national minimum wage should be paid. But travel between home and a place of training does not count

Salaried Hours Work is where a worker:

- ❖ Is paid under a contract for a set basic number of minimum hours in a year, and
- ❖ Is entitled under his or her contract to an annual salary, and
- ❖ Is paid in equal instalments.

This includes those who work only part of the year, e.g. playgroup or caretaking staff.

The rules are, broadly speaking, the same as for time work, except that hours of absence are included, if the worker is paid his/her normal pay when he or she is absent. i.e. if they form part of the worker's basic minimum hours under their contract of employment, rest breaks, lunch breaks, holidays, sick leave or maternity leave. The only hours that do not count are:

- ❖ Periods paid at less than normal pay, for example where contracted pay is reduced after a set period of sick leave
- ❖ Unpaid leave, including sabbaticals
- ❖ Industrial action

Salaried hours workers are not usually entitled to overtime pay. If overtime is worked, then this must be added to the basic contracted hours when calculating whether the worker is receiving the NMW. What it means in practice is that where the equivalent hourly rate of pay does not greatly exceed the NMW, time worked in excess of the contract minimum may result in the actual hourly rate of pay falling below the NMW. If overtime is paid, then the worker is treated as if he or she was doing time work for those hours, and there is no need to do a special calculation. If you do not pay overtime but allow workers to take time off in lieu (TOIL), you are still required to ensure that you pay salaried hours workers at least the NMW for the hours they actually work.

Unmeasured Work is work where there is a task to be done but no set hours for the task. The employer requires the worker to take the job and complete the task, but the hours taken to do this aren't specified and may vary from one pay period to the next. For community organisations, typical examples are where someone is paid a fixed amount per session, but the session is of variable duration, depending on the activity or task. To comply with the minimum wage rules, employers must first identify the number of hours to be worked and for which the NMW is to be paid. There are two options for doing this:-

- ❖ Coming to an 'average' agreement of hours to be worked; or
- ❖ paying the NMW for every hour actually worked

The average must be

- ❖ Agreed in writing with the worker before the start of the pay reference period
- ❖ Set out the average number of hours that the worker will take
- ❖ Realistic.

Since travel time must be paid for in the same way as for time workers, this (if relevant) must be included in the average.

22.5.5. Record Keeping

Employers are required to keep sufficient records of payments to workers to establish that they are paying the NMW, to which employees have the right of access. Where rates of pay are well above the NMW, the employer's payroll (PAYE and NI) records should be sufficient. However, the closer to the minimum an employee's gross pay is, and the longer the employee works in a pay reference period, the greater the risk that they could be paid below the NMW, and the more detailed the records must be. The DTI's recommendations for more detailed records are:-

- ❖ The pay reference period
- ❖ Gross pay paid to the worker
- ❖ Any travel or training during work hours and its length
- ❖ Overtime/shift premiums
- ❖ Amount of unconsolidated allowances
- ❖ Any benefits received by the worker
- ❖ Any deduction or payment for accommodation
- ❖ Amount of tips given to the worker through the payroll
- ❖ Amount of NMW pay calculated
- ❖ The total number of hours worked or 'fair estimate' or 'daily average' of hours to be worked
- ❖ Any absences, for example, rest breaks, sick leave, holiday
- ❖ Bank statements or other commercial documentation

Records must be kept for a minimum of three years, and it is up to the employer to prove that they have paid at least the NMW, if challenged.

22.6. Working Time Regulations

In essence the Regulations, which are classified as health and safety measures

- ❖ Set a working time limit (including overtime) of
 - 48 hours in any 7 days.
 - Calculated as an average over a 17 week period.
 - Written agreements can specify when the 17 week periods are to run, or if not specified it can be any 17 weeks which are consecutive
 - If the worker has worked less than 17 weeks then the average will be taken over that period
- ❖ Require employers to take all reasonable steps, in keeping with the need to protect the health and safety of workers, to ensure that this limit is not exceeded
 - However, the 48- hour maximum working time rule can be waived by agreement between an employer and its workers. Where an employer and employee have agreed to an opt-out , the employer must maintain records that
 - Identify the workers who have agreed that the limit should not apply,
 - Set out relevant terms
 - Specify the number of hours worked by each worker since the agreement came into effect
- ❖ Specify requirements for daily and weekly rest periods and rest breaks at work
 - If a worker works longer than 6 hours then the worker is entitled to an uninterrupted rest break of 20 minutes during which the worker is entitled to be away from his/her workstation
 - Not less than 11 consecutive hours rest in each 24 hour period
 - 24 hours in each 7 day period; or
 - Uninterrupted rest periods of not less than 24 hours in each 14 day period; or
 - 1 uninterrupted rest period of 48 hours in each 14 day period

The 7 day period will either be provided for in the worker's contract of employment or a collective agreement. In the absence of a written agreement this will be the start of the working week

- Where 14 day periods are used, the periods commenced on 5 October 1998 or the start of the week in which employment began after 5 October 1998, or by agreement
- The weekly rest period should not include any part of a daily rest break unless objectively justified by technical reasons or reasons concerning the organisation of the work
- ❖ Grant a statutory right to paid annual leave
 - A minimum of 4 weeks paid annual leave.
 - There is no statutory entitlement to exclude bank holidays from the 4 weeks. i.e. bank holidays can count towards the 4 week annual leave)
 - Part-time workers and sessional workers are entitled to paid annual leave on a pro rata, or proportionate, basis
 - Leave entitlement accrues at the rate of one-twelfth(of the entitlement) for each complete month's employment
 - Leave can be taken in instalments but there is no right to carry over and the employer cannot pay in lieu of leave, unless the worker's employment is terminated
 - Workers are entitled to be paid in lieu where they are owed leave on leaving. Workers will have to compensate employers where they have taken more than their entitlement on leaving
 - Workers can take any of their annual leave by giving notice (not necessarily in writing). However this does not give the employee the overriding right to take the leave since an employer can require an employee not to take such leave by notice
- ❖ Require employers to keep records of weekly hours worked by all employees
- ❖ Give specific protections for night workers including health and safety assessments
 - A night worker is someone whose working day involves regularly working 3 hours or more per night
 - Night is 11 pm to 6 am
 - There are special rules for young workers (under 18)
 - Community organisations don't generally employ night workers, so the rules applying to them aren't discussed further here

22.6.1. Issues for Community Organisations

a. Who is a worker?

The definitions of who is a worker, and therefore covered by the regulations, are the same as for the National Minimum Wage (NMW). As with the NMW, employers cannot seek to avoid the regulations by trying to use workers without entering into a contract of employment.

b. The 48 Hour Week

The maximum 48 hour week, while being an important health and safety issue, is in practice unlikely to be a problem for most community organisations. This is because the 48 hour rule only applies as an average over a 17-week period.

c. What is Working Time?

'Working time' is defined as when a worker is:

- ❖ Working
- ❖ At his or her employer's disposal, and
- ❖ Carrying out his or her employer's activities and duties

All three elements must be satisfied for time to be 'working time'.

- On-call time only counts when a worker is at his/her work-place
- Lunch (except a working lunch) and similar breaks do not count
- Time spent travelling as part of a worker's duties counts
- Time spent travelling to work does not count

Where there is any doubt, you should come to an agreement with your employees to add to these definitions (which is permitted by the Regulations).

d. Bank Holidays

There is currently no statutory entitlement for workers either to take bank holidays as holidays, or for these to be paid holidays. Accordingly, you could count bank holidays as being an integral part of the 4 weeks annual paid leave under the regulations, though in practice, most community organisations do treat bank holidays as additional holidays, with pay, granting days off in lieu where someone has to work over a bank holiday.

e. Annual closures

There is nothing to stop a community organisation requiring staff to take some or all of their annual leave entitlement at a time of their choosing, in order to have an annual closure or closures. Indeed, closing a community building for a period each year at a time when activities are at a low ebb can make good sense. However, you cannot suddenly start doing this, without getting the agreement of the staff concerned, where holiday entitlements and rules are set out in their contracts of employment.

f. Leave and Part-time Workers

In principle, part-time workers are entitled to paid annual leave pro-rata. In practice, calculating this can be problematic, and a bone of contention, especially if (as is usual) bank holidays are also granted as paid leave. If a part-time worker works mornings only, or any day of the week, except perhaps Mondays, then the calculations are straight-forward. However, if they work term times only, then matters become more complicated. The issue isn't usually the time taken off, but the holiday pay. To give an example. Some of your staff work all the year round, and some term times only. If you have any sense you will specify that your term time workers take their holidays during the school holidays, so the issue becomes one of how to calculate holiday pay. In practice, many community organisations will pay their term time only workers 4 weeks pay, at the term time rate. However, if you do the mathematics, such staff are being paid more pro-rata than full time staff, who when they find out, aren't happy. The mathematics is as follows:-

A full time worker works 48 weeks a year and gets 4 weeks holiday. Thus, they accrue holiday and holiday pay at $4/48$ (or $1/12$) per week. A term-time worker working 39 weeks should accrue holiday and holiday pay at the $1/12$ rate, so over their working year they should get $1/12 \times 39 = 3 \frac{1}{4}$ weeks holiday and pay.

You can do similar sums with similarly penalising outcomes for full time staff if part-time staff work only Mondays, and you pay for bank holidays on top of the 4 week statutory entitlement – Mondays because most bank holidays fall on a Monday. For example, assuming that at least 5 bank holidays fall on a Monday, a part-time worker working Mondays only will have their 4 Mondays off, with pay, as part of their statutory entitlement, and another 5 Mondays off, with pay, for bank holidays, giving them 9 weeks holiday a year, with pay, compared to the full time worker, with a maximum of 6 weeks off (4 weeks statutory, and 2 weeks for the 10 bank holidays a year) with pay!

g. What if a worker has more than one job?

Employers are required to take all reasonable steps to ensure that their workers do not exceed an average of 48 hours of weekly working time. Thus, you should ask the worker whether they are working elsewhere (or include in their contract a requirement that they notify you when getting other work) and, if the hours exceed the maximum, then arrange an adjustment of the hours accordingly regarding either the time s/he spends working for you or for their other employers. If the worker refuses to accept or to work to an agreed adjustment of hours, then you should agree with them to opt out of the 48-hour limit.

h. If a worker takes work home, does this count as working time?

Only if this had been previously agreed with their employer. Hence, when a worker does so on his/her own initiative and either is not required to do so or has not agreed this with his/her employer, the time does not count

as working time. If you want to put this on a regular footing, you should make an agreement to add working at home to the definition of working time.

i. What if a worker works through their rest breaks?

You must allow your workers the rest breaks required by the regulations, and should do all you can to encourage workers to take the breaks to which they are entitled, but you cannot compel them to take the breaks, if they choose voluntarily to work through them

22.7. Further information

Community Matters Information Sheets:-

No 17 Disability Discrimination Act 1995

No 19 Equal Opportunities

No. 53 Recruitment

No. 54 Contract of employment

No. 55 Managing Employees

No. 56 Individual Rights of Employees

No. 57 Termination of Employment

No. 58 National Minimum Wage

No. 59 Working Time Regulations

Your guide to the Working Time Regulations: sections 1 - 4.

URN No: 06/1908A

<http://www.dti.gov.uk/employment/employment-legislation/employment-guidance/page28978.html>

Your guide to the Working Time Regulations: sections 5 - 11.

URN No: 06/1908B

<http://www.dti.gov.uk/employment/employment-legislation/employment-guidance/page28979.html>

Employing People – a handbook for small firms (ACAS/H01)

Published by ACAS @ £4.95

<http://www.acas.org.uk/>

MATERNITY RIGHTS

Babies due on or after 6 April 2003

A GUIDE FOR EMPLOYERS AND EMPLOYEES

<http://www.dti.gov.uk/files/file18061.pdf>

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Chapter 23

23. Insurance

Getting the right insurance policies, and the right level of cover, is an important part of managing both your money and your risks. It only takes one break-in at uninsured premises to leave a community group virtually helpless, without the resources to replace stolen equipment or to repair damage. Under-insurance can be as bad as no insurance, since at best the insurance company will only pay out a proportion of the loss and at worst may refuse to pay anything. Also, whatever you do involves some risk, and we live in a world where people and organisations are increasingly likely to take your organisation to court.

Householders can cover most, if not all, of their risks with only 4 policies, covering

- ❖ Buildings
- ❖ Contents
- ❖ Motor vehicles
- ❖ Travel

and so it is with community organisations purchasing “all in” policies or bundles of insurances, provided that the bundles are designed specifically for charities, community organisations or groups managing community buildings. In general, a bundle purchased through a broker specialising in community organisations is usually the best option, but these need to be carefully checked to make sure that each section is suitable for your group, that all risks are covered and that the small print doesn't exclude risks which you need to cover, or limit the insurer's liability.

23.1. Mandatory

The only two insurances which are required by law are

- ❖ Employer's liability
- ❖ Motor vehicles

So if you don't employ staff, or run a motor vehicle, you don't have to be insured, though not to do so would be fool-hardy at best and, if your organisation is a charity, a serious breach of trust.

23.1.1. *Employer's liability*

If you employ staff you must by law take out employer's liability insurance. This should cover liability for injury or disease sustained by your employees arising out of their employment. The cover must be for at least £2 million and the insurance certificate must be displayed on the employer's premises. If you have volunteers, you should, if possible, cover them under the policy.

23.1.2. *Motor insurance*

If a voluntary organisation owns or hires a vehicle then a motor insurance policy must be held by the organisation. If the organisation's employees use their own vehicles on the organisation's business or activities then either the employee's own policy must cover business use, or the organisation's own insurance must cover the employee's vehicles (which might give rise to a taxable benefit). You should ask to see your employee's motor insurance policies to check that business use for their employer is covered. To ensure your group won't suffer financially if an employee or volunteer with inadequate motor insurance has an accident, you should take out a Contingent Liability policy against such an event.

23.2. Optional, but essential

Other insurances which whilst not compulsory are essential for a community organisation managing a community building are:-

- ❖ Public Liability Insurance
- ❖ Building Insurance
- ❖ Contents Insurance

- ❖ Legal expenses insurance

If your organisation gives advice, even if this is free, you will also need

- ❖ Professional indemnity insurance

If your organisation handles large amounts of cash (as it may do if there is a licensed bar on the premises, you should consider

- ❖ Money insurance

23.2.1. Public liability insurance

This covers personal injury or death to members of the public and damage to their property caused by the activities or negligence of your employees and volunteers. Public liability insurance should also cover death, injury and damage to property arising from ownership, occupation or management of premises.

23.2.2. Buildings insurance

If you own our buildings, this will cover damage to your building from fire, storm or subsidence. Be sure that the sum insured is enough to cover rebuilding and fees like architects and surveyors.

If you are leasing the building, the landlord is usually responsible for insuring it, but you need to check your lease or licence in case it is your responsibility. Check also that the landlord's policy covers a reasonable period for loss of rent (for example 2 years) so you do not have to pay rent while the building cannot be occupied, and that liability is divided between landlord and tenant so that, for example, if the tenant carried out improvements and these are destroyed then tenant is reimbursed for the cost of the improvements out of the insurance.

23.2.3. Contents insurance

This covers loss or damage to contents including office equipment, computers, stock and employees belongings, from fire, explosion, flood and theft. Make sure that you meet any security conditions required by the insurer such as doors of a certain thickness, bars on ground floor windows, security systems, or locks to a specific standard. If you fail to meet the insurers requirements, the insurer may refuse to pay if you make a claim. You may find that insurers won't cover you for theft unless there has been a forced entry.

Don't forget to include any equipment, such as a photocopier, which you lease, and it may be worth considering an "all risks" policy, which may cost a bit more but should cover your equipment even when it's not on your premises.

You need to weigh up whether to insurance the contents on a historic cost basis, in which case the insurance company will only pay out what the items cost when you purchased them, or whether to pay extra to insure them at replacement value, in which case the insurance company will pay out what it costs to replace items at today's prices.

Always keep receipts for insured items, and make sure that if you have insured at replacement value you know how much it would cost to replace all your equipment, so that you keep an adequate level of cover.

23.2.4. Legal expenses insurance

There are a range of insurances covering various types of legal costs. They include protection if you are sued and the costs of suing another organisations if you have a genuine claim or grievance against them. Of these, the most important from the point of view of a community organisation employing staff is employment disputes insurance.

Employment disputes insurance covers costs relating to industrial tribunals and compensation awards made by tribunals. Voluntary organisations are much more likely than either private or public sector employers to be taken to industrial tribunals by disgruntled employees (and even volunteers seeking employee status), and given the costs involved in being legally represented at a tribunal (and not to be legally represented would be fool-hardy), even a successful defence could bankrupt your organisation.

The advantages of this type of insurance are that not only will your costs and any compensation awards be covered but also you have support from experienced professionals. The insurance company will require that you inform them immediately a problem arises and follow the advice of their staff exactly, including adopting and following their prescribed discipline and grievance procedure. The disadvantage is that the insurance company take over some of the management decision making of the group. For example, you as a management committee might want to fight a meretricious or malicious complaint to an industrial tribunal, on a point of principle, but the insurance company want to “buy off” the complainant by settling “out of court”, because this will be much the cheapest course of action. Typically you cannot make claims in the first six months because the insurance companies do not want to meet the cost of existing disputes. They are covering new disputes and grievances only.

23.2.5. Professional indemnity insurance

This covers the risk that a supplier of services may not comply with its legal duties, so if your organisation provides advice, publishes advice in a newsletter, on a website, or runs training courses, then this policy should cover claims for loss arising from bad advice, even if this advice was free.

23.2.6. Money Insurance

This will cover your organisation for loss of cash, due for example to theft, if you hold significant amounts of cash on the premises, or whilst it is in transit to or from the bank, and, optionally, if the organisation’s money is sometimes kept in a management committee member’s house.

There are a whole range of other insurances which might be worth considering, including

- ❖ Personal accident, which covers accidents that could not be claimed for under public liability insurance, such as accidents that are not a result of the organisation’s negligence
- ❖ Fidelity bond insurance insures against employees stealing from the charity
- ❖ Increased cost of working or business interruption allows you to rent temporary premises while your damaged premises are being repaired following fire or flood, and to cover other additional costs such as installing telephones, printing temporary letterheads, moving costs and possibly loss of income due to your stopping activities for a time
- ❖ Events insurance can cover the risks associated with a one-off event, such as a fun day policies. You can even ensure against rain spoiling your open-air fundraising event, though such a Pluvius policy needs to be taken out at least 3 weeks before your event takes place.

23.3. Other Optional Insurances

A further policy which many unincorporated associations concerned at the unlimited liability status of their management committee members purchase is trustee liability insurance. Where trustees (the management committee of a charitable community organisation) act negligently, or in breach of their duties as trustees, such as spending funds on objectives outside those specified in the constitution or specified by a funder, it is possible for them to incur personal financial liabilities. On the face of it, this type of insurance appears to offer peace of

mind, particularly to trustees who own their own houses and are bringing up children, who would be affected by a significant payment of damages from the family's funds. However, if the trustees have acted with due diligence in a reasonably well managed charity, then the risk of being held liable by a court is low, and since the insurance won't cover actions that are unlawful (like acting outside constitution) or negligent (including regularly failing to turn up for trustee meetings, and failing to seek or take professional advice), the cover actually provided is more illusory than real, and may be poor value for money. Since trustee indemnity insurance is a trustee benefit, a charity will need not only to have the power in its constitution to take out such a policy but also the permission of the Charity Commissioners to exercise the power.

Other points to consider are

- ❖ Trading companies
If your community organisation has a connected trading company or subsidiary then the trading company will be an entity in its own right and will normally need its own insurances.
- ❖ Funders
Some funders insist that you have certain insurances, for example, local authorities often require you to take out public liability insurance. Check insurance requirements when you apply for funds and when you read the funding agreement.
- ❖ Disclosure
You must disclose to the insurer all material facts of which you are aware. Inform the broker or insurance company of any events that are likely to affect the level of risk. This would include taking on more employees or volunteers, or a break in even if you do not claim for loss resulting from the break in.
- ❖ Volunteers
You need to check that both your employer's liability insurance and public liability insurance cover volunteers. Both must explicitly mention volunteers if they are to be covered,

23.4. The bottom line

Be realistic in your expectations of what to pay for insurance. The days when insurers were prepared to subsidise insurance premiums for charity and voluntary groups out of the profits from their investments are long gone, and adequate cover is no longer cheap. When groups complain they can't get insurance, what they often mean is that they can't get insurance at a price they are prepared to pay. When choosing an insurance policy always get two or three quotes for comparison - its surprising how rates can differ between insurance companies, and agreeing exclusions - statements about what is not covered - or excesses – the amount you have to pay for the first part of any claim - can save several hundred pounds. However, consider any exclusions carefully, in the context of how appropriate the insurance is for your situation. And agreeing an excess may require you to pay the first £500 (or more) of any claim.

23.5. Check list

Before taking out insurance consider the following:

- ❖ Is the insurance compulsory or required to meet the needs of funding agreements?
- ❖ Is the insurance necessary or prudent? Does the person recommending it understand the charity's activities or are they seeking to earn commission by selling insurance that you do not need?
- ❖ What risks are covered by the policy?
- ❖ What risks are excluded?
- ❖ Does the quotation cover everything?
- ❖ Does the quotation cover more than is needed?
- ❖ How much is the premium, do you have a second quotation from another broker?
- ❖ Has the proposal form been completed in full? (The doctrine of utmost good faith requires that the insured tells the insurer of all material facts that the insured is aware of).
- ❖ What are the conditions of the policy? For example, do door locks need to be of a specific standard?

Remember to:

- ❖ Renew the insurance on time. Put a reminder in your diary/planner
- ❖ Promptly advise insurers of any significant change in the risk
- ❖ Notify insurers of all claims under any insurance policies
- ❖ Review insurance once a year, typically in January if policies renew in April so you have enough time to get alternative quotations

Check for:

- ❖ Double or overlapping insurances
- ❖ Level of cover
- ❖ Risks covered
- ❖ Risks faced by the charity

23.6. Brokers

The following insurance brokers have particular experience of insurance for voluntary sector organisations.

For those running community buildings, Community Matters should be a first point of contact.

Aon Risk Services, Trinity Court, 2/4 West Street, Fareham, Hants, PO16 0BH.

Tel: 08457-697504

AON Limited, Capital House, 1 Houndwell Place, Southampton, Hampshire, SO14 1HU. 0845 7402003
www.aon.com/uk/en/default.jsp

Ladbroke, Freepost NEA9003, Sheffield, S25 3ZZ. Tel 01909 565858

No limit on public liability. Generally no limit on employer's liability but, depending on the type of work, a limit may be placed of only covering people up to 70 years old. Personal accident has an age limit of 16-70 that may be extended to 75 in certain circumstances.

Stuart Alexander, 10 Philpot Lane, London, EC3M 8AB. Tel: 020 7335 1646.

There is no age limit for employer's liability and public liability. For personal accident there is no lower age limit, but there is an upper age limit of 75.

The Encompass Policy.

Keegan and Pennykid Insurance Brokers, 50 Queen Street, Edinburgh, EH2 3NS.

Freephone 0800 731 8030. Freefax 0800 731 8448. Email: mail@keegan-pennykid.com

Zurich Municipal's Community Insurance Centre in Southampton (08457 254 910) was recommended to us as having found cover for one organisation that was cheaper than they had originally been paying.

Independent Advice Services, 12th Floor, New London Bridge House, 25 London Bridge Street, London SE1 9ST. 020 7407 4070
www.advicenow.org.uk

23.7. Further Information

Community Accountancy Self Help Facts Sheet – Insurance
www.cash-online.org.uk/cashfacts

Getting the best insurance deal

<http://www.ncvo-vol.org.uk/?id=492>

Chapter 24

24. Management committee financial responsibilities

24. 1. The Role of The Treasurer

In principle, responsibility for managing the finances of a charitable community organisation is shared equally by all members of the management committee. In practice, the treasurer takes prime responsibility, though every other committee member should, indeed must, take an interest in the organisation's finances. If your treasurer is the only committee member taking responsibility for your community organisation's financial affairs, this is an unhealthy situation. Your treasurer would have an over-powerful role within your organisation, since the other committee members would not have the information to challenge the way that the organisation was being run, or be in a position to suggest alternatives.

In small community organisations, the treasurer will keep all the organisation's financial records. In larger organisations this will not be practicable and some of the treasurer's work will either be shared with other committee members, staff or volunteers, or be undertaken by a paid finance officer. In these arrangements, the treasurer will have a supervisory role.

Whether the treasurer works alone, with other volunteers, or with paid staff her or his responsibilities are the same:

- ❖ To ensure the organisation has in place a set of financial policies, including financial controls and reserve and these are reviewed annually
- ❖ To make sure that the finances of the organisation are handled properly
- ❖ To ensure that
 - Money is only spent in accordance with the organisation's purpose
 - Any money given to the group for a specific purpose is
 - Spent only on that specific purpose
 - Accounted for separately
- ❖ To make sure that
 - All income due is received
 - Receipts are issued for all money received by the group, including subscriptions
- ❖ To ensure that
 - All bills are paid
 - Receipts are obtained for all payments made by the group
- ❖ To make sure that the analysis books and records of all the group's financial transactions are kept up to date
- ❖ To act as one of the cheque signatories (there should be a pool of 4)
- ❖ To ensure that
 - Regular and accurate bank reconciliations take place
 - Money held on deposit earns a good rate of interest
 - Appropriate insurances are maintained
- ❖ If the organisation employs staff, to ensure
 - That the management committee is fully aware of all issues relating to employing staff, engaging contractors and paying expenses to volunteers
 - HM Revenue and Customs regulations are complied with and that all returns are made on time so that fines are avoided.
 - For sessional or contract staff, that they are either taxed, or can pass HM Revenue and Customs "employed or self employed?" test
- ❖ Before the start of each financial year,
 - To prepare the annual budget, forecasting incomings and outgoings for a year ahead, and a cash-flow forecast, for approval by the management committee
- ❖ To prepare budgets for specific projects and for fundraising

- ❖ At each and every meeting of the management committee,
 - To report to the management committee on the financial position of the group
 - Comparing actual incomings and outgoings with budgeted incomings and outgoings, showing the variance (difference) between the two
 - Making recommendations for corrective action, where necessary
- ❖ At the end of each financial year, to make sure
 - That either a Receipts and Payment Account and Statement of Assets and Liabilities, or Statement of Financial Activities (or Income & Expenditure Account) and Balance sheet, as appropriate, are prepared
 - That these are passed to the independent examiner or auditor for external scrutiny
- ❖ At the Annual General Meeting
 - To present the independently examined or audited accounts
- ❖ After the Annual General Meeting
 - To ensure that the annual accounts and report and the annual returns are made to the Charity Commissioners and/or Companies House, as appropriate, by the due dates

Where possible, some or all of these duties may be delegated to others - bill payment and the issuing of receipts, for example, or even, if you are lucky, the keeping up of the books - but the treasurer is still responsible, and should ensure that the work he or she has delegated is being carried out properly.

Even with the support of paid staff, the scope of the treasurer's duties is considerable, and it should be no part of his/her duties to undertake the fundraising necessary for the organisation's purposes. This should be the responsibility of another member of the management committee otherwise without portfolio.

24.1.1. Section Treasurers

Many community organisations running community buildings are an umbrella or parent for the groups who use the building. Some of these groups may be separate entities in their own right, but others will in fact be sections of the community organisation, and as such fall under the responsibility of the main organisation's management committee, and thus of its treasurer, even if they are on the face of it autonomous, appointing their own management committee, keeping their own accounts and even having their own bank accounts. Where sections have this degree of autonomy, the main organisation will still have to prepare consolidated accounts including the section totals within the overall figures, and the main committee can ultimately over-rule any decisions of the section committee.

It is more usual for sections to be semi-autonomous, being self-governing and keeping their own accounts, but drawing money from and paying money to the main organisation's bank account, usually through the organisation's treasurer and staff. Each such section should appoint its own treasurer, who should follow such rules and keep such accounts as may be required by the treasurer of the community organisation, and regularly pay over to him/her all money received and pass on to him/her all accounts for payment. How simple or complicated the rules and accounts should be depends on the nature of the section and its activities, but as a minimum, the section treasurer should keep a day-book recording details of all monies received and passed over to the organisation, and requests for payments raised, together with a duplicate receipt book, covering all monies received.

Where, for administrative convenience, a section treasurer is permitted to pay money directly into the main organisation's bank account, they must provide the originals of any and all paying in slips to the main treasurer, keeping copies for their own records. It may be expedient for the section to have its own petty cash account, to be run on the imprest system, but the diversion of cash income to pay section expenses should never be permitted, nor should netting off (that is, showing only the profit or loss on an activity, rather than the total of receipts and payments). Petty Cash vouchers and receipts should be required for all items of expenditure from the

imprest. The main Treasurer should routinely and regularly oversee the work of the section treasurers, inspecting any subsidiary books and accounts at least once a quarter.

As the section is an integral part of the community organisation, its items of expenditure, other than those covered by the petty cash float (such as the purchase of CDs for the dance group or prizes for the whist drive), should in principle require prior authorisation by the main committee of the community organisation. In practice, as much of a section's expenditure will be of a regular or recurrent nature, the main committee will not wish to have to record its agreement on each occasion, such as payment of the DJ for the regular monthly disco, and one authorisation covering the whole series should be sufficient. However such payments should still always be by cheque, as should all payments for the purchase of capital equipment, authorised and signed by the main organisation's treasurer (and counter-signed by another of the authorised signatories).

24.1.2. Part-time finance worker

There will come a time when, unless your treasurer is retired, or otherwise able to devote themselves almost full-time to your organisation, the work of keeping the books, on top of their other duties becomes too much. You could share the treasurer's role across a small team of volunteers, whether you call this team the treasury team, or assistant or deputy treasurers or even the finance sub-committee, or you could off-load part of the work onto a paid worker.

In practice, it is usually the book-keeping which is off-loaded this way, either as part of the duties of an administrator, or even the centre manager, or on to a part-time book-keeper or finance worker. Which course of action you choose is up to you and your management committee, but making book-keeping part of the responsibilities of the centre manager, or even an administrator, unless their responsibilities are primarily financial, is seldom satisfactory, with the other parts of their job getting in the way of the book-keeping. You are better off employing a part-time book-keeper, whose duties are solely to keep the books, or finance worker who will do other financial administration tasks in addition to keeping the books.

An outline job description for such a part-time finance worker can be found on the CASH web site: www.cash-online.org.uk. Note that, for small businesses, advisers usually recommend that the first person you should hire should be a book-keeper.

There will need to be a close working relationship between your treasurer and your finance worker, and it is your treasurer who will need to exercise technical oversight, though the worker's line manager is usually your centre manager (or warden, or whatever you call them). Also, be prepared to pay the rate for the job – they will have to be able to work largely unsupervised, and the book-keeping requirements for charitable community organisations are much more onerous than for the equivalent sized small business.

24.1.3. Further Information

CASH Facts Sheets - Treasurer's Job Description

Finance Worker's Job Description

Community Matters Information Sheets:

73 – The Treasurer's Duties

10 Accounting by charities - the new Regulations

The Charity Treasurer's Handbook by Gareth G. Morgan. ISBN 1 900360 89 6. Published by:- The Directory of Social Change @ £9.95

24.2. Other management committee members' financial responsibilities

As charity trustees, your management committee must accept ultimate responsibility for directing the affairs of your community organisation, and ensuring that it is solvent, well-run, and delivering the charitable outcomes for which it has been set up.

The committee members must:

- ❖ Ensure that the organisation complies with charity law, and with the requirements of the Charity Commission as regulator; in particular ensure that the charity prepares reports on what it has achieved and annual returns and accounts as required by law
- ❖ Ensure that the charity does not breach any of the requirements or rules set out in its constitution and that it remains true to the charitable purpose and objects set out there
- ❖ Comply with the requirements of other legislation and other regulators (if any) which govern the activities of the organisation
- ❖ Act with integrity, and avoid any personal conflicts of interest or misuse of charity funds or assets
- ❖ Ensure that the charity is and will remain solvent
- ❖ Use the organisation's funds and assets wisely, and only in furtherance of its objects
- ❖ Avoid undertaking activities that might place the charity's endowment, funds, assets or reputation at undue risk
- ❖ Take special care when investing the funds of the charity, or borrowing funds for the charity to use
- ❖ Use reasonable care and skill in their work as Trustees, using their personal skills and experience as needed to ensure that the charity is well-run and efficient
- ❖ Consider getting external professional advice on all matters where there may be material risk to the charity, or where the Trustees may be in breach of their duties

They need to take special care when

- ❖ Investing in stocks, shares and similar investments
- ❖ Reviewing investments
- ❖ Acquiring land and buildings or exercising powers in relation to land and buildings, such as taking a lease or a licence, or offering a lease or licence to a third party
- ❖ Setting investment criteria
- ❖ Selecting investment advisors, or choosing not to take advice
- ❖ Selecting nominees, agents or custodians, and deciding or reviewing the terms under which such persons act on their behalf

If things go wrong, the management committee of an unincorporated charitable organisation may be personally liable for any debts or losses that the organisation faces as a result. However, personal liability of this kind is rare, and management committee members who have followed these requirements will generally have little to fear.

24.2.1. Further Information:-

Community Matters Information Sheet No. 70 - Community Association Trustees

Charity Commission leaflets:

CC3 - Responsibilities of Charity Trustees

CC3(a) - Responsibilities of Charity Trustees: A Summary

Charitable Status: a Practical Handbook, by Andrew Phillips with Bates, Wells & Braithwaite ISBN 1 900360 83 7 obtainable from the

Directory of Social Change,

24 Stephenson Way, London NW1 2DP

___ 020 7209 5151 @ £12.95

www.dsc.org.uk

24.3. Conflicts of Interest

This section is primarily written around the rules governing the members of the management committee of a charitable community organisation who are the charity's trustees, but they apply equally to non-charitable community organisations, where the rules are best practice, rather than mandatory.

24.3.1. What is a conflict of interest?

A conflict of interest is any situation in which a committee member's personal interests, or interests which they owe to another body, and those of the organisation arise simultaneously or appear to clash. It is inevitable that conflicts of interest occur, and the issue is not personal integrity, but the management of any potential to profit from a committee member's position, or for him or her to be influenced by conflicting loyalties. Even the appearance of a conflict of interest can damage your organisation's reputation.

Conflicts of interest may come in a number of different forms:

1. Direct financial gain or benefit to the committee member, such as
 - ❖ Payment to a member for services provided to the charity; the award of a contract to another organisation in which a member has an interest and from which a member will receive a financial benefit
 - ❖ Or the employment of a member in a separate post within the charity, even when the member has resigned in order to take up the employment
2. Indirect financial gain, such as employment by the organisation of a spouse or partner of a member, where their finances are interdependent
3. Non-financial gain, such as when a user of the charity's services is also a member; and
4. Conflict of loyalties, such as where a member is appointed by the local authority or by a community organisation's sections or one of the organisation's funders, or where a friend of a member is employed by the charity

24.3.2. Common conflict of interest situations

The situations in which conflicts of interest commonly occur in community organisations managing community buildings are as follows:-

- ❖ Conflicts of loyalties are common in community organisations, especially where many committee members are representatives of user groups or sections, or the nominees of outside bodies. When they are dealing with the business of the organisation, committee members' overriding duty is to act in the best interests of the organisation and they must act independently of the organisation which they represent or which appointed them, even if this is the local authority.

There will be occasions where such committee members will have to act in a way which conflicts with the interests of the organisation appointing them, to another organisation of which they are a committee member, or to a member of their family. In all such circumstances, the best interests of the charity must come first; this duty overriding all other considerations. To ensure transparency and avoid any accusations of impropriety, any trustee who has a conflict of loyalties should declare this at the beginning of any meeting at which an issue is to be discussed that is subject to the conflict, and should in principle take no further part in the discussions on the issue. In practice, this may be difficult for community organisations managing community buildings, where a majority of committee members are user group representatives. If the treasurer proposes to put up the hire fees for user groups, or the affiliation fees, and all the user group representatives who are clearly conflicted stand down, the committee meeting may be inquorate!

Note that failure to act in the best interests of the charity could constitute a breach of trust for which a personal liability (financial or otherwise) could arise

- ❖ Members as users of the organisation's services (which will apply to most, if not all members of a community charity managing a community building). In once sense, all decisions taken will affect the services in which the user members, along with other users, participate. The question is whether any such decision taken by the members will confer a direct tangible benefit on them as users which are exclusive to them which are not shared with other users. User members can take part in such decisions, but should declare their interest at the outset
- ❖ A close relative, such as a spouse or partner, of a member is employed by the community organisation. Because of the potential for conflicts of interest to arise, and despite the fact that payment is not being made directly to a member, the payment will still need to be authorised, and if there is no suitable power in the organisation's governing document, the organisation will need to apply to the Charity Commissioners for the necessary authority
- ❖ Payment to a member for a service provided to the organisation, such as painting the community building or for book-keeping
- ❖ Payment for a separate post within the organisation, such as warden or centre manager to someone who is also a committee member. Note that resigning either before or after taking up the post doesn't resolve the conflict of interest, unless the member concerned had no involvement with the decision to create or retain the post, or with recruitment for it, and where that person resigned in advance of a fair and open competition for the post

In both cases, if members wish to pay one or more of their fellow members, such payment will need to be authorised, either by a clause in the organisation's governing document, or by the Charity Commissioners, even if the service is provided at below market cost.

- ❖ Members as directors of a subsidiary trading company. A committee member cannot be paid for his or her services as a director, or employee, of a subsidiary trading company (or, of course, as an employee or committee member of the parent organisation), unless authority is contained either in the governing document or has been provided by the Charity Commissioners.
- ❖ A member loans money to the organisation at a favourable rate of interest, or at no interest, without any security. The other members should protect themselves and the interests of the organisation by ensuring that formal agreements are in place.

24.3.3. How can conflicts of interest be managed effectively?

When dealing with conflicts of interest, the golden rule is for the management committee to look at how the situation appears to someone from outside their organisation, and make sure that a policy and procedures are in place which will allow them to demonstrate that such situations have been dealt with properly.

All management committee members need to be alert to possible conflicts of interest which they might have and to how they can minimise their effects. A key aspect of minimising the effects of conflicts of interest is to be open and transparent about such situations when they arise. All committee members should advise their community organisation of any actual or potential conflicts of interest of which they are aware, as soon as they arise.

Community organisations should have a policy on how they will deal with any conflicts which arise as a result of the work which the organisation undertakes. A policy can include guidance on the procedures to follow when a management committee member is subject to a conflict of interest, such as:

- ❖ The removal of the member concerned from the decision making process
- ❖ Managing the conflict of interest once a decision has been made; and
- ❖ Recording details of the discussions and decisions made

The management committee should establish a register of interests. In recording all their other interests openly, any actual or potential conflicts of interest can be identified more easily. The register of interests should be regularly updated. It is good practice at the beginning of a meeting for every committee member to declare any private interest which he or she has in an item to be discussed, and certainly before any discussion of the item itself. Simply declaring that a conflict exists and withdrawing from the discussion and any decision making will be all that is required if the management committee member is not receiving any material benefit as a result of

the conflict of interest. However, if a member is receiving a material benefit this will need authority, given either by the governing document, or the Charity Commissioners, or both. To make the operation of the community organisation as transparent as possible, the policy on conflicts of interest, and, subject to the provisions of the Data Protection Act 1998, the register of member's interests, available to the public.

All community organisations should disclose the benefits received by the members of their management committee in their report and annual accounts. This is a legal requirement for charitable companies, those non-company charities with a gross annual income or expenditure over £100,000, and smaller charities which prepare their accounts on an accruals basis.

24.3.4. Checklist for Committee Members

1. If you have identified that a conflict of interest exists, are you, or is the member concerned, receiving a material benefit as a result of that conflict of interest? If no, have you, or has the member, declared the interest in the register of interests and not taken part in any discussions/voting on that issue? If yes, has the benefit been authorised?
2. Does the governing document contain authority for the benefit arising from the conflict of interest? If yes, have the management committee complied strictly with the terms of the authority contained in the governing document? If no, have the management committee applied to the Commissioners for authority?
3. Once the management committee have the necessary authority, are there procedures in place to manage the conflict of interest effectively? If no, have the management committee ensured that procedures will be put in place for managing conflicts of interest?
4. Have the management committee ensured that any benefit received by its members is disclosed in the annual report and accounts?

24.3.5. Staff and Volunteers

Employees and volunteers are also subject to conflict of interests, where the objectives of the organisation and the interests of employees or volunteers do not coincide. Staff have great potential for conflicts of interest - consultancy work with client organisations, letting friends do casual work, or unqualified friends filling vacancies that need qualified staff. A few years ago a manager of a community centre paid his fourteen year old son £100 every weekend to clean the centre windows! For community organisations, family involvement is natural, so these family situations will arise. What is important is that there are systems in place to ensure that there is no favouritism. An equal opportunities policy is also essential so that services, employment and volunteering opportunities are open to all sections of the community.

Since your organisation will already have in place a register of committee members interests, this could and should be extended to cover employees and volunteers, with failure to declare an interest justifying disciplinary action. There should also be a written Code of Conduct covering trustees, staff and volunteers. A code of conduct cannot cover every eventuality, but it is a means through which both the organisations intentions are made clear and provides guidance on what standards of behaviour are expected. It should be reviewed annually or as the need arises.

24.4. Contracts and Leases

At the risk of both repeating what has been said before, and of over-simplification, a contract is a legally enforceable deal made between two legally competent parties for one of the parties to do something for the other party in exchange for money, or for something worth money. Why this is always lurking in the background in matters impinging on community organisations running community buildings is that most such community organisations are unincorporated associations, and as such are not considered to be a legally competent party, for the purposes of contract law. Why the issue doesn't loom larger is that most people and organisations community organisations deal with have themselves only the haziest notion of contract law, and mostly neither know nor care about the legal niceties, provided they or their bills are paid on time. In practice, where a contract is necessary, this will be between some (usually the officers, that is the Chair, Secretary and Treasurer) or all of

the members of your management committee, as competent individuals, acting in effect “in loco parentis” (literally, in the place of parents) on behalf of the association, and the other party.

However, there are one or two situations where the legal niceties can't be avoided, and one of these is the matter of the ownership and lease of community buildings. In a strict sense, an unincorporated association cannot own or lease land or buildings, and these are also long term obligations, whereas management committees, in principle, change every year. If you rely on the usual expedient of contracting via your officers, you may find yourselves regularly having to go to the trouble and expense of having to amend the contracts to change the names of the officers. In addition, you are initially creating and then perpetuating a conflict of interest situation. Fortunately, at least for charitable associations, there is a solution, and that is to have holding (or custodian) trustees, whose sole function is to be the custodians of real property and leases on behalf of your association. Holding trustees, of which there are usually two or three, are

- ❖ Appointed by the management committee
- ❖ Serve at the management committee's pleasure
- ❖ Have no active role and play no active part in the day to day management of your association

However, finding local worthies prepared to take on even this role in this day and age is easier said than done, and there is an alternative, and that is to transfer responsibility for holding deeds or leases to the Official Custodian, who is a civil servant employed by the Charity Commissioners. You will still have to have holding trustees initially, but can relieve them of all but short term responsibilities by transferring custodianship, with their consent and agreement, at your earliest convenience.

Few community organisations are fortunate enough to own their community building. Most are leased or licensed, or should be, from a local authority. I say should be because there are many community organisations occupying community premises who have neither lease nor licence, and without a lease or a licence your organisation has no security of tenure. If you occupy community premises without benefit of either licence, or preferably, lease, this is a major risk, and resolving this situation must be a high priority for your association. This is easier said than done - it takes two to tango, and if your local authority, or housing association, or whoever owns the building you occupy won't come to the dance, you are stuffed. I know of what I speak – my local community association (I'm their treasurer) has only just sorted out its lease, having been sitting tenants for over 30 years, almost entirely due to foot-dragging by our local authority, who were quite content to continue the previous gentleman's agreement. There are two problem with gentlemen's agreements; one is that it requires both parties to be gentlemen (and I for one am no gentleman), and the other is that agreements made with previous parties must be honoured. In the end, what swung the argument for us was our local authority's desire for us to access lottery and other external funding, and their eventual recognition that without a lease this would be difficult.

One of the vexed questions you will have to face over the lease or licence is the question of rent. If you are fortunate (as my local association are) this will be a nominal sum. If you are less fortunate, this will be set at a commercial level (whatever that means in terms of a community building), though you may in practice get the whole or part of this remitted or offset by a grant. The disadvantage of such an arrangement is that it is easy, given the financial pressures that local authorities are under, for the grant to shrink or even disappear, such grants being discretionary, since providing community premises isn't a statutory obligation for local authorities.

The above gives no more than the flavour of the important topics of leases and rents for community premises. You are strongly advised to consult the Community Matters publication *Occupying Community Premises* on all matters pertaining to leases and licenses for more and more detailed information. On the equally vexed topic of rents for community premises, the peppercorn rent web site at www.peppercornrent.co.uk is a useful resource, not least because it exposes the fallacy of the argument put forward by many local authorities that they are obliged, either by statute or the Treasury to charge commercial rents, neither of which is true. It is within the gift of local authorities to let out community premises at a peppercorn or nominal rent, or even to transfer ownership

to a community organisation at a discounted price, and this, provided certain sensible safeguards are in place, is with the blessing of the Treasury.

24.5. Operating and Finance Leases

Another of the fundamental principles which underpins accountancy is that form takes precedence over substance. What this means in practice is that if you are a sole trader, accountancy treats you and your business as separate entities, whereas in law you and your business are indissoluble. It is this principle which permits HM Revenue and Customs to treat your community organisation as an entity for tax purposes, though it isn't legally one. In the context of leases of equipment, or hire purchase agreements, which is what in practice this section is about, if you have a piece of equipment, such as a photocopier or the dish-washer in your bar, on a long term hire contract, or hire purchase agreement, then this principle applies, and for accountancy purposes the equipment is treated as if you actually own it, even if in law you don't. Such leases and hire purchase agreements are called finance leases. Short term hire, whether it be of a bouncy castle for your fun day, or a pressure washer to remove graffiti during your annual spring clean, or indeed any and all of the equipment you hire from your local equipment, where you don't by any stretch of the imagination "exercise the privileges of ownership" (to quote the text-books), are called operating leases.

Although less of an issue than it was, contracts covering the lease of photocopiers are a particular case in point. To be legally enforceable on both sides, the agreement must be signed by one or more of the trustees (the managing trustees, also known as the management committee), acting on behalf of an unincorporated association. Strictly, the contract is with the signatories, not the association, and it is their responsibility to pay the charges, though in practice they will be able to call on the association's resources, provided the decision to lease and the empowerment of the trustees was agreed at a minuted meeting of the trustees. Why such leases were problematic was that many were poor value for the association. Unfortunately, it usually took management committees a year or two to realise this, any by then it was (or they felt it was) too late to do anything about it. Leases are like any other contracts, they can be changed (though it needs both parties to agree), so if you find you have inherited a bad deal, and having in the first instance checked that it has actually been signed by a trustee, and is therefore enforceable, you should attempt to renegotiate the deal. You will almost certainly have to cross the leasing company's palms with silver, so it may come down to a simple calculation of how much it will cost you to buy out the contract as against continuing with the lease to the bitter end.

If the lease agreement was signed by a member of staff, for example your warden or centre manager, you have a problem, but a different (and more difficult) problem. You could, legally, repudiate the contract (even though you may have asked or instructed the member of staff to sign), since they neither have the power to bind the association to a contract, nor do you, as trustees, have the power to authorise them to bind the association to a contract (to use the legal jargon) but this would leave you in the morally difficult position of leaving the member of staff, acting in good faith, "holding your baby." In practice, most associations in this position would act as if the contract was valid, though if push came to shove, this is another of those situations where the trustees might have to find any funds required from their own pockets.

The way to avoid such situations is to look before you leap. Where long term contracts, spanning several years are concerned, your management committee must go into the financial pros and cons very carefully, and look into the background of the leasing company carefully and thoroughly. This is one area where the rules about seeking several quotes definitely mustn't be ignored, and if a deal looks too good to be true, it probably is too good to be true! Be especially careful when leasing high-tech equipment (and this is traditionally the sort of equipment that is leased). A lease makes sense if the equipment is unreliable, and needs expert maintenance and servicing, but doesn't if technological advances lead to rapid improvement in reliability and performance and rapid reductions in price, resulting in early obsolescence and requiring early replacement.

Another important issue with photocopiers and similar equipment, and for that matter, domestic carpets, is their suitability for the duty. A photocopier suitable for occasional use in a small office will be completely unsuitable

for a busy community organisation office, so it is a matter of not only comparing price and price per copy but also the total number of copies which can be done, and the rate of copying, both in short bursts and continuously – a heavy duty copier with the same specification as a light duty copier may cost 3 or 4 times as much. Having a clear upgrade path should also be an important consideration, so that if you find that in 2 or 3 years time you need a more capable machine, you can swap your existing machine for the better one without having to pay an arm and a leg.

Chapter 25

25. Legal Forms for Community Organisations

By legal form, I mean the structure or constitutional arrangements appropriate for community organisations. All will have a written document setting out what they are for and how they are to be managed. What this governing instrument (i.e. document) is called depends on the legal structure.

25.1. Unincorporated Associations

The commonest legal form or structure, and the one most characteristic of and applicable to the community organisations this book is aimed at is the unincorporated association. This is the simplest and most straight-forward structure, whose governing document is called a constitution. Usually, its management committee is elected annually by its membership – in effect, its supporters club – and this democratic accountability is one of its strengths. If the organisation's objects – what it is legally constituted to do – are charitable, and its activities are exclusively charitable, then the organisation is a charity, legally obliged to seek registration, unless exempt or excepted. Otherwise, there is no requirement, or indeed mechanism, for seeking or obtaining official recognition. Although the unlimited liability status of their management committee members is usually quoted as the major disadvantage of an unincorporated association, the real disadvantage, discussed in the previous chapter, is its inability to enter into contracts.

25.2. Companies Limited by Guarantee

Where community organisations are concerned either at the unlimited liability of their management committee members, or their inability to enter into contracts, the usual response is for them to be companies limited by guarantee. These need to register with Companies House, are subject to the Companies Act (they should be registered under Section 30) and their governing instruments are called a Memorandum of Association and Articles of Association. As with unincorporated associations, their management committee (that is, their board of directors) are democratically answerable to their members – their supporters club – who are also the guarantors (that is, they agree to put up a sum of money – usually £1, but no more than £10 – in the event the company becomes bankrupt. If the organisation's objects – what it is legally constituted to do – are charitable, and its activities are exclusively charitable, then the company is a charity, legally obliged to seek registration, unless exempt or excepted. This separate accountability to both company and charity law, and thus to both Companies House and the Charity Commissioners is one of the two major disadvantages of being a charitable company limited by guarantee, the other is that the Insolvency Act applies, and thus the directors become liable if the company continues to trade if it cannot pay its debts.

25.3. Charitable trust

Some founders of community organisations aren't enamoured by the democratic method of trustee appointment implicit in the standard unincorporated association and company limited by guarantee, fearing a watering down of their vision and a loss of control. For such control freaks, the trust, governed by a trust deed, is an attractive structure. If the organisation's objects – what it is legally constituted to do – are charitable, and its activities are exclusively charitable, then the trust is a charity, legally obliged to seek registration, unless exempt or excepted. Legally, the trust is a sum of money, or something of money's worth, but this can be a nominal rather than a substantive amount, the minimum being £1!

25.4. Community Benefit Society

As an alternative to becoming a company limited by guarantee, with the same advantages of corporate status and limited liability, a community organisation could seek to become a community benefit society. This is a mutual society or co-operative existing primarily for the benefit of the community, rather than its members, set up under the provisions of the Industrial and Provident Societies Act 1965, governed by a set of Rules and registered with and regulated by the Financial Services Authority. If the organisation's objects – what it is legally constituted to do – are charitable, and its activities are exclusively charitable, then the society is a charity, but legally an exempt charity, and therefore unable to register with the Charity Commission. Having only one regulator is a clear advantage, but in

order to claim the financial benefits of charitable status, it will be necessary to register with HM Revenue and Customs. Before being able to go down this route, the prospective society must satisfy the Financial Services Authority that there are special reasons why it should not become a limited company registered under the Companies Act. In addition, unlike the Charity Commission who make available general purpose governing documents for unincorporated associations, companies limited by guarantee and trusts on their web site free of charge, the Financial Services Authority does not provide model Rules, nor does it sign-post where these might be obtained. What the special reasons are is not defined, but the Financial Services Authority suggests that an acceptable reason might be "one member, one vote", which would reflect the ethos of many community organisations. For further information, see http://www.fsa.gov.uk/Pages/doing/small_firms/MSR/pdf/cooperative.pdf

25.5. Community Interest Company

Becoming a charity has some disadvantages, one of which is the general prohibition on trustees being paid for their work as trustees, which is seen by some in community organisations as both a disincentive and a form of discrimination. Offsetting this disadvantage is the advantage that there is a legal lock on the assets of a charity, which generally prohibits the sale of these where they are held "in trust" for the community. Non-charitable limited companies have no such prohibitions on paying their directors, but conversely it is difficult, if not impossible, to prevent the members (the guarantors, for a company limited by guarantee) of such a company, even one set up as a not-for-profit company, converting it to a for-profit company, and thus disposing of assets which the community view as theirs, for personal gain.

The current national government have an interest in promoting social enterprises. As is discussed elsewhere in this document, social enterprise is a concept rather than a legal structure, which can be interpreted variously as a for-profit company which invests some or all of these profits in the community, in preference to distributing them to share-holders or as a not-for-profit company which seeks investment from the private sector, and needs to make profits in order to pay dividends to these investors. Many existing community organisations, even those which are charities, would see themselves as social enterprises, so what apart from the ability to obtain private capital, is special about the government's vision? Nothing, perhaps, except the entrepreneurs at the head of the social firm, who need to be rewarded with material riches in this world rather than, as is the case with charity trustees, immaterial riches in the next. To promote this vision of a sort of hybrid between a not-for-profit and a for-profit company headed up by paid entrepreneurs, central government has brought into being the Community Interest Company.

Community Interest Companies (CICs) are limited companies, and therefore governed by a Memorandum of Association and Articles of Association, with special additional features created for the use of people who want to conduct a business or other activity for community benefit, and not purely for private advantage. This is achieved by a "community interest test" and "asset lock", which ensure that the CIC is established for community purposes and the assets and profits are dedicated to these purposes. Registration of a company as a CIC has to be approved by the Regulator of Community Interest Companies, who also has a continuing monitoring and enforcement role. Such a company cannot also be a charity.

At the time of writing, the Regulator of Community Interest Companies is in place, and his office is open for business. The Regulator clearly expects the CIC form to be attractive to those charities wanting to set up a trading arm, so if you are interested in finding out more about community interest companies see <http://www.cicregulator.gov.uk>.

25.6. Charitable Incorporated Organisation

As pointed out above, charitable companies are currently covered by two different, and not necessarily compatible, Acts of Parliament and answerable to two separate, and independent from one another, regulators. This is neither efficient and effective nor necessary. Accordingly, the Charities Act which received the Royal Assent in November 2006 established a new legal form, with corporate status and limited liability, called the Charitable Incorporated Organisation (CIO), governed by a constitution and registered with and regulated by the Charity Commissioners.

The Act permits not only new organisations to register as CIOs but also existing charitable companies to metamorphose into CIOs, and provides a straight-forward upgrade path for unincorporated associations seeking corporate status with limited liability. However, it will be early 2008 before the Charity Commission is open for business in the matter of registering CIOs. For further information, see <http://www.charitycommission.gov.uk/enhancingcharities/incorporg.asp>.

25.7. Bona Fide Co-operatives

This is a mutual society or co-operative existing primarily for the benefit of its members, and therefore not charitable, set up under the provisions of the Industrial and Provident Societies Act 1965, governed by a set of Rules and registered with and regulated by the Financial Services Authority. This form is not suitable for community organisations running community buildings, but can be appropriate for a social club operating on community premises and donating under gift aid its profits to the charitable organisation running the community building. If you are interested in setting up such a social club, especially if its purpose is to provide a licensed bar on community premises as a source of income, you are strongly advised to seek advice from Community Matters, who are acknowledged experts in this field. For further information on bona-fide cooperatives, see http://www.fsa.gov.uk/Pages/doing/small_firms/MSR/pdf/cooperative.pdf.

Sources of Additional Information (Charity Commission, Inland Revenue websites etc.)

acas (The advisory, conciliation and arbitration service)

National office
Brandon House
180 Borough High Street
London
SE1 1LW
Tel: 020 7210 3613
08457 47 47 47 help line
Email: www.acas.org.uk

ACEVO (Association of Chief Executives of Voluntary Organisations)

1 New Oxford Street
London
WC1A 1NU
Tel: 0845 345 8481
Fax: 0845 345 8482
Email: info@acevo.org.uk
Web site: www.acevo.org.uk

Community Matters

12-20 Baron Street
London N1 9LL
Tel: 020 7837 7887
Fax: 020 7278 9253
Information & Advice: Tel: 08707 272 373
E-mail: communitymatters@communitymatters.org.uk.
Website: www.communitymatters.org.uk.

CASH (Community Accountancy Self Help)

1 Thorpe Close
London W10 5XL
Tel: 020 8969 0747
Fax: 020 8960 8926
E-mail: services@cash-online.org.uk
Website: www.cash-online.org.uk

Community Trading Services Ltd.

12-20 Baron Street
London N1 9LL

Charity Commission

The Charity Commission (strictly, the Charity Commissioners for England and Wales) have 4 offices, based in:-

London
Harmsworth House
13-15 Bouverie Street

London
EC4Y 8DP
Fax : 020 7674 2300

Taunton
Woodfield House
Tangier
Taunton
Somerset
TA1 4BL
Fax : 01823 345003

Liverpool
12 Princes Dock
Princes Parade
Liverpool.
L3 1DE
Fax : 0151 703 1555

Newport
8th Floor
Clarence House
Clarence Place
Newport
South Wales
NP19 7AA

Which offices deal with which charities is a matrix defying logic, so in the first instance, contact their call centre (based in Liverpool) tel: 0870 333 0123, or their web site: www.charitycommission.gov.uk

Chantrey Vellacott DFK

Russell Square House
10/12 Russell Square
London
WC1B 5LF
Tel: 020 7509 9000
Email: info@cvedfk.com
Web site : www.cvedfk.com/sectors/charities

CIVICUS - World Alliance for Citizen Participation

CIVICUS House
24 Gwigwi Mrwebi Street
(former Pim) corner Quinn St.,
Newtown
2001 Johannesburg,
South Africa
Tel: +27 11 833 5959
Fax: +27 11 833 7997
Email: news@civicus.org
Web site: www.civicus.org

Directory of Social Change

For all enquiries,

Tel: 08450 777707

Web site: www.dsc.org.uk

Email: info@dsc.org.uk

London office

Directory of Social Change

24 Stephenson Way

London

NW1 2DP

Tel: 020 7391 4800

Fax: 020 7391 4808

Liverpool office

Directory of Social Change

Federation House

Hope Street, Liverpool

L1 9BW

Tel: 0151 708 0117

Fax: 0151 708 0139

Financial Services Authority

25 The North Colonnade,

Canary Wharf,

London

E14 5HS

Tel: 020 7066 1000 Switchboard

0845 606 1234 Consumer Helpline

Fax: 020 7066 1099

Website: www.fsa.gov.uk

NAVCA (National Association for Voluntary and Community Action)

177 Arundel Street

Sheffield S1 2NU

Tel: 0114 278 6636

Fax: 0114 278 7004

Email: navca@navca.org.uk

Website: www.navca.org.uk

HM Revenue and Customs

It is impossible to give contact addresses and telephone numbers for this new government department formed from the merger of the **Inland Revenue** (who dealt with tax and national insurance) and **HM Customs and Excise** (who dealt with VAT and import of alcoholic drink and tobacco), not because there aren't any but because there are too many, all dealing either with a local geographic area or a specialist topic. Contact details for the office dealing with your local area or subject of interest can be extracted from their website:

www.hmrc.gov.uk

Community Accountancy National Network

c/o John O'Brien,

Community Accounting Plus
1st Floor, Ormiston House,
32-36 Pelham Street,
Nottingham, NG1 2EG.
Tel: 0115 947 0839
Email: enquiries@communityaccounting.co.uk.

Association of Charity Independent Examiners

Bentley Resource Centre
High Street
Bentley
Doncaster DN5 0AA
Tel: 01302 828338
Fax: 01302 872973
Email: info@acie.org.uk
Web site: www.acie.org.uk

Department of Trade and Industry

National Minimum Wage
Web site: www.dti.gov.uk/er/nmw

Funder Finder

65 Raglan Road,
Leeds, LS2 9DZ,
Tel: 0113 243 3008
Fax: 0113 243 2966
Email: www.funderfinder.org.uk

Jordans Limited

Charity Services

Web site: www.jordans.co.uk/jordans3.nsf/Main/Charities
email: customerservices@jordans.co.uk

Bristol (head) office

21 St Thomas Street, Bristol BS1 6JS
Tel: 0117 923 0600
Fax: 0117 923 0063

London office

20-22 Bedford Row,
London WC1R 4JS
Tel: 020 7400 3333
Fax: 020 7400 3366

Cardiff office

44 Whitchurch Road,

Cardiff CF14 3UQ
Tel: 029 2037 1901
Fax: 029 2038 2342

Jordans (Scotland) Limited - trading as Oswalds
24 Great King Street, Edinburgh EH3 6QN
Tel: 0131 557 6966
Fax: 0131 556 2917

MANGO (Management Accounting for Non-Government Organisations)

97A St Aldates,
Oxford,
OX1 1BT.
Fax: 01865 423560
Tel: 01865 423818 (training)
Web site: www.mango.org.uk

Volunteering England

Tel: 0845 305 6979
Email: information@volunteeringengland.org

London office
Regents Wharf
8 All Saints Street
London N1 9RL
United Kingdom
Fax : 020 7520 8910

Birmingham office
New Oxford House
16 Waterloo Street
Birmingham B2 5UG
United Kingdom
Fax: 0121 633 4043

National Council for Voluntary Organisations

(NCVO)
Regents Wharf
8 All Saints Street
London N1 9RL
Tel: 0800 2798 798 (help desk)
020 7713 6161 (switchboard)
Web site: www.ncvo-vol.org.uk Main site
www.askncvo.org.uk AskNCVO

Peppercorn Rent

C/O West Hampstead CA
60-62 Mill Lane
London NW6
Web site: www.peppercornrent.co.uk

Sayer Vincent

8 Angel Gate
City Road
London
EC1V 2SJ
Tel: 020 7841 6360
Fax: 020 7841 6361
Email: info@sayervincent.co.uk
Web site: www.sayervincent.co.uk

Voluntary Arts Network

Web site: www.voluntaryarts.org
PO Box 200,
Cardiff,
CF5 1YH
Tel: 02920 395 395
Fax: 02920 397 397
Email: info@voluntaryarts.org

Voluntary Arts England
PO Box 1056,
City Road,
London
NE99 1UE
Tel: 0191 233 3864
Email: info@vaengland.org.uk

Voluntary Arts Ireland
PO Box 200,
Downpatrick
BT30 6WE
Tel: 02844 839327
Fax: 02844 839192
Email: info@vaireland.org

Voluntary Arts Scotland
PO Box 17200,
Edinburgh
EH11 2YG
Tel: 0131 313 2555
Fax: 0131 313 2666
Email: info@vascotland.org.uk

Voluntary Arts Wales
PO Box 200,
Welshpool,
Powys
SY21 7WN
Tel: 01938 556 455
Fax: 01938 556 451
Email: info@vaw.org.uk

VoIResource - information for voluntary and community organisations

This is an entirely web-based “virtual” organisation

<http://www.volresource.org.uk>

Useful Web Sites for Community Organisations

ACEVO

<http://www.acevo.org.uk>

ACRE (Action with Communities in Rural England),

<http://www.acre.org.uk>

BASSAC

<http://www.bassac.org.uk>

CAF

<http://www.casfonline.org>

CFDG

<http://www.cfdg.org.uk>

Chantrey Vellacott DFK

<http://www.cvdfk.org.uk>

CASH

<http://www.cash-online.org.uk>

Cash Call

<http://www.data-developments-co.uk>

Charity Commission

<http://www.charitycommission.gov.uk>

Community Accountancy Plus

<http://www.communityaccounting.co.uk>

Community Matters

<http://www.communitymatters.org.uk>

Department for Communities and Local Government

<http://www.communities.gov.uk/>

Directgov – the “one stop shop” to all on-line public services

<http://www.direct.gov.uk>

N.B You can access your Local Authority via this web site

Directory of Social Change

<http://www.dsc.org.uk>

Dosh Software Ltd.

<http://www.dosh.co.uk>

DTI – National Minimum Wage

<http://www.dti.gov.uk/er/nmw>

Financial Services Authority

<http://www.fsa.gov.uk>

HMSO – now absorbed into OPSI (q.v.)

Independent Examiners

<http://www.acie.org.uk>

HM Revenue and Customs

<http://www.hmrc.gov.uk>

❖ Charities

<http://www.hmrc.gov.uk/charities/index.htm>

IT for Charities

<http://www.itforcharities.co.uk>

Jordans

<http://www.jordans.co.uk>

LVSC

<http://www.actionlink.org.uk/lvsc>

MANGO (Management Accounting for Non-Government Organisations)

<http://www.mango.org.uk>

Moneysoft

<http://www.moneysoft.co.uk>

National Centre for Volunteering

<http://www.volunteering.org.uk>

NAVCA (National Association for Voluntary and Community Action – formerly NACVS)

<http://www.navca.org.uk>

NCVO (National Council for Voluntary Organisations)

<http://www.ncvo-vol.org.uk>

AskNCVO

<http://www.askncvo.org.uk>

Quickbooks

<http://www.quickbooks.co.uk>

OPSI The Office of Public Sector Information

<http://www.opsi.gov.uk>

SAGE

<http://www.sage.co.uk>

<http://www.intelligent-solutions-ltd.co.uk>

Sayer Vincent

<http://www.sayervincent.co.uk>

Unity Trust Bank

<http://www.unity.uk.com>

Voluntary Action Sheffield

<http://www.vas.org.uk>

Voluntary Arts Network

<http://www.voluntaryarts.org.uk>

Voluntary Resources

<http://www.volresource.org.uk>

Funding web sites:-

Association for London Government – now called London Councils (q.v.)

Awards for All

www.awardsforall.org.uk

Big Lottery Fund

www.biglotteryfund.org.uk

Bridge House Estates Trust

www.bridgehousegrants.org.uk

Fit4Funding - The Charities Information Bureau

www.cibfunding.org.uk

City Parochial Foundation & Trust for London

www.cityparochial.org.uk

Funder Finder

www.funderfinder.org.uk

Funding Information

www.fundinginformation.org

Government Funding

www.governmentfunding.org.uk

London Councils

www.londoncouncils.gov.uk

Scarman Trust

www.thescarmantrust.org

Glossary of Terms

Some of the terms below are not strictly accountancy terms, but have been included because they help to explain the importance of good financial management. Some of the terms are difficult to put into layman's language, but have been included because it is essential for community organisations to have at least basic knowledge of what their accountant, independent examiner or auditor is talking about.

Accrual

1. The process of matching income received in a given time period to the expenditure incurred in the same time period, and vice-versa.
2. An item of income or expenditure recorded or occurring in a later time period properly belonging to an earlier time period. For example, the bill from your independent examiner for looking at your last year's accounts will be received this year.

Accruals accounts. Accounts kept or prepared on an *accruals* basis.

Accounting is concerned with all aspects of the work of a voluntary group which can be measured in money terms, especially

- ❖ Planning what money will be received and paid out in the future
 - We call this budgeting
- ❖ Recording
 - What money has been received and paid out by the group
 - What money is owed to the group and what money is owed by the group and by whom
 - What assets the group owns
- ❖ Classifying and summarising the recorded data so that it can be understood by and made use of by the group
- ❖ Communicating to the group and other interested people and organisations what has been learned by classifying and summarising the data

Accountant's report (also called an **Audit Exemption Report**) A report, given by a qualified accountant, confirming that the accounts of a charitable company currently with an income or expenditure of between £90,000 a year and £250,000 a year (to be increased, in early 2007 following the passing of the 2006 Charities Act, to £500,000), have been properly prepared,.

Accounting regulations The Charities (Accounts and Reports) Regulations 1995 and 2000, usually abbreviated to Accounting Regulations. The Statutory Instruments which set out the requirements, under the 1993 Charities Act, for the content and form of charity accounts and the trustees annual report.

Accumulated fund. The sum total of an organisation's annual surpluses and deficits since its start. This will also be the value of the net worth of the organisation, expressed as the difference between its **assets** and its **liabilities**. For charities, the accumulated fund is made up of four separate funds:-

1. **The reserves**
2. **The restricted fund**
3. **The endowment fund**
4. **The designated fund**

The **unrestricted funds** are the reserves plus the designated fund

Assets. Items possessed by an organisation – including money goods or property, and any legal rights the organisation may have to receive goods, services, money or property. e.g.

- ❖ Fixed assets - Property of all kinds – land, buildings, furniture, fittings, equipment, stocks of goods (not for sale), motor vehicles

- ❖ Stocks of goods for sale
- ❖ Cash in hand and at the bank
- ❖ Benefits – the debts owed to the organisation

Audit. An examination of the accounts of a charity undertaken by a **Registered Auditor**, to confirm that they give a “true and fair” view of the state of its finances. The **Accounting Regulations** require all charities with an annual income or expenditure greater than a threshold value (currently £250,000, to be increased to £500,000 in early 2007) to have an audit. Increasingly, charities below this threshold are being required to have an audit by funders – especially Local Authorities. **Registered Auditors** are chartered accountants belonging to one of the recognised professional accounting bodies who are registered as auditors with that body and regulated by that body.

Bank reconciliation. A process for comparing your book-keeping records with your bank statements, and explaining (reconciling) all differences between them. An essential check on both accuracy of your bookkeeping, and the errors made by your bank.

Balance sheet. A summary of the **assets** and **liabilities** of an organisation at a given point in time, usually the financial year end, which also describes the funds that are represented by the net assets (the difference between the assets and the liabilities). A balance sheet can be seen as a snapshot of the organisation’s finances.

Book-keeping is that part of accounting dealing with the recording.

Budget. A plan showing what money will be received and paid out over a future period of time (usually a year).

Budget Headings. The main entries in a list of incomings and outgoings against which to construct a budget. In a large organisation, budget headings will be broken down into sub-headings which will in turn be broken down into line items.

Capital.

1. The monetary resources invested in an organisation. **Assets** minus **liabilities**
2. An **endowment fund** (or funds) which must be retained by the trustees on behalf of the beneficiaries of a charity, and not spent

Capitalise. To spread the cost of a **fixed asset** over its useful life by means of a depreciation charge.

Capital expenditure. Money spent on buying **fixed assets**. See **Note 2**

Cash flow. A forecast looking at the flows of monies into and out of your bank account over the period covered by a budget.

Charity. A voluntary organisation set up “pro bono publico” (for the public good) whose activities are defined as charitable by the 1993 Charities Act.

Charities Act. The 1993 Act of Parliament that defines what charities are, and sets out the rules and regulations they must follow.

Charities SORP. Statement of Recommended Practice on Accounting and Reporting by Charities, endorsed by the Charity Commissioners for England and Wales. The current edition dates from February/March 2005. A charity is not legally obliged to follow the SORP, but will have a hard time convincing the Charity Commissioners that its accounts comply with the **Accounting Regulations** if it does not.

Charity Commission. The non-ministerial government department established by the 2006 Charities Act to register and regulate charities. See also *the Charity Commissioners for England and Wales*.

Computerised accounts. Accounts kept using computer software packages designed for the purpose of keeping accounts, alongside or instead of the traditional paper-based bank analysis book. Well known accounting packages include Quickbooks and Sage. Accounts kept in Excel, a spread-sheet program, don't strictly count, since this isn't an accounting package.

Core. The routine on-going activities of an organisation not covered by a project or projects.

Thus:-

- ❖ **Core funding.** Funding for an organisation's non-project activities
- ❖ **Core expenditure.** Expenditure by or on behalf of core activities

Credit. To make an entry on the right hand side of a ledger. See **Note 2**

- ❖ To decrease an asset.
- ❖ To increase capital
- ❖ To increase a liability

Creditors. People you owe money to.

Debit. To make an entry on the left hand side of a ledger. See **Note 2**

- ❖ To Increase an asset.
- ❖ To decrease capital
- ❖ To decrease a liability

Debtors. People or organisations who owe you money.

Designated funds. Part of the *unrestricted funds* of a *charity* which the *trustees* have ear-marked for a particular purpose.

Depreciation. A charge applied each year to each fixed asset representing the amount of the value of the fixed asset which has been consumed during the year. There are many ways of calculating depreciation, the simplest being to divide the cost of the fixed asset by its estimated useful life. e.g. If a new computer costs £1000 and has an estimated useful life of 5 years, the depreciation charge is £200 per year.

Direct charitable expenditure. Expenditure relating directly to the objects of a charity. i.e. the expenditure concerned with the charity's activities, as distinct from *management and administration costs* and *fundraising costs*.

Direct costs. Costs associated with and dependent upon a particular activity or project. If the activity or project isn't done, these costs don't come about. **See note 4.**

Double entry book-keeping. A system of book-keeping where each item of income or expenditure is recorded twice, once as a debit to an account and once as a credit to a different account.

Endowment. Capital, in the form of property, shares, or money, donated or willed to a charity, which must be kept intact and not spent. There are two types:-

1. **Permanent endowment**, when only the earnings from property, the dividends on shares and the interest on money can be spent by the trustees, the principal (the capital) being kept intact.

2. **Expendable endowment**, when the principal can (eventually, and at the trustees' discretion, be converted into income, and spent.

Expenditure. Monies paid out and owing to creditors relating to a defined time period.

Financial controls. A set of written procedures governing how an organisation manages all its finances.

Financial statements. The organisation's accounts including all the notes to the accounts, and any other statements that need to be included.

Fixed assets. Items of significant value with a useful life of more than one year. Examples are:- Land and buildings, fixtures and fittings, office equipment, plant and machinery, motor vehicles.

In **receipts and payments accounts**, the full cost of a fixed asset is shown in the accounts when it is paid for. In **accruals accounts**, only the depreciation charge for the year is shown.

Fixed asset register. A written record containing details of all fixed assets, including when they were acquired, the price paid for them, and their current whereabouts. Charities are required by law to keep a fixed asset register.

Fixed cost. An item whose cost doesn't change as the quantity used changes. See **Note 3**

Full cost recovery. The pricing of projects such that the funds received cover not only the project's **direct cost** but also a fair proportion of the organisation's **indirect costs**.

Fundraising costs. All the costs incurred by a charity when it raises funds, not only the costs of fundraising events and activities but also from all advertising, publicity and mailing, and especially any fees or commissions paid to agents.

General funds. See **unrestricted funds**.

Funds that may be used generally for the advancement of the charity's objectives – they are not restricted funds, nor funds that have been earmarked for a particular purpose.

Governing document (or instrument). The document setting out the **objects** and laws of the organisation. It may be called a Constitution, Rules, Memorandum and Articles of Association, Trust Deed, or (in Scotland) Explanatory Document or Founding Deed, depending on the precise legal structure of the organisation. For a charity, it must be approved by the Charity Commissioners before it is registered or, afterwards, if amendments are made to the governing document.

Gross income. Generally, all the income of the organisation during a financial year, before any deductions are made. For charities, the definition excludes all income from endowments, and the sale of fixed assets and investments.

Heads of charity. The four broad headings into which charitable purposes are grouped:

1. The relief of financial hardship
2. The advancement of education
3. The advancement of religion
4. Other charitable purposes for the benefit of the community, e.g.
 - ❖ The relief of old age, sickness or disability, where there is no financial need
 - ❖ promoting racial harmony
 - ❖ The resettlement and rehabilitation of offenders and drug abusers
 - ❖ Providing help for victims of natural or civil disasters

- ❖ Promoting human rights
- ❖ The provision of recreational facilities which are open to everyone
- ❖ Urban and rural regeneration and community capacity building
- ❖ Promotion of health
- ❖

The 2006 Charities Act redefines these heads of charity as:-

- ❖ the prevention or relief of poverty
- ❖ the advancement of education
- ❖ the advancement of religion
- ❖ the advancement of health or the saving of lives
- ❖ the advancement of citizenship or community development
- ❖ the advancement of the arts, culture, heritage or science
- ❖ the advancement of amateur sport
- ❖ the advancement of human rights, conflict resolution or reconciliation or the promotion of religious or racial harmony or equality and diversity
- ❖ the advancement of environmental protection or improvement
- ❖ the relief of those in need by reason of youth, age, ill-health, disability, financial hardship or other disadvantage
- ❖ the advancement of animal welfare
- ❖ the promotion of the efficiency of the armed forces of the Crown; or the efficiency of the police, fire and rescue services or ambulance services, and;
- ❖ any other purposes charitable in law

This list, which will come into force early in 2007, covers the majority of purposes which are already charitable; the last category means that everything which is currently charitable is included

Income. Monies received and owing from debtors relating to a defined time period.

Income and Expenditure Accounts. A set of **accruals accounts** relating to a defined time period kept on the basis of

- ❖ Monies received and owing from debtors
- ❖ Monies paid out and owing to creditors
- ❖ Expenditure on fixed assets is capitalised

The set comprises

- ❖ **The Income and expenditure Account**
- ❖ **The Balance Sheet**

Income and expenditure account. A summary of the income and expenditure for a defined time period, usually a financial year, showing the **revenue expenditure** in full but only the **depreciation** charge for the **capital expenditure**.

Incomings. A general term covering both receipts and income.

Incoming resources. All resources available to the organisation, including restricted income, income from endowments, gifts in kind and intangible income.

Independent examination. An examination of the accounts of a charity undertaken by *an Independent Examiner*, to check that

- ❖ Proper Accounting records are being kept
- ❖ There is nothing obviously wrong with the accounts

An independent examination is less stringent than an audit. The **Accounting Regulations** require all charities with an annual income or expenditure greater than a threshold value (currently £10,000) but less than the audit threshold (currently £250,000, but increasing to £500,000 early in 2007) to have an independent examination. Increasingly, charities below the £10,000 threshold, and community organisations which are not charities are being required to have an independent examination by funders – especially Local Authorities.

Independent Examiner. The person appointed to carry out an independent examination, who must be completely independent of the group. They don't have to be a qualified accountant, but they must be someone who is recognised to be financially competent, and have experience of charity accounts.

Indirect costs. Costs not associated with or dependent upon any particular activity or project. These costs happen whatever the activities or projects undertaken. See **note 4**

Liabilities. The debts owed by the organisation, for goods, services and expenses. In the balance sheet, the amounts owed by the organisation at the time the balance sheet is drawn-up - the cost has been incurred, but the bills remain to be paid.

Management and administration. Costs directly resulting from the management of a charity's assets, compliance with statutory requirements, and administration relating only to governance, **not** either administration in general or administration relating to activities in furtherance of the charity's objects, or to fundraising.

Objects. The purpose or purposes for which the organisation was set up, defined in a clause in the organisation's governing document. For a charity, the objects must

- ❖ Fit within one or more of the **heads of charity**
- ❖ Be expressed in legal terms

Charities can only legally carry out activities which are covered by their objects. Trustees who direct or permit their charity to act outside the scope of its objects are said to have acted **ultra vires**.

Outgoings. A general term covering both payments and expenditure.

Overheads. Another name for indirect costs. Like so many terms in accounting, often used inconsistently or inaccurately. So, it may be used as another name for central or core costs. Overheads are often assumed to be the basic costs of running the organisation, including, typically, office running costs, salaries of non-project staff, rent etc. See **note 4**.

Payments. Monies (cash, cheques, bank transfers, etc.) actually paid out during a defined time period.

Permanent endowment. An endowment fund where the trustees have no discretion to convert the capital into income.

Pre-payment. An item of income or expenditure recorded or occurring in an earlier time period properly belonging to a later time period. For example, an insurance premium paid last year for a policy covering this year.

Project. A task or set of tasks carried out by a team of people over a period of time with

- ❖ A defined start
- ❖ A defined end

- ❖ A specific purpose

Thus:-

- ❖ **Project funding.** Funding for a specific project
- ❖ **Project Expenditure.** Expenditure by or on behalf of a specific project

By definition, for charities, external project funding is restricted funding.

Public benefit The 2006 Charities Act establishes the requirement that all charities must exist for the public benefit, and the Charity Commission has a new objective to promote understanding and awareness of this public benefit requirement. This provision of the 2006 Act won't come into force until early 2008.

Receipts. Monies (cash, cheques, bank transfers, etc.) actually received during a defined time period.

Receipts and Payments Accounts. A set of accounts relating to a defined time period kept on a strictly monies received, monies paid out basis. The set comprises

- ❖ The Receipts and Payments Account
- ❖ The Statement of Assets and Liabilities

The **Accounting Regulations** permit charities which are not companies to opt for receipts and payments accounts if their income or expenditure in any year is less than £100,000.

Receipts and payments account. A summary of the money transactions of an organisation over a defined time period (usually a year).

Reserves. Money or moneys worth taken from its accumulated **unrestricted fund** surpluses which has been set aside by an organisation for use in an emergency or times of financial difficulty. All organisations should have reserves. The size of the reserves should be related to the **risk** the organisation faces. For charities, the amount of money available to form the reserves can be determined as follows:-

Accumulated fund, less endowment fund, restricted fund and designated fund

If this amount is less than the trustees think appropriate, future budgets should be adjusted to make surpluses so that the reserves can be built up. If this amount is more, the trustees should make plans to spend the excess by expanding services or improving benefits. Generally, charities have no legal right to accumulate large surpluses.

Restricted fund. Funds granted or donated to, or raised by, a charity for a specific purpose within the objects of the charity, which can only be spent on that purpose. Miss-use of restricted funds is a serious breach of trust.

Revenue expenditure. Money spend on paying running costs. In practice, money spent on everything which isn't capital expenditure. See **Note 2**

Risk. An event or activity in the future which may or may not happen, but if it does, will have an adverse impact.

Single entry book-keeping. A system of book-keeping where each item of income or expenditure is recorded only once, either as a debit or as a credit.

SORP. See Charities SORP.

Statement of Assets and Liabilities. A list or table showing at the financial year end

- ❖ What assets you own, by type and (optionally) value
- ❖ Who owes you money and (optionally) how much they owe
- ❖ Who you owe money to and (optionally) how much you owe

Statement of financial activities (SOFA) A special type of income and expenditure account conforming to the **Charities SORP**. The SOFA summaries the origin, movement and end use of all the financial resources of a charity, including transfers between funds, during a defined time period (usually a year).

The Charity Commissioners for England and Wales. The civil servants who register and regulate charities.

Thresholds The income and/or expenditure triggers which determine the requirements for charities to register with the Charity Commission

- ❖ prepare accounts on a Receipts and Payments or Accruals basis
- ❖ make their accounts available to the Charity Commission
- ❖ have their accounts independently examined or audited

Current thresholds are:-

- ❖ Registration £1,000
- ❖ Accounts to Charity Commission £10,000
- ❖ Receipts and Payments Under £100,000
- ❖ Independent Examination between £10,000 and £250,000
- ❖ Audit Over £250,000

From early 2007, thresholds will be:-

- ❖ Registration £5,000
- ❖ Accounts to Charity Commission £10,000
- ❖ Receipts and Payments Under £100,000
- ❖ Independent Examination between £10,000 and £500,000
- ❖ Audit Over £500,000

Total expenditure The out-goings of the organisation for the financial year, excluding purchases of fixed assets and investments.

Treasurer. The management committee member responsible for ensuring that financial records are kept and financial information is made available to the management committee so that they can make decisions.

Trustees. The members of the management committee of a charity. The team of volunteers responsible in law for the day-to-day management of a charity.

Ultra vires. A legal Latin term (literal meaning “beyond strength”) used to describe the actions of trustees who have permitted a charity to engage in activities not covered by its **objects**. Acting ultra vires is a serious breach of trust.

Unrestricted funds. Funds which can be spent on any or all of a charity’s objects, as the trustees see fit.

Variable cost. An item whose costs change in proportion to the quantity used. See **Note 3**

Variance. A difference between an amount budgeted for an item and the actual amount of the item, whether incoming or outgoing. For income, an adverse variance is where the actual amount is less than the budgeted amount, and for expenditure, it is where the actual amount is greater than the budgeted amount. A positive variance is the opposite of these. In general, a positive variance is a good thing on an item of income, but not necessarily so on an item of expenditure, since it may indicate that something planned hasn’t happened.

Notes:-

Note 1:- In Local Government circles, capital and revenue expenditure have special meanings, since central government places restrictions on what local authorities can and can't do under these headings. These restrictions do not apply to the voluntary sector.

Note 2:- Custom and practice uses credit and debit to cover paying money (cash or cheque) into or drawing money out of a bank account. From your bank's point of view, when crediting your account, the bank is increasing a liability – the bank owes you more money. When debiting your account, the bank is decreasing its liability to you – it owes you less. If you kept double entry books, in your own accounts, these transaction would be the other way round. To avoid this confusion, it is best to use deposits when putting money into the bank and withdrawals when taking money out.

Note 3:- Staff is often treated as a variable cost, charged at a rate per hour. From an organisational view-point, labour is really a fixed cost, since the staff have to be paid regardless of the level of activity, and they can't be hired and fired willy-nilly.

Note 4:- The line between indirect costs (or overheads) and project costs can be difficult to draw, especially where costs are shared. In the end, it is a matter of what definition you use. For example,

- Does your definition include or exclude staff costs?
- Are all your core costs genuinely overheads?