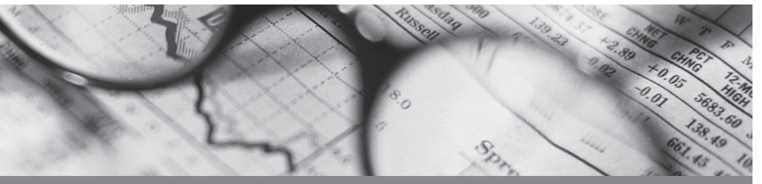
The Muttart Foundation

Alberta



Financial Responsibilities of Not-for-Profit Boards

BOARD DEVELOPMENT

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Financial Responsibilities of Not-for-Profit Boards

A Self-Guided Workbook

The Right to Copy this Workbook

An Important Note Before You Get Started

Not-for-profit organizations vary considerably in their make-up, their objectives and their methods of operation.

The information in this workbook is written generally and may not exactly fit the needs of your organization. It is meant to be a starting point for you to deal with some of the issues which face many not-for-profit organizations.

The publisher does not give legal or other professional advice. Therefore, if you are doubtful about acting on any information in this workbook, or want clarification, you may wish to seek professional advice to make sure it answers your concerns and issues.

The Muttart Foundation and the Government of Alberta are not liable if you use any of the contents of this workbook. Make sure you have the benefit of professional advice which relates directly to your organization.

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The Muttart Foundation
1150 Scotia Place
10060 Jasper Avenue
Edmonton, Alberta T5J 3R8
Phone: (780) 425-9616
FAX: (780) 425-0282

Alberta Culture and Community Spirit
Board Development Program
907, 10405 Jasper Avenue
Edmonton, Alberta T5J 4R7
Phone: (780) 427-2001
FAX: (780) 427-4155

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Introduction

Do you want to avoid that sinking sensation as a board member after you approve a budget or financial statement you did not understand? Financial Responsibilities of Not-for-Profit Boards is a self-guided workbook written for the policy governing board member who has little or no financial background. The workbook does not attempt to replace the need for sound and professional financial advice. However, for the non-financial board member, it provides basic information and practical approaches that transform a list of numbers into helpful information. Financial tools like the budget are broken into small steps that are easily followed. Especially important for the policy governing board are the links to policy that are identified at the end of each section. The appendix, the glossary of terms and the resources list provide additional helpful information.

Before getting started on the workbook, turn to Appendix 1 and find the Financial Management Checklist. Use this tool to help you determine what work, if any, the organization needs to get started working on.

Chapter One explores the roles and responsibilities of those in the organization who are involved in several aspects of financial management. The roles discussed are the Board, the Treasurer, the Finance Committee and the Senior Staff.

Chapter Two details the development of the budget and its relationship to planning. A step-by-step approach with illustrations lays out the process.

Chapter Three provides a broad overview of the basics of bookkeeping. This is intended to insure that the board member has been introduced to the parts that make up the financial cogs of the organization. This chapter also places an emphasis on establishing checks and balances to create an effective internal control system.

"information – the currency of good governance."
– *CCAF-FCVI 1997*

Reading financial statements is the focus of Chapter Four. Some basic accounting concepts are presented. As well, a series of questions is provided to equip the non-financial board members with a starting point for thought and discussion.

In Chapter Five other aspects of financial management are considered. Issues like, "When to Computerize?" "Payroll Deductions and GST Remittance," "Charitable Donations", "Workers' Compensation Board," "Money Management," and "Fund Development" are touched upon. Each chapter is meant to be a starting point for developing, implementing and monitoring the organization's financial policy.

The Appendix items are suggestions that you may find helpful in planning and managing financial affairs. The Glossary explains commonly used financial terms. There is a checklist for policy planning as well as a Financial Management Checklist. Also included is a sample financial policy. A sample job description for a treasurer is included which can be revised to fit your organization's needs. Also included is a published article which outlines ways to limit liability. This article can assist in priority areas when planning new policies. The resource list is extensive but by no means comprehensive.

On behalf of Alberta Culture and Community Spirit and The Muttart Foundation we hope that you find yourself on solid ground when you next approve a budget or a financial statement.

May you vote in a spirit of knowledge and confidence.

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Understanding Roles, Responsibilities and the Use of Policy

The board member of an established organization with a senior staff and support staff is in a very different position from the board member of an organization without staff. A board without senior staff assumes the administrative and managerial responsibilities of the senior staff. To help with the understanding of financial responsibilities, there needs to be a distinction made between those responsibilities of the board and those of management. These distinctions will help with the establishment of policies within which the board operates, and by which you are assured responsible financial management is in place.

There are four different bodies that can be involved in financial management. These are the board, the Finance Committee, the Treasurer and the senior staff. The existence of each depends on the size of your organization. If your organization is small, then it may only have the first and most important entity – the board.

As a board there are global duties to be fulfilled. These duties are:

Purpose: establishing the organization's purpose or mission.

Continuity: providing continuity for the management and the implementation of organization's affairs.

Progress: setting the rate of progress that the organization takes in reaching its mission.

Identity: securing community support and appreciation for the organization's objects, beliefs, vision, mission, and long-term direction.

"…before you accept a directorship…fully understand the responsibilities."
– *Volunteer Vancouver 1984*

BOARD MEMBER

Each member of the board of directors shares equally in the carrying out the mandate of the organization, as well as the responsibility of prudent management of the organization's finances. Financial management in a not-for-profit organization can be described as the managing and accounting of funds to ensure these funds are spent in accordance with board objectives. The effective acquisition, allocation and use of funds determines the extent to which goals and objectives of the board are realized.

Board members are responsible for the overall management of the organization's resources – the responsibility does not simply fall to the Treasurer of the organization. Board members can, in some instances, be held individually liable for debts of the organization in the event of non-performance.

These responsibilities cover many areas of operation. For example, as a board member you will be required to approve the budget. This means asking sufficient questions so that the budget is understood.

Does the budget reflect the organization's priorities?

What are the fundamental assumptions upon which the budget has been prepared (eg. inflation rates)?

Who is responsible for monitoring and controlling budget expenditures?

What are the board's budget policies that govern the preparation and control of the budget?

By asking these types of questions, the discussion at the board level focuses on the core issues of the organization. What are our risks to our organization? What are the strategies for handling these risks? These questions help to avoid the type of discussion that centers on operational expenses like the price of photocopying paper. A way to focus on the core issues is for the board to set written financial policies that keep board members focused on their role in the financial management function of an organization.

An added benefit of focusing the discussion on the core issues is that all members are placed on an equal footing. A board member without financial training can contribute to the discussion on an equal level to that of the financially trained board member. Keeping to the core issues will be helpful whether you are discussing the budget, the financial statements, the capital reserves or any other aspect of financial management.

It is the individual board member's responsibility to understand the financial information that is being presented. If they don't understand the information and how it relates to their organization, they will be unable to make informed decisions. Board members should not be afraid to ask for clarification on the financial information presented.

Board members may be liable if they are not fulfilling their individual responsibilities as board members. Individual responsibilities include: attending board or committee meetings; reading and understanding financial reports; understanding the board's financial policies; participating in approving the annual budget, audit, annual financial report and financial statements. These individual responsibilities, if carried out, minimize the situations where financial affairs are being conducted poorly or dishonestly.

Board members must not allow personal interests or those of a third party to conflict with those of the organization. When appropriate, the board member should declare to the board that they have a conflict or a potential conflict. They should withdraw from discussion on the issue and should not take part in a vote regarding the issue.

Funds must be used by an organization for the purpose intended. If they are not spent in accordance with funders' criteria, there is potential liability for the board.

Individual board members may be liable for payroll deductions for staff that are payable to Canada Revenue Agency and not remitted in a timely fashion. These include income taxes, Canada Pension Plan, and Employment Insurance deductions. There is also a liability for Goods and Services Tax remittances to Canada Revenue Agency. Organizations should have procedures in place to ensure these deductions are being remitted when required.

Authorized cheque signers in an organization assume a responsibility to ensure that they are signing cheques that have been prepared following board policy. The expenditures should be approved through a process such as the budget process. They do not assume any greater personal liability than other board members do, unless negligence of fraud has been identified. There should be no signing of blank cheques. The signing officers should not live in the same household, nor should they be related.

Professional accountants who sit on boards of directors do assume a greater legal responsibility for financial management than do other non-financial board members. They are assumed to have a greater level of skill in the financial area that they must apply to their responsibilities as board members.

FINANCE COMMITTEE

Depending on the complexity of the organization, the board may wish to have a Finance Committee. This Committee's terms of reference may be written to include some audit responsibilities. The Committee can be made up of two or more board members who meet throughout the year. The Committee may be responsible for reviewing the Treasurer's records and reports, for example. Usually a review is conducted at the end of the organization's fiscal year. The Committee reviews the budget prior to the board, monitors budget performance, reviews the financial statements as prepared by the external auditors. Following the review the Committee recommends to the board acceptance of the Committee's findings with respect to the budget and various audit reports.

The work of the Committee not only protects the organization but provides assurances to its members and supporters that finances are being handled appropriately.

AUDIT COMMITTEE

Once an organization reaches a certain size, it may require both a finance committee and an audit committee. The role of the audit committee would be to ensure that the audit is conducted in an efficient and cost effective manner, to oversee the financial systems and internal controls, to recommend approval of the annual audited financial statements to the board and to recommend the appointment of the external auditor.

If the organization does not need two separate committees, the finance committee may take on some of these roles or the board itself may fulfill some of the roles.

TREASURER

The Treasurer's function is to ensure management of the organization's finances and report either directly to the board of Directors or through the Finance Committee to the board of Directors. In addition to their responsibility as a member of the board, the Treasurer may maintain all bank accounts, supervise all financial transactions, monitor the organization's budget, report to the Board of Directors and general membership on finances, and prepare any required financial reporting forms. Some organizations delegate these functions to senior staff.

SENIOR STAFF

If an organization has senior staff, the board is responsible for defining the roles, responsibilities and authority this person needs to carry out their job. The senior staff (also called executive director, general manager or chief executive officer), ensures that the financial policies established by the Board of Directors are carried out. As well, they are responsible for the day to day financial transactions of the organization.

The following flow chart shows lines of authority in a Policy Governing Board (with senior staff) in contrast to an Administrative Governing Board (without senior staff).

Lines of Authority in a Policy Governing Board

The Board
authorizes the

Chairperson of the Board
to liaise with the

Executive Director
who supervises the

Staff
who implement board policy through program and services

Lines of Authority in an Administrative Governing Board

The Board
authorizes the

Executive Committee
to monitor and supervise the

Volunteer and Paid Staff
who implement board policy through program and services

SUMMARY

Sound financial management is one of the most important policy development and monitoring areas of a board of directors. Board responsibilities are somewhat different in an organization with senior staff compared to an organization without senior staff. Financial policy is developed to reflect these different roles and responsibilities facing these two types of boards.

Appendix 2 lists a financial policy checklist which will help to determine where policy needs to be developed or improved. Appendices 3 and 4 include sample policies both for governing board with senior staff as well as an administrative governing board without senior staff. These examples are intended to serve as a starting point for discussion for the organization. Appendix 5 includes a worksheet to develop the job description for the Board Treasurer. The organization may find other positions performing some of the tasks listed for the treasurer. Each organization is different but the important issue is that someone is identified as responsible for these tasks and that this decision be recorded.

Financial policy is written so that the roles, responsibilities and limits of authority of those responsible for financial management are clearly articulated. Using simple language with a straightforward tone is the way to ensure that everyone can read and understand what is meant by the policy.

CHAPTER 2

Planning and Tracking for Results

"The budget is the financial plan of action….."

"The budget is a working document which reflects the joint planning effort of many people."

The budget is the most important tool used by the board to ensure that its financial management responsibilities are being met. Most organizations prepare budgets on a regular basis and use them as both planning and controlling tools. Approval and monitoring of the budget is the most critical job of the board.

This chapter deals with many of the aspects of budgeting that not-for-profit organizations will encounter. In this chapter the basic elements of budget planning, budget control, cash budgets, flexible budgets, the capital budget and several other key aspects of budgeting within the not-for-profit setting are presented.

The first function of a budget is to record, in monetary terms, what the realistic goals and objectives of the organization are for the coming year or years. The budget is the financial plan of action based on the board's decisions for the future of the organization. The second function of the budget is to provide a tool to monitor the financial activities throughout the year. Properly used, the budget can be a guide which will help the board see when goals are met. For a budget to provide this type of information and control, five elements must be present:

1. The budget is thoughtfully prepared.
2. The budget is prepared and/or approved by the board.
3. The budget is broken down into time periods which match the time periods in the financial statements.
4. The financial statements are prepared on a timely basis throughout the year and compared to the budget right on the statements.
5. The board is prepared to discuss and possibly take action where a comparison with the budget shows an important difference from what was budgeted to what actually happened.

All of these five elements are discussed in this chapter, for budget control is the chief means of exercising the board's fiduciary responsibility. Fiduciary means the responsibility for funds which are entrusted to the board on behalf of the public.

BUDGET PLANNING

Budget planning is central to how the board exercises its responsibilities as financial managers. It is important that the board be able to link organizational goals and objectives to its resources.

The budget represents the end result of a review by the board of its objectives or goals expressed in monetary terms. The budget is a working document which reflects the joint planning effort of many people. The budget is meant to form the basis for action and has the support of the board.

Preparing an effective budget consists of the following five steps:

1. **List the objectives or goals of the organization for the following year.** These are the goals or objectives that have been established as part of a planning process that the board has undertaken. For many organizations this process will be essentially a re-evaluation of the existing grants or services. Care is taken to avoid deciding too quickly that an existing program continues unchanged. If several people in the organization are responsible for authorizing expenditures, the budget is structured so that only one person is ultimately responsible for each program or project. That person is responsible for setting the budget and ensuring that spending is within the approved budget.
2. **Estimate the cost of each objective or goal.** For continuing programs, last year's actual expense and actual budget are helpful in estimating this cost. In reviewing prior years' expenses, be sure to account for one-time expenses such as equipment purchases or special events that do not need to be included in the upcoming budget year. For new programs or modifications to existing programs, a substantial amount of work may be necessary to accurately estimate the cots involved. This process is done in detail since elements of a particular goal or objective may involve many categories of expenses and salaries.

   It may not always be necessary to adapt this specific program structure for an organization. If it is a new organization and has only one program or one service to deliver, structuring the budget is straightforward. In essence, the budget reflects the way in which an organization plans to do business. Do not underestimate costs.

3. **Forecast the expected income of the organization over the time period of the budget – usually one year.** For many organizations, contributions from the general public, generated by the organization's programs, and grants from government are the principal income. Careful consideration needs to be given to the expected revenues that may flow from these sources.

   Organization's estimates for income can be overly optimistic and this could prove to be the organization's downfall if there is no margin of error associated with budget planning. Organizations want to avoid the shock of discovery six months into the budget year that the expected revenues are not near the budgeted amount. This type of discovery can mean that drastic action with respect to the organization's commitments needs to be taken. Do not overestimate revenues.

4. **Compare the total expected revenue to the expense for achieving the overall goal.** First match the expenses with the revenue. If the organization is running a single service or limited number of services, then it is not necessary to do these kinds of allocations.

   The most critical element is to ensure that there is good information so that there are reliable income and expense figures. Ask the question, "Is it possible that the expenses have been underestimated or that the revenues have been overestimated?" If the organization has limited cash reserves or limited possibilities in terms of finding additional funding, then care needs to be taken when constructing the budget.

   Ensure safety margins are built into the budget. Allow leeway in preparing the budget in order to meet unexpected events. This kind of an allowance is normally referred to as contingency planning. Resist the temptation to set up a large contingency fund as an expense. Throughout the year, boards or staff may have a tendency to take anything extra that they want to do out of the "contingency fund" without the proper evaluation of the expense. There should be additional approval required in the process to spend contingency dollars, e.g. board approval.

5. **Present the budget to the board for ratification or approval.** Following a thorough discussion at the board, all members view the budget as the 'financial plan of action' for the coming year.

RESPONSIBILITIES FOR BUDGET PREPARATION AND CONTROL

While the process for budget preparation is generally understood, what happens after this is also important. The board needs to clarify who has responsibility for formulating the budget, and who ensures that it is moved to a committee of the board, and finally, to the board for approval. Figure 1 sets out a responsibility matrix for budget decision-making that an organization should complete when planning.

The preparation of the budget involves policy decisions in most organizations. The Treasurer may be the person best qualified to handle 'the numbers' but no single individual should make the policy decisions that grow from the budget. To avoid a situation where one person is formulating the budget as well as determining policy choices, a budget committee is formed consisting of key people from the board. This can mean that either the board is the budget committee or it appoints a sub-committee of board members.

It is important in the preparation of the budget that the role of the board is clearly understood. If the organization has no staff, then members of the board will be required to prepare the detailed budgets. If the organization has senior staff, then the board can delegate to the senior staff some of the responsibility for preparing a budget for the budget committee and the board's approval.

It can be useful to prepare budget guidelines. In this case the staff comes to the committee or the board seeking approval of basic budget guidelines. These guidelines provide estimates regarding inflation factors for salaries, supplies and other items which affect expenses and revenues.

"…it is useful to prepare budget guidelines…"

FIGURE 1
Budget Policy Responsibility Matrix

Resposibility	Senior Staff	Treasurer	The Board
For budget preparation			
For budget approval			
For budget monitoring			
For key expenditures decisions (purchase of capital items, hiring of new staff, and wage increases)			

Revenue budget categories may include:
- Grants
- Fundraising
- Donations
- Interest Income

Expense budget categories may include:
- Salaries
- Benefits
- Contracts
- Rent/Utilities
- Program Expenses

These and other key revenue and expenditure assumptions that form the budget are important elements for the board to consider before the budget numbers are calculated.

Approving the budget guidelines before a complete budget is prepared allows the board to take part in the budget planning early in the process. This approach also avoids a situation where board members see a vast amount of numbers they do not understand.

PREPARING THE REVENUE BUDGET

Revenue is the term for the money that comes into the organization through grants, donations and other kinds of income. Once the budget has been approved, the next step is to divide the budget into segments. These segments can be compared over time and used as a basis for monitoring. Some organizations do this by dividing the total budget by twelve and showing the resulting amounts as a monthly budget, which is then compared to actual monthly revenues and expenditures.

Monthly revenue and expense statements can produce results which are misleading. When the revenues do not occur on a regular basis throughout the year, then the budget and the reporting of actual revenues ca be quite misleading. Some grants are received in a lump sum in advance which is meant to cover several months of expenses. It may look as if the organization has a surplus of funds when in fact the organization may be short of operating funds by the end of the year.

One of the best ways to allocate the annual budget into a monthly or quarterly budget is to analyze the revenue pattern of the previous year. The following worksheet is an example. In Figure 2 the New Budget ($120,000) represents a $20,000 increase over the Actual Last Year ($100,000).

FIGURE 2
Last Year's Budget as a Basis for New Budget

	Step 1	**Step 2**	**Step 3**
	Actual Last Year	**Percent of Last Year's Total**	**New Budget**
Revenue			
First Quarter	$30,000	30%	$36,000
Second Quarter	$25,000	25%	$30,000
Third Quarter	$25,000	25%	$30,000
Fourth Quarter	$20,000	20%	$24,000
Total Revenue	**$100,000**	**100%**	**$120,000**

The steps involved in constructing this type of revenue budget are as follows:

Step 1

Summarize the revenues on the same basis as they were received last year.

Step 2

Calculate the percentage of the Total Revenues that each quarter's revenue represented.

Step 3

Forecast the New Budget based upon the same percentages for each quarter.

This approach will assist in the monitoring of the revenue budget.

If at the end of the first quarter total revenue of only $33,000 has been received, compared to an expected budget of $36,000, it is clear that steps need to be taken to balance the budget by year's end. Either the revenue has to be increased or expenditures need to be decreased. Without some action being taken by the board the organization will be in a deficit position. (That is, the expenses are greater than the revenue.)

FIGURE 3
Worksheet Preparing 1999 Expense Budget (in thousands)

Previous Year	Actual Current Year				Proposed Budget (for upcoming year)		
Preceding Year	To Date (10 Months)*	Estimate Balance of Year	Estimate for Year	Budget Current Year	Proposed Minimum	Proposed Maximum	Final

* Two months prior to year end start the preparation for the succeeding year's budget.

PREPARING THE EXPENSE BUDGET

Expenses are costs to the organization such as salaries and rent. Figure 3 shows an expense budget worksheet with areas for the previous year, actual year and the proposed budget for the new year.

The expense side of the budget is shown in the same way as the revenues. Generally, expenses tend to occur at a more uniform rate than the revenues although this is not always the case. The cost of fundraising events, for example, is not always uniform. In some ways, the expense side of the budget is more important than the revenue side because it may be easier to decrease expenditures than to raise additional donations. If the budget is regularly compared to actual expenditures it can be an effective tool to show unbudgeted expenditures.

However, a monthly revenue and expenditure report is recommended if the board needs financial information more regularly. In situations where revenues and expenditures are needing very close monitoring, monthly reports may be necessary.

One way of allowing the board to fully examine its options when setting a budget is to focus the discussion on the last three columns of the worksheet shown in Figure 3. This portion of the worksheet is shown here as Figure 4.

FIGURE 4
Proposed Budget

Proposed Budget for Upcoming Year

Proposed Minimum	Proposed Maximum	Final

Essentially there are two steps to this worksheet:

Step 1

Establish three columns for the proposed budget. The three columns are the minimums, the maximum and the final amount. As the board considers each program, it can record the minimum and the maximum it feels is appropriate. No attempt is made at the beginning to fix a final budget amount, instead all budget items are considered as to the minimum and maximum cost, and totals are made.

Step 2

After all programs have been considered and after a preliminary review of potential revenue has been made, the board is in a position to make decisions. This approach promotes board discussion about the activities of the organization as the board arrives at final estimates for expenditure purposes.

BUDGET MONITORING POLICY

Once the budget has been approved by the board, the next major task is to monitor it on a regular basis. The budget process does not end with the preparation of one year's budget. The budget must be monitored each month, or at least quarterly as the fiscal year passes in order to assess how the plans and estimates compare with the facts.

In addition to general monitoring, the board usually stipulates specific items that it approves. Generally the board approves the purchase of capital items, a lease of premises, the hiring of new staff and wage increases for the staff.

The board sets out in policy the frequency of reports on the budget and the key items for which the board expects to make decisions.

BUDGET COMPARISONS

Figure 5, "Statement of Revenue and Expenses and Comparison with Budget, for the month of June and for six months ended June 30, 1999" is a helpful structure to:

- allow a board member to compare the month's performance relative to budget and
- see whether the performance is favourable or unfavourable.

Also, the statement allows the reader to see the six month's performance and to review the variance from budget over this longer period of time.

The statement gives the reader information about the organization's activities for the two periods that are shown. It has the effect of alerting the reader to the fact that unless something happens, there may be a deficit for the year.

Take a look at the budget comparisons in Figure 5 for the Hole in One Golf Course and follow these steps to examine it.

FIGURE 5
The Hole in one Golf Course

Statement of Revenue and Expenses and Comparison with Budget for the Month of June and for Six Months Ended June and for Six Months Ended June 10, 1999.

MONTH (JUNE)

Revenue	**Actual**	**Budget**	**Variance Favorable (Unfavorable)**
Annual Dues	$15,650	$17,000	($1,350)
Initiation Fees	2,100	2,000	100
Greens Fees	4,750	4,000	750
Swimming	3,300	3,000	300
Other	6,710	8,000	-1,290
Total **(excluding restaurant)**	**$32,510**	**$34,000**	**$(1,490)**
Restaurant	37,850	34,000	3,850
Total Income	**$70,360**	**$68,000**	**$2,360**
Expenses			
Maintenance – Grounds	$14,650	$12,000	($2,650)
Maintenance – Buildings	3,450	3,000	-450
Golf Activities	13,500	10,000	-3,500
Swimming Pool	3,400	3,000	-400
Administrative	4,200	3,700	-500
Revenue Canada	3,700	3,500	-200
Other Expenses	4,150	5,000	850
Restaurant	29,550	27,000	-2,550
Total Expenses	**$76,600**	**$67,200**	**($9,400)**
Excess of Revenue over (under) Expenses	**($6,240)**	**$800**	**($7,040)**

2

1

FIGURE 5
The Hole in one Golf Course

Statement of Revenue and Expenses and Comparison with Budget for the Month of June and for Six Months Ended June and for Six Months Ended June 10, 1999.

6 MONTHS (JANUARY 1 – JUNE 30)

Revenue	**Actual**	**Budget**	**Variance Favorable (Unfavorable)**
Annual Dues	$81,900	$90,000	($8,100)
Initiation Fees	6,600	4,500	2,100
Greens Fees	11,000	8,000	3,000
Swimming	2,300	2,000	300
Other	18,250	14,000	4,250
Total **(excluding restaurant)**	**$120,050**	**$118,500**	**$1,550**
Restaurant	168,500	180,000	-11,500
Total Income	**$288,550**	**$298,500**	**$(9,950)**
Expenses			
Maintenance – Grounds	$37,650	$36,000	($1,650)
Maintenance – Buildings	18,100	19,000	900
Golf Activities	19,500	16,000	-3,500
Swimming Pool	5,100	4,000	-1,100
Administrative	24,150	22,000	-2,150
Revenue Canada	23,500	21,000	-2,500
Other Expenses	19,560	20,000	440
Restaurant	145,650	153,000	7,350
Total Expenses	**$293,210**	**$291,000**	**($2,210)**
Excess of Revenue over (under) Expenses	**($4,660)**	**$7,500**	**($12,160)**

4

3

Step 1

The budget planned to the end of June indicates a surplus of $800 (see reference 1).

Step 2

The actual revenues and expenses indicate a deficit of $6,240 for the month (see reference 2).

Step 3

The budget for the 6 month period to the end of June indicates a surplus of $7,500 (see reference 3).

Step 4

The actual revenues and expenses indicated for the 6 month period shows a deficit of almost $5,000 (see reference 4).

A board member reading the statement looks for any variance from the budget. This form of presentation makes it easier to identify the variance. Once the unfavorable variances have been pinpointed, the reasons for them can be explored. Board members then ask questions to determine if any action needs to be taken.

Both the current month and the year to date figures are shown in this example. Both are important. The monthly figures give a picture of what is currently happening. This cannot be learned from the six month figures. If only the six months were shown, a reader would have to refer to the previous month's statements showing the first five months to see what happened in June. It is important to have this distinction between the current month, its actual versus its budget and its variance, and year to date, which in this example is the most current six months.

CASH BUDGETS

The cash budget summarizes the estimated cash inflows (receipts) and cash outflows (disbursements) of the organization over a given time period, usually one year. It also shows the cash position normally on a monthly basis as well as for the entire period that the budget has been developed. It is the presentation of the flow of cash **in** and **out** of the organization that is extremely important for financial management.

The main purpose of the cash budget is to predict **when** and **by how much** the organization's cash resources will either be in **excess** or **below** the estimated requirements to cover the cash demands of the organization. Once the predictions have been made, management can begin to plan how best to utilize existing and expected cash resources. This includes funds secured from outside, such as banking arrangements. A cash budget is easy to prepare and is based on an established budget. Most of the information required for its preparation is contained in the operating budget.

Depending on the financial position of your organization, it may be appropriate to prepare the cash forecasts on a monthly basis. If the organization is experiencing some difficulties with cash flow, it is advisable to do the forecast more often, perhaps weekly.

Figure 6 illustrates a cash budget of a senior citizens' lodge operation. The cash position of the lodge for each month is shown.

The cash budget itemizes all the receipts and disbursements over the forecast period. Near the bottom of Figure 6 note the heading to 'Financial Transactions'. Here the organization's cash flow is being summarized.

For many organizations this type of budgetary cash flow forecasting is mandatory so that appropriate arrangements (i.e. loans) can be established with the bank in advance of the specific cash requirements occurring. Good planning helps to ensure that the organization has sufficient time to negotiate a loan on favorable terms or take other action aimed at reducing or eliminating the need for the loan.

The cash budget is vital in terms of planning for any borrowings, the repayment of debt and the efficient utilization of positive or excess cash balances. The cash budget should be reviewed periodically and corrections made and plans adjusted as the year progresses.

OTHER TYPES OF BUDGETS

Essentially the basic type of budgeting that has been described here is the **operating budget**. It has been used in order to explain and illustrate the process of budgetary planning and budget control. However, there are many other different types of budgets. Two other types of budgets are flexible budgets and capital budgets.

Flexible budgets are used when there is variability with respect to volumes. For example, if the organization is a retirement lodge and has a pattern of expenditures that is linked to the level of occupancy in the lodge, the board may find it helpful to look at the budget in terms of various occupancy forecasts so that they can monitor performance relative to occupancy levels. In this instance, the board could be looking at actual expenditures and comparing them to the budget for that level of activity. Clearly, when the budget is based on one level of occupancy, and indeed the occupancy level is lower – the expenditures should be correspondingly lower.

Depending upon the specific circumstances the organization is addressing it may be useful to develop both an operating and a capital budget. A capital budget could be formulated where a major purchase or acquisition is contemplated.
An example is the purchase or construction of office premises for the society. In these circumstances the benefits that will be gained from the acquisition of the office building extend beyond one year – the normal period for the operating budget.

The funds for the capital acquisition may be distinct and separate from the funds for operating purposes and the society may need to repay the funds (e.g. a mortgage) over a longer time frame. To cover the costs of a major project, the society may accumulate capital reserves, arrange a mortgage or bank loan or launch a specific fund development campaign – all of which

FIGURE 6

Sunnybrook Senior's Lodge

Monthly Cash Budget Fiscal Year 1994

ITEM **Receipts from Operations**	**January**	**February**	**March**	**April**	**May**	**June**	**July**
Rentals							
Initiation Fees							
Guest Fees							
Restaurant and Gift Shop							
Other							
Total Operating Receipts	**$31,310**	**$28,270**	**$30,320**	**$28,470**	**$27,065**	**$26,615**	**$26,665**
From Other Sources							
Contributions							
Investment Income							
Sale of Property							
Total Nonoperating Receipts	**$6,200**	**$30,460**	**$6,410**	**$4,400**	**$3,350**	**$2,300**	**$2,275**
Total Receipts	**$37,510**	**$58,730**	**$36,730**	**$32,870**	**$30,415**	**$28,915**	**$28,940**
Disbursements For Operations							
Salaries and Wages							
Supplies							
Maintenance							
Merchandise for Sale							
Food and Beverages							
Contractual Services							
Administrative Expenses							
Taxes and Insurance				18,000			
Total Disbursements for Operations	**$37,675**	**$25,525**	**$25,655**	**$43,575**	**$25,425**	**$26,925**	**$27,025**
For Other Purposes							
New Construction							
Repayment of Long-term Debt			7,850			7,850	$0
Purchase of Fixed Assets	$0	4,000					
Total Other Disbursements	**$0**	**$4,000**	**$7,850**	**$0**	**$0**	**$7,850**	**$0**
Total Disbursements	**$37,675**	**$29,525**	**$33,505**	**$43,575**	**$25,425**	**$34,775**	**$27,025**
Net Receipts (Disbursements)	**($165)**	**$29,205**	**$3,225**	**($10,705)**	**$4,990**	**($5,860)**	**$1,915**
Financial Transactions							
Beginning Cash Balance	5,500	5,335	4,540	4,765	4,060	4,050	4,190
Cash Available	$5,335	$35,540	$7,765	($5,940)	$9,050	($1,810)	$6,105
Sale (purchase) of Securities		-30,000	-3,000	10,000	-5,000	6,000	-2,000
Short-term borrowing (repayment)							
Ending Cash Balance	**5,335**	**$5,540**	**$4,765**	**$4,060**	**$4,050**	**$4,190**	**$4,105**

FIGURE 6 contiued
Sunnybrook Senior's Lodge
Monthly Cash Budget Fiscal Year 1994

ITEM Receipts from Operations	August	September	October	November	December	Total
Rentals						
Initiation Fees						
Guest Fees						
Restaurant and Gift Shop						
Other						
Total Operating Receipts	**$28,365**	**$30,270**	**$31,760**	**$34,255**	**$27235**	**$350,600**
From Other Sources						
Contributions						
Investment Income						
Sale of Property						
Total Nonoperating Receipts	**$2,250**	**$2,225**	**$1,200**	**$1,200**	**$1,200**	**$63,470**
Total Receipts	**$30,615**	**$32,495**	**$32,960**	**$35,455**	**$28,435**	**$414,070**
Disbursements For Operations						
Salaries and Wages						
Supplies						
Maintenance						
Merchandise for Sale						
Food and Beverages						
Contractual Services						
Administrative Expenses						
Taxes and Insurance					30,000	$48,000
Total Disbursements for Operations	**$27,365**	**$27,665**	**$26,415**	**$27,435**	**$59,615**	**$380,300**
For Other Purposes						
New Construction				10,000	25,000	
Repayment of Long-tern Debt		7,850			7,850	
Purchase of Fixed Assets	11,000		$0			
Total Other Disbursements	**$11,000**	**$7,850**	**$0**	**$10,000**	**$32,850**	**$81,400**
Total Disbursements	**$38,365**	**$35,515**	**$26,415**	**$37,435**	**$92,465**	**$461,700**
Net Receipts (Disbursements)	**($7,750)**	**($3,020)**	**$6,545**	**($1,980)**	**($64,030)**	**($47,630)**
Financial Transactions						
Beginning Cash Balance	4,105	4,355	4,335	4,880	4,900	$5,500
Cash Advance	($3,645)	$1,335	$10,880	$2,900	($59,130)	($42,130)
Sale (purchase) of Securities	8,000	3,000	-6,000	2,000	17,000	
Short-term borrowing (repayment)					47,000	47,000
Ending Cash Balance	**$4,355**	**$4,335**	**$4,880**	**$4,900**	**$4,870**	**$4,870**

Figure 6

Sunnybrook Senior's Lodge

By following the steps outlined below you will see how the cash balance can change over the year and by tracking it, the organization can forecast its cash position and any borrowing required.

Step 1
The cash balance at the beginning of the year is $5,500 (see reference 1). In January the Lodge receives $37,510 (reference 2) and disburses $37,675 (reference 3), resulting in $165 (reference 5) less in cash at the end of January.

Step 2
The cash balance, therefore, at the end of January is $5,335 (reference 4) which is the opening balance of $5,500 minus the change in cash ($165) at the end of January.

As the year proceeds the organization is purchasing or selling securities (see line 29) in an attempt to maintain an ending cash balance every month that is between $4,000 and $5,000.

In this illustration the only short-term borrowing (line 30) occurs in December in order to meet construction obligations and the payment of property taxes and insurance.

are not the typical funding sources for the operating programs.

If an organization has capital assets, they may have a policy that requires them to be capitalized and amortized. If an organization has more than $500,000 in revenues annually, they are required to capitalize and amortize their capital assets. This concept means that capital assets such as a building or a computer system is expensed over a number of years which is the useful life of the asset to the organization. This expensing is called amortization. If you have capital assets and are amortizing them, it is important to budget for amortization, even though it does not involve an outlay of cash. It does have an impact on the financial position of the organization at the end of the year.

Small organizations can expense all of their capital assets in the year that they are purchased. Organizations that are required to capitalize can set a policy on what level they consider the item as a capital asset. For example, they may set this level at $1,000. Any asset that costs $1,000 or more, would be capitalized. Anything under $1,000, they would expense. The level should be reasonable for the size of the organization.

Whether assets are capitalized or not, the cash that is paid for them should be included in the cash budget at the full amount.

When the organization decided to establish a capital budget, the amounts to purchase or build the facility together with the source of funds to cover the costs of the project are presented for approval by the board. This capital amount will be shown in the financial statements.

SUMMARY

For the important aspects of budgeting, the board establishes policies that address the key areas of the budget. These policies are set out for everyone's understanding and usually include:

- the frequency with which the board wants to receive budget reports;
- the expected type of information that the board wants to receive in order that it can be assured it more fully understands what is happening with the various programs of the organization; and,
- policies with respect to the cash budget of the organization and requirements on management to maintain minimum cash balances.

In summary, the budget policies of the board help create the appropriate degree of board participation in budgetary planning and control. As well, policy can create the trigger mechanisms for board involvement and action whenever the early warning mechanisms indicate potential trouble. Finally, the existence of budget policy gives assurance that responsibilities are assigned and the basis for board involvement are known.

CHAPTER

3 Making Sure the Accounts are in Order

This section of the workbook will address the following accounting topics:

- the establishment and maintenance of bank accounts, bank records and other financial records of the organization;
- matters related to internal control; and
- the roles and responsibilities of the various bodies within the organization including the Board, the Finance Committee and the Treasurer.

This discussion will focus on the needs of the smaller organizations rather than the larger organizations. This section covers the basic elements of bookkeeping.

OPENING A BANK ACCOUNT

One of the first tasks of the organization is to establish a bank account. The selection of the bank can be based on the fees and services provided. Many financial institutions waive service fees for charitable organizations. Ensure that the account you set up will provide you with a bank statement and the cancelled cheques each month. The bank provides you with the forms associated with opening an account, one of which permits the bank to open an account in the name of the organization. It authorizes the bank to accept deposits and to honour the cheques drawn in the name of the organization. The Board of Directors needs to make a motion to authorize the opening of the account.

The board gives the authority to individuals to make transactions on the account. This is an important board decision. One of the signatures

“…although it is unusual, banks make errors that need to be corrected.”

on the cheques written on the organization’s account should be the Treasurer. This is the individual the organization has asked to take on some of the financial responsibilities.

There must be two signatures on every cheque. Another signing authority might be an officer of the board or the senior staff. Having at least two signatures on the cheque is a procedure to ensure that at least two individuals have the opportunity to look at the request for the expenditure. As well, this ensures the expenditure is in line with the budget and board policy. Avoid presigning cheques. This negates the control of having two signatures. If cheques must be presigned, establish other controls as a way of ensuring that the risk of inappropriate cheques being written is minimized. The board decides what is safe and appropriate for the organization in terms of its banking policy. It considers what is practical and what risks are acceptable in order to be efficient.

RECONCILING A CHEQUING ACCOUNT

It is important to reconcile the chequing account each month to ensure that the balance in the chequebook is correct. Also, although it is unusual, banks make errors that need to be corrected. When the organization receives its bank statement each deposit in the chequebook should be checked against the bank statement. The easiest method is to follow the procedures that are outlined on the back of your bank statement on how to prepare a bank reconciliation.

Normally the bank statement is received several days after the end of the month. This time lag means that new transactions have occurred since the bank’s closing date. These transactions can probably be ignored during the reconciliation. One can select any date for reconciliation but it is easiest if the ending date of the bank statement is selected. If a monthly report is prepared, then itis important to reconcile to the last transaction included in that monthly report.

Every organization needs to maintain a file of bank statements and cancelled cheques. After the bank account has been reconciled (on the front or back of the bank statement or on another piece of paper) it is stapled to the bank statement so it does not get lost. The statements are filed by month. Deposit slips are stapled to each statement or if too numerous, can be kept in their own file. Cancelled cheques are filed chronologically by date written, which usually means by cheque number in the order they were entered into the chequebook.

FINANCIAL RECORDS

The key to financial records is, "Can the reports be prepared easily, accurately and on a timely basis form these records?" If the organization is relatively small and with one program, the chequebook may be an adequate source to keep the financial records.

As the organization grows, and the number of transactions increases, additional records need to be kept. Even a small organization may receive a significant number of revenues from a variety of sources. In this case, the chequebook alone is not an adequate record.

The two basic records needed are the cash receipts journal and cash disbursements journal.

CASH RECEIPTS JOURNAL

Figure 7 is an example of a record of the financial transaction that occurs when the cash changes hands. The cash receipts journal is a listing of all the cash receipts in the order they were received. Each amount is assigned to the appropriate category. To record this information, use accounting paper which can be purchased in stationery stores. These forms make it easier to keep the financial records in the appropriate journals. The columns in the journal should be labeled to correspond with the line items in the budget. A line item is considered one type of revenue that is separately recorded. An example of this is a government grant, a fee for service, or a donation. This makes preparation and presentation easier.

There does not have to be a column for every item. A miscellaneous column can be very useful, particularly if it is occurring less frequently – once a month or so. As the money is received, each receipt is entered, noting the date and its source. The total amount received is entered in the first column under cash. Then moving across the same row enter it again under whatever category is appropriate. Figure 7 provides an illustration of the Cash Receipts Journal for the XYZ Society.

FIGURE 7
Cash Receipts Journal

XYZ SOCIETY

	200X					**Dance**	**Miscellaneous**	
	Date							
1	9	29	**Received From**	**Cash**	**Contributions**	**Income**	**Item**	**Amount**
2			J. Jones	225.50	225.50			
3			B. Booth	195.00	195.00			
4	9	30	Jones Supplies	80.67	80.67			
5			**Total September**	**501.17**	**501.17**			
6								
7	10	2	Audrey Smith	200.12	200.12			
8	10	6	Harriet Hamel	125.00	125.00			
9			Quick Copies	41.00			Refund	41.00
10			Hugh Love	140.83	140.83			
11			Susan Smith	200.00	200.00			
12	10	10	R. Mitchell	100.00	100.00			
13	10	12	S. Gramiak	1,200.00	1,200.00			
14	10	20	G.M. Berry	200.00	200.00			
15	10	21	Dance Proceeds	1,219.07		1,219.07		
			Bruce Smith	100.00	100.00			
16	10	22	James Kernel	100.00	100.00			
17	10	27	Marilyn MacDonald	215.00	215.00			
18			Ken Kwan	200.00	200.00			
19	10	28	William Wand	100.39	100.39			
			Kathleen Kwack	200.00	200.00			
20	10	30	Cola Inc.	82.00			Deposit	82.00
21			**Total October**	**4,423,41**	**3,081.34**	**1,219.07**		**123.00**

FIGURE 8
Cash Disbursements Journal

XYZ SOCIETY

	200X								**Miscellaneous**	
	Date									
			Payee	**Cheque #**	**Cash**	**Phone**	**Copying**	**Postage**	**Item**	**Amount**
1			Forward		529.00		90.00	73.00		366.00
2	10	18	Repair Works	122	112.00				Repair Calculator	112.00
3	10	23	The Legion Hall	123	400.00				Dance	400.00
4	10	23	The Copy Company	124	30.00		30.00			
5	10	27	Party Party Party	125	39.00				Dance	39.00
6	10	28	Telephones Never Forget	126	229.00	229.00				
7	10	30	H. Snow & the Snowflakes	127	800.00				Dance	800.00
8	10	30	The Post Office	128	83.00			83.00		
9			**Total – October**		**2212.00**	**229.00**	**120.00**	**156.00**		**1717.00**
10					A	B	C	D		E

CASH DISBURSEMENTS JOURNAL

The Cash Disbursements Journal shown in Figure 8 is a listing of the cash spent in the order that it was spent. The expenditure is then put into the correct category. There does not have to be a column for each expense category. A miscellaneous column can be used for less frequent disbursements.

Both journals use a system that is referred to as “double-entry bookkeeping”. In the Cash Disbursements Journal this means that each cash disbursement is recorded and then the appropriate category is also recorded for the expenditure. Each line must add across. At the end of the month, each column is added. The total of all the categories must equal the total cash column. (“B” + “C” + “D” + “E” add together to equal “A”).

PETTY CASH

To allow for small payments that may be required "on the spot" or for items that are too small to write a cheque for, a petty cash system may be established. This is done through board policy.

The amount of petty cash that may be required is determined by the organization, usually from $50.00 to $200.00. A cheque is written for this amount and cashed. It is important that the petty cash be controlled by one person who is accountable for the funds. The petty cash should be kept in a secure location. To make a disbursement from petty cash, a petty cash voucher should be filled out. It is preferred that a receipt is turned in at the same time, however, sometimes the cash is given out first. In either case, a voucher should be filled out. When the receipt is received, it should be stapled to the voucher. The amount of cash and receipt totals in the petty cash should always add up to the amount of the original petty cash cheque. When the amount of cash runs low, the receipts are added up and a new cheque written to the individual in charge of petty cash. The receipts are expensed to the appropriate expense account in the accounting records. The petty cash should be checked from time to time by a person other than the one in charge of the petty cash to ensure that the funds are being properly managed.

Treasurer's Report
"A report that people understand is better than one with too many confusing details."

THE TREASURER'S REPORT

The Treasurer of any organization reports on the financial transactions to the board. This report is made monthly. If the organization meets every two months or quarterly it may be enough to report at each meeting. The purpose of financial reporting is to make sure that the board understands the financial position of the organization. With that understanding, the board can make important decisions based upon good financial information. No matter how often the board meetings are held, it is still useful to give board members the Treasurer's Report monthly in writing and a week before the meeting.

The Treasurer's Report for a smaller organization simply lists:

a. the name of the organization;
b. the period which the report covers;
c. the cash balance at the beginning of the period;
d. the income received during the period;
e. the expenses paid during the period;
f. the cash balance at the end of the period; and
g. the signature of the Treasurer.

The cash balance at the end of the period should agree with the balance on the bank reconciliation. The formatting is optional. Figure 9 is provided here for the XYZ Society. It is useful both as a report to the Board of Directors or for a general membership meeting. Accuracy is important but great detail is not.

FIGURE 9
Treasurer's Report for the Month Ended October 31, 1999

1	Cash balance, September 30		6,800
2			
3			
4	Revenue:		
5	Donations	3,080	
6	Proceeds from Social	1,219	
7	Other	123	**4,422**
8			**11,222**
9			
10	Expenes:		
11	Social	1,462	
12	Telephone	229	
13	Copying	120	
14	Postage	156	
15	Stationery	142	
16	Other	112	**2,221**
17			
18	Cash balance, October 31		**9,001**
19			
20			
21			
22			
23	*Sharon McNalley, Treasurer*		

The Treasurer's Report does not need to show every single transaction that occurs during the period. In reporting revenue and expenses only the significant items are shown with smaller amounts combined under the category "other". A report that people understand is better than one with too many details.

The Treasurer's Report is written and there are copies for all members who will be present at the meeting when the report is presented. Members receive the report in advance of the meeting.

The report follows the same format as the budget so that the categories for revenues and expenditures on

Internal control

"the person who approves a bill to be paid is not the same person who signs the cheque to pay it."

the Treasurer's Report align with the budget. The reporting is consistent from one report to the next. Items may get added from time to time but the order is maintained. This makes it possible for the board to compare the reports from month to month and year to year.

INTERNAL CONTROL

Internal control refers to the procedures adopted by the organization to prevent fraud and detect errors, and to ensure the timely and accurate reporting of financial information. The board puts in place policies that help to ensure the operation is appropriately controlled. Taken together the procedures form a system of control that needs to be understood by the whole organization.

Internal Control is a system that tries to make sure that money is being spent in a way that the board wants it to be spent. It also provides some assurance that the money or other things of value do not disappear and that mistakes do not occur. For example, one of the basic elements of good internal control is that no one person should handle all aspects of any financial transaction. This is referred to as the segregation of duties. It creates an internal system of checks and balances.

An example of segregation of duties is that the person who approves a bill to be paid is not the same person who signs the cheque to pay it.

Similarly the person who authorizes the transaction is not the person who records it in the accounting records.

It is often the case in smaller organizations with no paid senior staff, that the Treasurer is doing both functions. It may not be easy or practical to involve several people in the financial transactions. It is important to recognize that there are limitations to the amount of internal control that can be placed on the organization. If the organization finds itself in this position, then perhaps a Finance Committee might help to "segregate" the duties.

CASH RECEIPTS

Cash and cheques are deposited in the bank as soon as possible. It is best if only one person, i.e. the Treasurer, handles all the receipts. If any of the other members of the organization receive money, they record the payor and the amount and turn it over to the Treasurer as soon as possible.
The Treasurer also counts the money received and gives the person a receipt indicating the amount received.

CHARITABLE RECEIPTS

A not-for-profit organization that has received registered charity status from Canada Revenue Agency (CRA) can issue charitable donation receipts. They are also referred to as tax receipts. Tax receipts can be issued under the following conditions:

- Transfer of property (not services) to a charity
- Transfer is made voluntarily
- Donor receives no benefit in return
- Must be philanthropic for the good of society

If the organization is a registered charity, receipts for donations must be fully controlled.

- A sequentially numbered receipt book with double copies is needed.
- Donations can be issued as soon as a donation is received or at one time during the year, such as at the end of the calendar year. It is recommended that receipts be issued as soon as possible after a donation is received.
- Charitable donation receipts must contain:
    - Statement that this is an “Official Receipt for Income Tax Purposes”
    - Charitable taxation number
    - Name and address of charity as recorded with Canada Revenue Agency (CRA)
    - Place or locality where receipt was issued
    - Name and address of donor, including first name and initial if an individual
    - Amount of cash donation or fair market value of gift
    - If cash donation – day or year when charity received donation
    - If non-cash donation – day when charity received donation, brief description of property, name and address of appraiser if appraisal done
- If another receipt is issued for the same donation, the words “this receipt replaces receipt #___” must be clearly shown
- Spoiled or voided receipts are kept in the receipt book
- Receipts for other than charitable donations should be issued with other kinds of receipts.

Unused receipts must be kept secure and must be able to be accounted for.

It is important to ensure that charitable donation receipts are issued in accordance with Canada Revenue Agency (CRA) guidelines. These are available on the Canada Revenue Agency (CRA) website at www.cra-arc.gc.ca or at your local taxation office.

Finance Committee

"The first task of the Finance Committee is to make sure a system exists for keeping tack of the cash…"

CASH DISBURSEMENTS

Any invoice or bill is approved for payment by the person who knows why the expense was incurred. For internal control purposes, it is better that it be someone other than the Treasurer. The authority to approve invoicing is restricted to the President or the committee chairs. The minutes of the Board of Directors record who can approve invoices.

There should be a requirement for receipts to be presented for reimbursement if individuals have paid for something on behalf of the organization. If a receipt is not available, there should be a voucher filled out with an explanation as to why a receipt is not available. Approvals for reimbursement should be by someone other than the individual that is being reimbursed. If a number of individuals are being reimbursed on a regular basis, a claim form or expense report should be developed for the organization's use.

From a practical standpoint, if most of the invoices originate with someone other than the Treasurer, few difficult or complicated situations should arise. The Treasurer is assured that any time a bill is received, approval is indicated by signature and the date. As the invoices are paid, the cheque number is written on the invoice and it is filed in numerical order.

If the organization writes more than 30 cheques a month, it is appropriate to consider filing the invoices alphabetically by payee. The rule to follow is, set up a payment system that prevents an invoice from being paid twice and a filing system that allows each invoice to be found easily when needed.

BANK RECONCILIATION

All of the organization's bank accounts are reconciled each month. The best internal control is to have the bank mail the statements to someone who is not a cheque signer. They reconcile the account independently of the Treasurer. If this is not practical, the Treasurer can reconcile the bank account each month. However, the reconciliation should be regularly reviewed by another board member. This is an important control and should not be overlooked.

FINANCE COMMITTEE

An organization with a volunteer Treasurer and a volunteer board may not require a complex accounting structure or an audit process involving external auditors. Organizations receiving grants usually require audits or at least a review of their financial reports by an external auditing firm. One of the ways that the board can be more certain about the financial management of the affairs of the organization is to appoint a Finance Committee and delegate some audit responsibilities to it. This committee, in addition to its audit responsibilities, may be the committee that would prepare the budget and review the monthly statements on behalf of the board. The committee would report any outstanding items to the board.

The purpose of the Finance Committee is to protect both the organization and the Treasurer. An audit gives the organization's supporters confidence that financial matters are properly handled. It gives the Treasurer a feeling of completion of the year's work and protects the Treasurer, to some extent, from criticism from other members of the board and society members.

The first task of the Finance Committee is to make sure a system exists for keeping track of the cash receipts and disbursements. This system should allow the Treasurer to make reports to the board on a regular basis.

The Finance Committee should physically examine the financial records by:

- reviewing the cash receipts;
- ensuring that all receipts are listed by date received, name of the payer and the reasons for receipt;
- reviewing all disbursements in the cash disbursements journal. These are listed by date paid, name of payee and the reason for payment. The cash receipts journal and the cash disbursements journal, as mentioned earlier, may actually be the chequebook.

All disbursements are proven by an invoice and these should be filed by the paid date or by vendor. The cheque number and paid date are written on the invoice. The Committee examines a random selection of invoices to ensure the organization's approval system is being followed. If there are unusually large dollar items, they are examined.

The same process is followed by the Committee with respect to examining the cancelled cheques, examining the bank accounts, and the monthly bank reconciliations, looking at the unpaid bills and the amounts due at the end of each year.

When examining the salaries and wages account the Committee should check that the pay rates are those approved by the Board of Directors and are recorded in the minutes. The Committee should also examine copies of the payroll remittances to be sure that withholdings for income tax, Canada Pension Plan and Employment Insurance (EI) are remitted to Canada Revenue Agency (CRA) on a monthly basis. Board members may be personally liable if these remittances are not made.

In reviewing the Treasurer's report the Committee checks that the year end totals in the cash receipts and cash disbursement records agree with the report. After the Finance Committee is finished its review, a written report is prepared for the board.

The board ensures the expectations or duties it assigns to the Finance Committee are clear and written in policy. It is useful to record these specified duties and responsibilities as outlined above in the minutes of the board.

GETTING ASSISTANCE

This chapter demonstrates some straightforward ways to set up a set of accounts. The board then ensures that the financial operations of the organization are being appropriately recorded, regularly reported and periodically cross-checked.

It may be helpful for the organization to view its record of accounts and its process with an accountant. This will mean that the board can be assured that major elements of control in the system are not missing.

This will ensure the proper safeguarding of the organization's resources. As the organization grows and the management of its finances becomes more demanding, the board may wish to hire a bookkeeper. The accounting position may report to the senior staff. Smaller organizations are finding that sharing the services of one bookkeeper not only meets their needs, but also keeps their expenses down. If the organization is very small, these responsibilities could be fulfilled by a senior staff with some accounting training. It may be useful to consult a professional accountant to help define the responsibilities for the position.

An organization may require the preparation of financial statements, an audit, or a review by a third party. These services are normally provided by an accounting firm. Audited statements contain an auditor's opinion that they believe that the statements are a fair representation of the financial position of the organization at year-end. A review is less expensive, and does not provide the same level of assurance.

The accountant's opinion in a review states that nothing has come to their attention that causes them to believe that the statements are not fairly stated. The level of work required in a review is less than in an audit.

By-laws of organizations established under the Societies Act may include a provision that allows for two members (not on the board) of the organization to perform an audit. The organization should ensure that these individuals have the appropriate knowledge to carry out the audit.

In Alberta, an accountant performing audit or review services must be a member of one of the three accounting bodies recognized in legislation as able to provide these services. These accounting bodies are the Certified General Accountants Association (CGA), the Institute of Chartered Accountants (CA) and the Society of Certified Management Accountants (CMA). Each body has set criteria for registering within their own organization for members to be able to perform these services, even for not-for-profit organizations.

The necessary financial statements that need to be prepared include the statement of financial position or balance sheet; the statement of operations or income statement; the statement of changes in net assets or fund balances; and the statement of cash flows or the statement of changes in financial position. In addition, there are notes to the financial statements that provide further explanation of certain items listed on the statement of financial position or the statement of operations. Chapter 4 covers reading a financial statement.

CHAPTER

4 Reading a Financial Statement

The Financial Statements of an organization are a widely used and helpful way to get a clear picture of the organization's financial health. The statements are a necessary part of the information required to make decisions about the present and future direction of the organization. A donor may wish to see how previous donations have been used. Many foundations, corporations and funding bodies expect financial statements to be included in fund requests. Potential board members or employees may wish to read the financial statements so they can determine the financial stability of the organization before they get involved.

A word to the wise. If you approve the financial statements at a board meeting, that means you understand and agree with the information presented. Take the time you need to understand the statements before you record your approval by your vote.

AUDITOR'S REPORT

If the organization has been audited by an external auditor, the auditor will give their opinion as to whether the financial statements fairly reflect the financial picture of the organization for a particular period and at a particular point in time, usually the year-end. They also report whether the statements are presented in accordance with "generally accepted accounting principles". Generally accepted accounting principles (GAAP) are broad and specific rules adopted by the accounting profession as guidelines for measuring, recording and reporting the financial transactions and activities of an organization.

Accounting standards were developed specifically for not-for-profit organizations as they are becoming a larger and larger part of the economy as well as other trends in the not-for-profit sector. It was felt that there should be more of a reporting

"If you approve the financial statements at a board meeting, that means you understand and agree with the information presented."

responsibility for these organizations. This led to thinking about guidelines which led to the development of standards. In addition to this, funders and other financial statement users wanted some kind of consistent reporting for not-for-profits.

If an auditor is comfortable that they have had access to all of the information of the organization and that it has been presently completely and accurately in accordance with generally accepted accounting principles, they will give an unqualified opinion. If they have not been able to verify certain information or the information is not presented in accordance with GAAP, they may present their opinion with reservations. This is also referred to as a qualified opinion. The most common qualification is the verification of revenues where the auditor has been unable to determine if all the revenues have been included in the financial report.

FINANCIAL STATEMENTS

The new accounting standards for not-for-profit organizations changes the more common names for the reports that make up the statements. Statements that are prepared by an organization on a monthly or quarterly basis typically include the statement of operations and the statement of financial position. A statement of cash flows may or may not be prepared.

Financial statements normally include four reports plus notes. These statements are the statement of financial position also known as the balance sheet; the statement of operations also known as the income statement; the statement of changes in net assets or fund balances; and the statement of cash flows also known as the statement of changes in financial position. In this chapter we will look at the purpose of these statements and how to read them to get an understanding of the information they contain. Following the description, a sample statement is presented with key questions or observations which will equip the board members with some tools to approach the sometimes confusing “lists of numbers”.

STATEMENT OF OPERATIONS

This statement is also sometimes called the income statement, the revenue and expenditure statement, the operating statement or the profit and loss statement. This report shows what an organization received as income (revenue) and what was spent over a period of time (expenditures or expenses). Funds (money) that come into the organization are called revenue and funds that are spent are called expenses or expenditures. The difference between what was received as revenue and what was spent as expenses is either a surplus (more revenue than expenses) or a deficit (more expenses than revenue). The surplus or deficit is reported on the bottom line.

Key facts to keep in mind when reading the statement:

- This is a consolidation of regular reports received monthly or quarterly.
- The budget categories and the revenue and expense categories should be the same from period to period so that they can be compared. An auditor may change some of them to conform to certain reporting requirements.
- The headings on the statement include the name of the organization, the statement of operations and time period being reported.

REPORTING OF CONTRIBUTIONS

The new accounting standards introduced new methods of reporting contributions. A contribution is the transfer of assets or resources to an organization with nothing given in return. Examples include: government grants, foundation grants, and donations. Things not considered to be contributions would be membership fees, fee-for-service revenue, and fund raising event revenue.

Contributions can be restricted by the contributor as to how the funds are to be used. The restriction can be for a specific program or to be matched to a particular expense or to be added to an endowment fund which is required to be kept permanently by the organization. They can be unrestricted which means the organization can plan how to use the funds.

Organizations can determine how they want to report their contributions in one of two methods. These are the restricted fund method and the deferral method.

RESTRICTED FUND METHOD

To use the restricted fund method, the organization would be using fund accounting which is matching revenues and expenses to specific purposes. They are reported on separately. For example, all funds related to capital assets would be recorded and reported in a separate fund.

The restricted fund method treats the flow of funds in the same manner as a cash method of accounting. The revenues and expenses of restricted contributions are not matched. For example, if a three year grant is received in one year, the total grant is recognized as revenue in year one. There is a surplus in the fund at the end of the year which is drawn down each year of the three years. At the end of year three there is a surplus or deficit for the total grant.

In reporting using this method, there are no unrestricted revenues reported in the restricted fund. All unrestricted revenues are reported in the general fund. They may be transferred to the restricted fund through an interfund transfer at the end of the year.

The statements of the organization would show several columns for the various funds of the organization.

FIGURE 10
Statement of Operations
Helping Hand Society Statement of Operations for the Year Ended December 31,1995

	1995 Total	1994 Total
Program Revenue		
Municipal Grants	**$77,300**	$77,137
Wild Rose Foundation grant		1,304
Fee for service	**209,649**	164,486
Interest income	**29**	87
Employment grant	**5,846**	1,906
Membership fees	**100**	325
Total Program Revenue	**292,924**	245,245
Program Expense		
Advertising	**391**	590
Amortization	**7,408**	4,295
Association dues	**179**	203
Bad debts	**827**	781
Bank charges	**1,332**	877
Containers	**1,332**	877
Employee Benefits (CPP/UI/WCB/group)	**17,387**	13,391
Equipment leasing		329
Equipment purchased	**988**	2,648
Insurance	**795**	763
Meals	**18,673**	20,945
Office	**1,127**	1,227
Professional fees	**2,484**	1,284
Rent	**4,620**	4,620
Seminars, conferences and training	**(128)**	2,798
Supplies	**4,151**	2,637
Travel	**702**	533
Volunteer appreciation	**267**	
Wages and salaries	**242,168**	190,450
	303,371	249,693
Excess (Deficiency) of Program Revenue Over Program Expense	**10,447**	4,448
Fundraising	**10,371**	10,645
Excess (Deficiency) of Revenue Over Expense	**76**	6,197

DEFERRAL METHOD

The deferral method resembles the accrual method of accounting. The revenues are matched with the expenses they relate to. In our example of the three year grant, only one third would be recognized as revenue in each of the three years. The balance would show on the statement of financial position as deferred contributions.

The statement of operations would report the deferred contributions as revenue for that period under the revenue section. If an organization receives a donation or funding for the purchase of a capital asset, the revenue is amortized over the same number of periods as the amortization expense for that asset. That is, the revenue and expense of the asset is being matched.

The statements of the organization may or may not show several columns for the various funds of the organization. The organization's funds would be set up to report the results of various programs or projects as opposed to the restricted fund method where the funds are set up to show the restrictions.

STATEMENT OF REVENUE AND EXPENSES

Questions to ask:

Difference in Revenue

- What is different from last year? Has the revenue decreased or increased significantly?
- Was this a planned change?

Difference in Expenditures

- Have the expenses changed significantly? What brought about this change?
- Did the finance committee alert the board to expect these changes?
- If there are any unexpected changes, is there a plan or a policy to plan this in the future?
- Is this an ongoing condition?

Results

- Have the results been what the board planned to achieve? How has this been assessed? Is there a plan to link results to expenditures in the future?

Bottom Line

- If using the restricted fund method, are the surpluses a result of multi-year funding being recognized in the current year?
- Are there any deferred contributions that have been included in current year operations?
- Is there a surplus or a deficit?

- What is the policy regarding the use of any surplus? Do the funders have a policy regarding use of surplus funds?
- If there is a deficit, what plans are there to cover this budget shortfall?
- Is there an accumulated deficit from previous years? What are the plans to manage the deficit?

STATEMENT OF FINANCIAL POSITION

The statement of financial position has traditionally been called the balance sheet. The statement of financial position is a snapshot of the organization at a particular point in time.

This statement presents the basic accounting equation:

Assets = Liabilities + Equity

Assets are what the organization owns or what is owed to them. They are a result of past transactions or events and therefore represent the collective history of the organization from its start up to the date of the report.

Liabilities are what is owed to someone else by the organization. This may include cash that is owed or services that are still owed because they have been prepaid before the end of the year.

The deferred contributions that were discussed earlier would be shown on the statement of financial position under the liabilities section as the organization still owes service for the contribution that was made. Deferred contributions are not the same as unearned revenue. The unearned revenue would relate to fees that have been paid in advance for a particular service such as membership fees and for example, prepaid fees for a fund raising event.

Equity in a not-for-profit organization is known as net assets or fund balances depending on whether the organization is reporting using fund accounting or not. Equity is what is left over of the assets once all the liabilities have been paid.

The equity section is broken down to clearly show the restrictions on the equity. This breakdown can be as follows:

Investment in Capital Assets

This is the net capital assets (original cost minus accumulated amortization) minus any debt on the assets such as a mortgage. If the deferral method of reporting contributions is being used, it would also be minus any deferred contributions related to the capital assets. This is the amount of equity the organization has in the capital assets.

Restricted Net Asset (Fund Balances)

This is equity that has been restricted either externally by a funder or internally by the board. It may be broken down further into endowment funds, externally restricted (from an outside funder) and internally restricted (restricted by the board) funds. The third type of equity is unrestricted net assets (fund balances). These are the accumulation of the surpluses and deficits in the operating funds of the organization.

FIGURE 11
Statement of Financial Position Helping Hand Society Statement of Operations for the Year Ended December 31,1995

	1995	1994
Assets		
Current Assets		
Cash in accounts – general	$ —	$9,520
– restricted	13,244	8,375
Total cash in accounts	$13,244	$17,895
Accounts receivable	28,756	9,111
	$42,000	$27,006
Capital Assets		
Furniture & Office Equipment	$5,352	$5,352
Computer	10,648	10,648
	16,000	16,000
Accumulated Amortization	(11,703)	(4,295)
	4,297	11,705
	$46,297	$38,711
Liabilities		
Current Liabilities		
Cheques issued in excess of deposits and not released	$4,017	$ —
Accounts Payable	5,359	1,714
Total Current Liabilities	$9,376	$1,714
Net Assets		
Investment in Capital Assets	4,297	11,705
Restricted Net Assets	13,244	8,375
Unrestricted Net Assets	19,380	16,917
Total Net Assets	**$36,921**	$36,997

Approved by the Board

Director Director

A BASIC ACCOUNTING RULE

In order to make sense of a Balance Sheet it is important to understand the basic rule of accounting :

Assets = Liabilities + Equity

A balance sheet is made up of these three parts:

1. **Assets** are what the organization owns or what is owed to them.
2. **Liabilities** are debts the organization has not paid.
3. **Equity** in a not-for-profit organization is made up of what is left of the money after the liabilities are subtracted from the assets, plus the reserves if there are any.

BALANCE SHEET

Questions to ask:

- Are the investments and cash handled so that the best rate of interest is being earned?
- Has the board set any directions as to the use of the unrestricted funds?
- What plans are there to increase cash available for operations?
- How will payables be paid when cash is in a deficit position?
- What are the restrictions on the restricted funds?
- Is there insurance to cover replacement of any vehicles, buildings or goods which the organization owns?
- Is there an investment policy that defines the type of investments that are acceptable?
- Is there a record of all capital assets with dates of purchase, supplier, serial number and cost?

STATEMENT OF CHANGES IN CASH FLOW

The statement of Changes in Cash Flow is a record of all the funds coming into the organization and all of the funds flowing out of the organization during a certain period.

This is a way to record revenue that does not go on the Income Statement. These funds might be a bank loan, money raised for a capital campaign, or an endowment. As well, there may be payments that have been made that are expenses. Examples of these include loan payment, purchase of a building or an investment in bonds. The statement of cash flows shows a more complete picture of cash flows in an organization than the statement of operation. If all cash flows relate to operations, that is, they all flow through the statement of operations, a statement of cash flows is not prepared as it does not provide any further information to the statement user.

The statement of cash flows can be prepared in two ways. Figure 12 shows the indirect method which shows the additions to cash by using the excess of revenues over expenditures and adding or subtracting changes in cash use throughout the period.

Figure 13 shows the direct method that shows where the cash came from and how it was used. This method is a lot easier to understand by most not-for-profit organizations and is now the most recommended method in generally accepted accounting principles.

FIGURE 12
Statement of Changes in Cash Position
Helping Hand Society Statement of Operations
for the Year Ended December 31,1995

	1995	1994
Cash Provided by (Used In)		
Operating Activities		
Excess of revenue over expense	**$ 76**	$ 6,197
Non-cash items – amortization	**7,408**	4,295
Changes in non-cash working capital components:		
Accounts receivable	**(19,645)**	4,079
Accounts payable	**3,645**	(6,194)
Unexpended grants	**—**	(1,648)
Net Cash Increase (Decrease)		
During the Year	**(8,668)**	6,805
Cash Position, Begininning of Year	**$17,895**	$11,090
Cash Position, End of Year	**$9,227**	$17,895
Cash Position Defined:		
Cash in accounts – general	**$ —**	9,520
– restricted	**$9,520**	8,375
Cheques issued in excess of deposits and not released	**(4,017)**	
	$9,227	$17,895

FIGURE 13
Statement of Cash Flows – Direct method
For the Year Ended December 31,1995

Cash Flows from (service delivery, etc.)

- Cash received for operating purposes
- Cash received from general donations
- Cash received from seminars
- Cash received from foundations
- Interest income received for operating purposes
- Cash paid for salaries and benefits
- Cash paid for materials and services
- Mortgage interest paid

Net Cash generated through operating activities

Cash flows from financing and investing activities

- Mortgage financing
- Contributions of cash for endowments
- Contributions for equipment and furnishings
- Purchase of capital assets
- Mortgage principle repayments

Net cash used in financing and investing activities
Net increase (decrease) in cash and term deposits
Cash and term deposits, beginning of year
Cash and term deposits, end of year

STATEMENT OF CHANGES IN FINANCIAL POSITION

Questions to ask:

- What is the impact of the changes in cash flow?
- Were these changes planned or are they a surprise?
- Are all of the funds earning the best return on the investment possible?
- Is there a plan or policy in place to ensure these funds are invested so that they are working toward the organization's long term objectives?
- Is there enough cash being generated through operations to sustain the organization?
- Is all cash appropriately restricted?

STATEMENT OF CHANGES IN NET ASSETS/FUND BALANCES

This statement shows the changes in the individual equity balances for the year. If the organization is not reporting on a fund basis, this is a separate statement. If they are reporting on a fund basis, it can be combined with the statement of operations to show the changes in fund balances.

CHAPTER

5 Other Matters

This chapter will discuss several aspects of financial management which do not necessarily fall within the topics of budgeting and accounting. Specifically, four areas have been identified:

- when to computerize,
- payroll deductions for Employment Insurance, Canada Pension Plan, Workers' Compensation, and the remittance for Good and Services Tax (GST),
- money management, and
- fund development.

WHEN TO COMPUTERIZE

Once the organization reaches the stage where a significant volume of transactions are being regularly processed, then it is beneficial to examine the costs/benefits of computerizing the accounting and budget reporting information systems. Before a purchase of software is made, several factors should be considered, including:

- Is the software compatible with the organization's auditors or financial advisors? Does it need to be?
- What training is required to operate the software? Are any of the staff already trained?
- What are the software packages in common use for which upgrades, manuals and other materials are available?
- What hardware is required, including printers?

Before the organization purchases a software package, discuss the requirements with the auditor and determine the need for compatibility. If the organization does not have an auditor ask an accountant for direction in the selection of an appropriate package and advice on the implementation of the program.

Software is relatively inexpensive. However, the training of a staff member can be time consuming and costly. Assess the skills of the staff and/or board members who will most likely operate the software. Keep in mind the organization's size and avoid purchasing accounting software that has more capacity than the organization would ever need. If one or more of them is familiar with an existing and commonly-used package then consider it as the preferred choice. You may want to obtain guidance in this area from an accountant.

PAYROLL DEDUCTIONS AND GST REMITTANCE

Each employee of the organization will pay Employment Insurance (EI), contribute to the Canada Pension Plan (CPP), pay Income Taxes. As the employer, the organization is responsible for sending these deductions from payroll to Canada Revenue Agency (CRA) or the appropriate entity (e.g. WCB). For all of these deductions from payroll, information bulletins are available form Canada Revenue Agency (CRA). These information bulletins are detailed in terms of how to calculate amounts to be remitted. For specific bulletins such as 'The Employers' Guide to Payroll Deductions – Basic Information', or 'Payroll Deduction Tables for CPP, EI and Income Tax', or the 'Income Tax Guide for the Non-Profit Organization', the organization is encouraged to contact the Canada Revenue Agency (CRA) tax services office or your accountant for assistance.

With respect to the GST, Canada Revenue Agency (CRA) produces information bulletins for charities and other-not-for profit organizations. These are available on their website at www.rc.gc.ca as well as all District Taxation Offices. The GST rules for the not-for-profit sector changed considerably in 1996. There are different rules for charities than for other not-for-profits. Charities have been provided with a simplified method of reporting when they collect GST on any goods and services.

The guides produced by Canada Revenue Agency (CRA) explain when and how you need to register, the basis for exemptions, claiming rebates and other valuable information.

CHARITABLE DONATIONS

All registered charities are required to file a T3010 which is referred to as the Registered Charity Information and Public Information Return.

The Income Tax Act requires every registered charity to file one completed copy of Form T3010:

- within six months after the end of the charity's fiscal period (taxation year), and
- without notice or demand.

The return must include all:

- relevant confidential schedules, and
- financial statements for the corresponding period.

If your charity is carrying on one or more related businesses, you should submit separate financial statements for each related business.

Information bulletins on this filing are available from Canada Revenue Agency (CRA). Failure to file an annual return can result in revocation of the charity's registration and loss of the charitable number.

WORKERS' COMPENSATION BOARD

Depending upon the nature of activities undertaken by your organization, insurance premiums may be payable to the Workers' Compensation Board (WCB). Just because the organization is a society, it is not necessarily exempt. Exemptions are granted after an assessment has been conducted by the WCB of the specific circumstances within which the organization operates.

Even if your organization is granted an exemption, the organization may choose to make voluntary payments so that insurance is established. The organization contacts the WCB to determine the requirement for insurance. The payments are totally an employer expense and depending upon the category the organization falls within, payments need to be made annually or quarterly.

For detailed information about your situation and the WCB implications, contact the WCB office. There are offices in Calgary, Edmonton, Grande Prairie, Lethbridge and Red Deer.

MONEY MANAGEMENT

Not infrequently the organization may have surplus funds either set aside as a reserve or designated for a particular purpose such as a specific capital project. If this is the case, then attention needs to be directed to ensure the money is wisely invested with the best rate of return. There are several options that can earn a return on the invested funds. Some of these are a bank savings account, a term certificate, stocks and bonds, and mutual funds.

Interest rates fluctuate, so groups with surplus funds should ask a bank manager, a stockbroker or an investment management firm about options available to maximize the return on their money.

To assist not-for-profit organizations several communities across Alberta have established community foundations such as the Calgary Foundation, the Edmonton Community Foundation, the Drayton Valley Community Foundation and the Lethbridge Foundation. There are similar foundations in Medicine Hat, Red Deer, Mayerthorpe and Camrose. Some of these foundations may be willing to manage the organization's surplus funds. These foundations will normally charge a management fee but they generally earn higher returns than Guaranteed Investment Certificates and other bank savings account arrangements. An interested organization can contact one of these organizations. The organization can then:

- determine the availability of the service
- its suitability for the circumstances of the organization
- the returns that have been earned
- the inherent risks
- the fees the organization would becharged for the service

An organization also needs to clarify what kind of service is being requested. Does the organization want its money administered by the community foundation or are they setting up an endowment?

FUND DEVELOPMENT

Fund development is a major activity for many not-for-profit boards. There are many resources available on the subject. As the organization begins to consider the implications of fund development, some basic questions need to be asked:

- What is the experience of other boards with the particular anticipated event?
- How many sales of (tickets) are required to break even?
- Can the organization protect itself against unsuccessful fund development activities?
- What will be lost if you do not achieve goals?
- Should the organization engage in fund development to support its operating budget?
- When should the organization utilize the services of a professional fund developer? What are the costs? What are the implications?
- Does fund development affect other sources of funding?
- What reporting is required by Canada Revenue Agency (CRA)?
- Does the organization have a policy against engaging in any fund development activities?
- How does the organization handle bequests?

In developing the budgets and monitoring the revenues and expenditures all of the matters discussed in this chapter may surface. The purpose in raising each one is to alert the organization's financial manager(s) to the potential need to address the issue and some of the factors to consider in so doing.

Whether the challenge is surplus funds (money management) or a deficiency of funds (fund development) the financially responsible organization must identify alternative strategies for dealing with the problem. Persistent attention to the position of the organization's financial resources should help to ensure that the important programs goals and objectives continue to be achieved.

Computerizations, payroll deductions, money management and fund development are important issues for not-for-profit organizations. This chapter has outlined various aspects of each topic and identified strategies groups could choose to adopt in dealing with problems that arise.

The "bottom line" with these topics as well as the others covered in this workbook is – paying close attention to the position of an organization's financial resources will help a board achieve the organization's goals and objectives.

APPENDICES

GLOSSARY

accounts payable – amounts owed by an organization, e.g. unpaid bills for purchases, monthly obligations, loan repayments.

amortization – a) allocation of cost over the useful life of the asset in a rational and systematic manner. b) allocation of revenue (deferred contributions) over a number of periods to match expenses related to the revenue.

assets – what the organization owns or is owed to them as a result of past transactions or events.

audit – independent verification of economic events.

balance sheet – an accounting statement of an organization's financial condition as of a certain date, generally at the end of its fiscal quarter or year.

budget – a financial report containing estimates of income and expenses.

capital reserve – monies set aside for capital purposes.

cash flow – the flow of monies into (receipts) and out of (disbursements) the organization.

contingency planning – allowing for financial flexibility in preparing a budget in order to meet unanticipated events.

cost – the amount paid or charged for something.

deficit – a deficiency in amount – an excess of expenditures over revenue.

disbursement – payment

expenditure – actual expenses incurred at the end of a reporting period or a fiscal year.

expense – a cost, e.g. stationery and supplies, printing and duplicating, postage and telephone.

fiduciary – fiduciary responsibilities relates to holding a position of trust that requires a board member to act honestly, in good faith, and in the best interests of the organization.

fiscal year – any twelve month period the organization has designated as their business "year".

fund – a sum of money or resources intended for a special purpose.

governance – to control and direct the making and administration of policy.

insurance – coverage by contract whereby one party agrees to indemnify or guarantee another against loss by a specified contingent event or peril.

internal control – all measures taken to safeguard assets, check the accuracy and reliability of accounting data, promote operating efficiency, and ensure compliance with the organization's policies and legislation.

investment – using money to provide income or profit.

invoice – bill for goods or services received or provided.

journal – a record of transactions, can be manual or computerized.

not-for-profit – an organization whose main objective is to provide service to the community, not to generate a profit.

APPENDIX I
A Financial Management Checklist

How does your organization rate in financial management? Use this quick checklist to find out.

1. Has the board adopted a written policy stating the responsibilities and authorities it has delegated to the executive director?

   ☐ yes
   ☐ no

2. Does the board periodically review the activity of the executive director to ensure he or she has not exceeded the scope of his or her authority?

   ☐ yes
   ☐ no

3. Does the board review the financial statements of the agency on a regular basis?

   ☐ yes
   ☐ no

4. Have you recently read and understood your organization's constitution and by-laws?

   ☐ yes
   ☐ no

5. Are there members of staff who would benefit from an upgrading course in financial management?

   ☐ yes
   ☐ no

6. Is your organization required to file annual reports to Canada Revenue Agency (CRA) (to maintain your tax exempt status) or with any other government agency? If so, are they filed on a timely basis?

   ☐ yes
   ☐ no

7. Has the board of directors furnished all agency banks with resolutions authorizing bank accounts and designated cheque signers?

   ☐ yes
   ☐ no

8. Does the board determine that agency activities remain consistent with those indicated in its operating budget?

   ☐ yes
   ☐ no

9. Is your current budget consistent with your organization's goals and plans?

   ☐ yes
   ☐ no

10. Do you review on a monthly or quarterly basis, actual income and expenditure compared with your current budget?

    ☐ yes
    ☐ no

11. Does the board of directors approve the operating and the capital expenditures budget of the agency?

    ☐ yes
    ☐ no

12. Must the board give its approval before the budgets can be exceeded?

    ☐ yes
    ☐ no

13. Does your organization prepare a cash flow budget to predict cash flow problems? do you know how "deficit" periods are dealt with?

    ☐ yes
    ☐ no

14. Have your organization's books been set up by a competent bookkeeper or accountant?

    ☐ yes
    ☐ no

15. Is your organization eligible for "registered charity" status under the Income Tax Act? If so, has a "tax number" been applied for and received?

    ☐ yes
    ☐ no

16. Are funds donated for special purposes kept separate from general funds?

- [ ] yes
- [ ] no

17. Has the agency received a letter from Canada Revenue Agency (CRA) granting tax exempt status?

- [ ] yes
- [ ] no

18. Does your organization use numbered cheques with its name and address printed on each cheque? Do you know who has custody and control of unused cheques?

- [ ] yes
- [ ] no

19. Are all disbursements, except those from petty cash, made by pre-numbered cheques?

- [ ] yes
- [ ] no

20. Are voided cheques preserved and filed after appropriate mutilation?

- [ ] yes
- [ ] no

21. Are dual signatures required on cheques over a stated amount? (If so, state amount $ __________)

- [ ] yes
- [ ] no

22. Has the board of directors authorized the amount of the petty cash fund and adopted a policy as to the nature of the expenditures which should be paid from this fund?

- [ ] yes
- [ ] no

23. Is adequate supporting documentation required for all petty cash disbursements?

- [ ] yes
- [ ] no

24. Is access to petty cash limited to one person?

- [ ] yes
- [ ] no

25. If the board of directors has established a dollar limit on petty cash disbursements, is such a limit being observed?

- [ ] yes
- [ ] no

26. Do you get proper financial statements frequently enough to present an accurate picture of the financial health of your organization?

- [ ] yes
- [ ] no

27. Is your organization regularly audited?

- [ ] yes
- [ ] no

Adapted from Financial Management for Community Groups, with thanks to Volunteer Vancouver, 1984.

APPENDIX 2
Financial Policy Checklist

The following list details where an organization may need to review or update their policy. Whether the organization is a Policy Governing Board with senior staff or an Administrative Governing Board without senior staff will direct the level and detail of policy needed.

Budget Responsibilities – this policy sets out the responsibilities of the board, the Treasurer and the senior staff with respect to budget preparation, approval and monitoring.

Budget Monitoring – this policy establishes the frequency, format and content of monitoring reports. Also it indicates the board's directions with respect to the approval of major purchases, the lease of premises, the hiring of new staff and other key items.

Cash Management – this policy places requirements on senior staff to maintain minimum cash balances and to report regularly on the cash position of the organization.

Banking – the board stipulates the individuals or positions in the organization that are authorized to make transactions (eg. the signing of cheques) on its behalf and the procedures for authorizing transactions (eg. two signatures on the cheque).

Accounting – this policy addresses a number of elements such as the requirement for regular reconciliations of the bank accounts and the expected procedures to be followed. It may also stipulate how incoming funds are to be handled, how the records are to be kept in order to ensure they are accurate and current, how the payroll is to be administered so that employees are paid in accordance with applicable codes, how purchase orders are to be used, how the petty cash is to be disbursed and numerous other items.

Finance Committee – the responsibilities of the Finance Committee are to review the receipts and the disbursements and the related reports that should be established as a policy of the board. This Committee should also check to ensure payroll remittances and other deductions have been made in accordance with the appropriate regulations.

Money Management – the board defines its requirements for ensuring surplus funds are invested and earning interest or a return. Of equal importance, the policy should also address the borrowing of funds so that the board is able to authorize the borrowing of money.

Fund Development – in this area the board defines the general purposes for fund development, the important elements to consider in formulating a plan and other elements to consider (such as reporting to Canada Revenue Agency (CRA)).

APPENDIX 3
Operational Policy Statement for a Policy Governing Board (Senior Staff)

The **intent statement** answers the questions:

- Why does this policy exist?
- What is the reason for this policy?
- What is the policy supposed to accomplish?
- What are the desired outcomes from this policy that guide the board, committees, and staff?

The intent statement explains:

- The philosophical basis of the policy. What is believed and valued?
- The desired outcome of the policy.
- What is required of the board and the staff?

The intent statement provides the context for evaluating a policy's effectiveness and appropriateness. Without an intent statement, regulations and procedures have no foundation, and are easily questioned. They also become quickly outdated or invalid.

Example Intent Statement for a Policy Governing Board

Policy Type: Operational

Policy Title: Budget

To make sure that the Blue River Recreation Association continues to exist and stays financially sound, the executive director shall develop the budget, based on the mission, the board's priorities, and the organization's long-term plan. Budgets will not place the organization in financial jeopardy, and will show acceptable levels of foresight.

A **regulation statement** answers the question:

- What restrictions or limitations will focus implementation of the intent statement?

A regulation statement directs action. Each intent statement may have a number of regulation statements. Regulations provide direction for the procedures.

Example Regulation Statements for a Budget Policy

1. Budgets will provide:
    - Enough detail to give accurate projections of revenues and expenses.
    - Separation of capital and operational items.
    - Appropriate detail for the annual fiscal audit.
    - Disclosure of planning assumptions.
2. Annual budgets will not plan to expend more funds than are conservatively projected to be received.
3. Budgets must be based on board-stated priorities (framework policies) and on a long-term administrative plan.
4. Budgets must be submitted for approval two months before the fiscal year end.

A **procedure statement** answers the question:

- Who does what, how, and in what sequence?

Procedure statements set out methods and actions, resulting in the board's desired outcome, as expressed in the intent statement and regulations. Procedures are expressed as mandatory (shall) or discretionary (may).

In the budget example, the board gives the intent and regulations to the executive director. She or her designate develops procedures to make sure that the budget is developed, using the board's intent and regulation statements for direction. The board does not need to approve the procedures.

In an administrative governing board, either the board itself, or a committee, develops the procedures. The procedures would specify the how-to's of the budget development process, including who (either a committee or a position) is responsible for each step in the process. In most cases, the board approves the total policy.

APPENDIX 4
Operational Policy for an Administrative Governing Board, Including Regulations and Procedures (No Senior Staff)

Example Contract Policy for an Administrative Governing Board

Policy Type: Operational – Finance

Policy: Contracting

Intent: Contracts are a necessary part of doing business for the Birch Hill Food Bank. To maintain the confidence of the public and the membership, all contracts will be awarded in an atmosphere of openness, competitive opportunity, and equal access to information. No contracts will be entered into that place the Food Bank in financial jeopardy.

Regulations:

1 The Birch Hill Food Bank enters into contracts only with registered companies or societies, registered partnerships and individuals.

2 Contracts must be consistent with the mission of the organization, and within the approved budget.

3 All contracts over $1000.00 require a minimum of four quotes. The lowest quote will not necessarily be taken; however, reasons for accepting a higher quote must be documented and kept on file.

4. Any board member bidding on a contract must withdraw from both discussion and voting on the contract.

5. The Finance Committee reviews all contracts for content and format.

6. The Executive Committee must give final approval for all contracts. The board must approve out-of-the-ordinary contracts (those exceeding $2000.00 or those not budgeted for) before signing.

7. The Board Chairperson, the Treasurer, and the Contractor sign all contracts.

8. The Executive Committee must approve all changes to contracts, including completion dates. All work stops until changes are approved.

Procedures:

1. For purchases under $1500.00, the initiating board committee prepares a draft contract and submits it to the Finance Committee for review. The Finance Committee reviews contracts to make sure that:

1.1 Standard contract formats are used.

1.2 Budgeted monies are available as outlined in the contract.

1.3 Optional clauses are correctly outlined.

2. The Finance Committee communicates, in writing, any changes to the contract to the initiating committee. If acceptable, the Chair of the Finance Committee initials the contract and forwarded to the Executive Committee for final approval and signing. The Executive Committee forwards out-of-the-ordinary contracts to the board for approval.

3. The Finance Committee makes any changes and resubmits the contract to the Executive Committee for final approval.

4. The Board Chair, the Treasurer, and the Contractor sign and date four copies of each contract.

   The Finance Committee distributes copies of each contract as follows:

4.1 Contractor

4.2 Organization's files

4.3 Finance Committee

4.4 Chair of the originating committee

5. The chairperson of the committee originating a contract monitors delivery of the service. They review all invoices to make sure that billings are consistent with contract specifications and services received. The chairperson signs invoices as proof of receipt of services, and forwards them to the Treasurer for payment. The initiating board committee prepares reports for the Executive Committee and/or Board as directed.
6. The initiating board committee submits any changes to contracts to the Executive Committee for approval.

Approved: ______________________

Reviewed: ______________________

APPENDIX 5
What might the Board Treasurer do?

Some boards combine Secretary and Treasurer roles into one position.

- Serves on the Executive Committee.
- Gives regular reports to the board on the financial state of the organization.
- Keeps financial reports on file.
- Chairs the Finance Committee.
- Orients the new Treasurer.
- Acts as signing officer, with another officer or Executive Director for cheques and other documents.

Add any other duties in the space below.

Depending on your board type and structure, the Treasurer also performs these duties:

Policy Governing

- Has an executive director or a paid business manager to manage day-to-day finances, then the Board Treasurer has a responsibility to oversee the financial functioning of the organization and provide reports for the board. The Board Treasurer may oversee an independent audit from an outside accounting firm.
- Makes sure that all employee deductions are remitted.
- Keeps accurate accounts of board receipts and disbursements for Board-related expenditures.
- Speaks for the budget in partnership with the executive director and Finance Committee.
- Makes sure all necessary financial reports are filed.

Note: In policy governing boards, the duties of the Treasurer do not interfere with the executive director's financial accountability to the board.

Administrative Governing

- Administrative governing boards have no executive director or senior staff person. The Board Treasurer deals with the day-to-day financial affairs. This person may be assisted by a paid clerical staff person. The Board Treasurer is responsible for the accounting of the funds of the organization its budget and expenditures.
- Keeps full and accurate accounts of all organizational receipts and disbursements.
- Receives and banks all monies due to the organization.
- Disburses all monies as directed by the board.
- Prepares and monitors overall budget with Finance Committee. Prepares program budgets with Program Chairperson.
- Submits Employment Insurance Commission (EI) and Canada Pension Plan (CPP) payments to Canada Revenue Agency (CRA) for all paid staff. This person may also do other payroll functions.
- Files necessary financial reports, tax reports and audits.

APPENDIX 6
Reporting Requirements for Not-For-Profit Organizations

Statutes	When to File	Where to File	What Forms to File
Income Tax Act: Charities (Federal)	Annually, within 6 months of fiscal year end	Charities Division Canada Revenue Agency (CRA) Ottawa ON K1A 0L5	One copy of Return of Information (Form T3010), all required schedules and one copy of financial statements
Income Tax Act: Not-for-Profits Other than Charities	Annually, within 6 months of fiscal year end	Canada Revenue Agency (CRA) Taxation Data Centre Winnipeg MN R3C 3M3	T2 or T2 Short Income Tax Return
Income Tax Act: Not-for-Profits Other than Charities	Annually, within 6 months of fiscal year end	Employer Services Division Ottawa Tax Centre 875 Heron Road Ottawa ON K1A 1A2	T1044 – Not-for-profit Information Return if criteria are met*
Statistics Act	When requested	Statistics Canada	Surveys, e.g. Research & Development Summary
Excise Act (Federal)	Semi-annually or annually	Winnipeg Tax Centre Box 14002 STN Main Winnipeg MN R3C 3P8	GST Returns or GST Rebates
Income Tax Act (Federal)	Before February 28 each year	Canada Revenue Agency (CRA) Ottawa Taxation Centre Ottawa ON K1A 1A2	T4, T4A Summary

*T1044 Criteria:

1) Received or are entitled to receive greater than $10,000 in dividends, interest, rentals or royalties during fiscal year
2) Have greater than $200,000 in total assets at the end of the immediately preceding fiscal period
3) Have previously filed the T1044 Return

APPENDIX 7
But Am I Liable – Whatever That Is?

by Laird Hunter

If for-profit enterprises have profit centres, not-for-profit endeavours have worry centers. Volunteers in a variety of roles concern themselves about whether they are doing the right thing. With limited exception, the men and women who provide the countless hours necessary to make the voluntary sector work, do so with utmost honesty and competence. But every once in a while something happens. And so, many volunteers pre-occupy themselves worrying about their personal liability as directors. This month's column looks at some of the legal concepts in this important area. In later issues, we will review other aspects of board and members liability. Readers are encouraged to send in suggestions for this and other topics.

Most non-profit organizations are incorporated. This is done for one or more of a variety of reasons: a funder wants it, someone says it is a good idea, registering a charity is easier if the group is already a society, and because, somehow, being incorporated limits liability. While it is true that one of the principal advantages of incorporation is limited liability, directors can still be held personally liable for activities done while acting as a director. So, what does limited liability mean? And how does it relate to the personal liability of directors?

Limited liability can be looked at two ways. You can look at it from the point of view of the organization or from the vantage point of the member. From the perspective of the society, it means that the extent to which the organization can be required to financially compensate for its wrongdoings is limited by its financial resources. In turn, and from the member's viewpoint, this means her responsibility for a claim against the society is limited to the amount of membership dues which are required to be paid. In a non-profit company, the shareholder/member's liability is limited to the value of the shares which the member has agreed to purchase.

An example. A society has no insurance (not a good idea but it makes the example simpler). It has equipment and fundraising supplies worth $3,000.00, if sold. Twenty-five members have paid their annual dues of $10.00 each. This money is in the bank.
Ten members have not paid their dues. The society has no debts except one to a printing company. The printing company has sued the society for failing to pay its bill and has a judgment for $3,500.00. How much can the printing company collect with its judgment? And, from where?

Equipment and Supplies	$3,000.00
Dues in Bank	$ 250.00
Dues to Collect	$ 100.00
Total	**$3,350.00**

This is the total amount available to the society to satisfy its liabilities. Personal liability for the directors or the members does not arise. The directors have not violated any of the several duties the law imposes on them. And the members are limited in their liability to the amount they owe the society.

The duties and liabilities of directors come about by reference to three principal sources:

1. the statute under which the organization which they serve is registered,
2. other federal and provincial statutes, and
3. the common law – the body of rules which the courts have developed.

In subsequent articles, these areas will be elaborated. In the meantime, the following checklist can be used to focus the areas where directors (and members generally) should pay particular attention.

Measures For a Director to Take at Board Meetings With a View to Reducing Personal Liability

Before the Meeting

- Be familiar with and understand the nature and extent of the organization's objects, bylaws and policies.
- Know if the organization is trustee of property and if so the nature of the trust.
- Make sure you receive and read all documents and reports on which voting will be required.

At the Meeting

- Attend the meeting.
- Keep personal notes of your views of the various matters discussed at meetings.
- Insist on written professional opinions from those on whose advice the Board is expected to act
- Insist on the minutes recording any disclosure, dissent or abstention by you or any other member of the Board.
- Vote against any expenditure which in your opinion puts the organization into an insolvent position.
- Avoid a conflict of interest. Disclose any personal interests in contracts with the organization. Don't vote when the contract is considered by the Board. For extra assurance don't participate in the board discussion and leave the room when the vote is taken. Have these steps recorded in the minutes.

After the Meeting

- Carefully review the minutes of the meetings and bring to the attention of the secretary and the other directors at the next meeting any errors or omissions.
- Keep a notebook of all the minutes and the other important documents you receive while you serve on the board.
- Send a letter by registered mail to the mailing address of the organization if the Secretary or Chairperson refuses on notice at the meeting to record your disclosure, dissent, or abstention from voting.
- Keep the society's information confidential, unless the Board or the members in meeting authorize its release.

Other Measures for the Organization to Take With a View to Reducing Liability Both of Organization and Personal Liability of Directors

- As a Board, get written legal opinions on any important or contentious matters.
- Ensure the organization has controls to monitor the writing of cheques and the signing of contracts.
- Maintain a director's manual for new directors which contains all organizational documents and relevant information and establish procedures to see that it is kept up to date.
- Provide for indemnification through bylaws, if allowed, and make sure broad coverage liability insurance is in place where available.
- Monitor the issue of tax receipts. See to it that procedures are put into place so that the value of receipts is not inflated, especially where the receipt is for a gift-in-kind.
- Insist committees both report to the Board and obtain Board approval for their actions.

Following these checklists should lessen the anxiety of board members and reduce the activity in worry centres. Later columns will add more detail to some of these points and provide additional information for volunteers and directors of non-profit organizations on other aspects of their liability.

Laird Hunter is a lawyer with the firm of Worton, Hunter & Callaghan in Edmonton, Alberta. This article has been reprinted with permission from the Legal Resource Centre, Faculty of Extension, University of Alberta.

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1. Society is used as a generic term in this article. There will be differences depending on the registration statute. These differences will be addressed in later articles. Also the emphasis here is on the non-profit in contrast to the charity.
2. This obligation falls to the organizations and directors of registered charities

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