

# Board Development

## Financial Responsibilities of Not-for-Profit Boards

### Roles and Responsibilities

The management of an organization's finances is one of the least understood, yet most important responsibilities of a board member. This responsibility is on two levels—as an individual board member and as a board collectively. The way in which individual board members exercise this responsibility is by voting for financial policies and the budget. All board members must ensure they understand (and agree with) what they are approving.

Collectively, the board carries the fiduciary responsibility (the responsibility for funds entrusted to the board on behalf of the public) for the organization. The entire board is responsible for the financial health of the organization. The budget, the accounting information system and financial policies are the tools the board uses to exercise its fiduciary responsibility.

It is often believed that the financial responsibility of an organization falls to the Treasurer or to paid staff. The reality is that all board members share in this responsibility. Board members, in some cases, can be held individually liable for debts of the organization in the event of non-performance.

The board of directors may choose to delegate authority for some financial management duties. Duties are typically assigned to one of the following:

**Finance Committee:** usually composed of two or more board members who carry out duties assigned in the terms of reference for the committee.

**Treasurer:** duties assigned often include maintaining all bank accounts, supervising all financial transactions, reporting to the Board of Directors and general membership on finance, and preparing required financial documents.

**Senior Staff:** in organizations with paid staff, many of the financial duties are assigned to senior staff.

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### Other Types of Budgets

#### **Flexible budget**

*Some organizations have patterns of revenues and expenses related to volume, e.g. occupancy. In this case, it is helpful to budget in terms of various occupancy forecasts to monitor revenues and expenses for each level of occupancy.*

#### **Capital budget**

*A capital budget can be developed when a major purchase or acquisition is being planned. It shows the costs of the purchase and the source of funding to cover the costs.*

#### **Cash budget**

*This budget shows the cash moving in and out of the organization, usually on a monthly basis. It allows for planning if there are excesses or shortfalls of cash.*

## The Budget

The budget has two functions.

**Planning:** the budget documents, in monetary terms, the goals and objectives of the organization for a specified period of time (usually one year).

**Monitoring:** the budget serves as a guide to track the organization's progress on the achievement of its goals.

Boards can sometimes get “bogged down” in the financial details of the organization. So how do boards stay focused on the “big issues” and not waste valuable time debating the price of pencils? By asking the right questions.

- Does the budget reflect the organization's priorities?
- What are the fundamental assumptions upon which the budget has been based?
- 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?

These types of questions focus discussion on the core issues of the organization. They also place all board members on an equal footing, regardless of their personal financial expertise.

## Preparing the Budget

The board must identify who is responsible for budget preparation. This person (or team of people) should then follow the five steps of effective budget preparation.

1. List the objectives or goals of the organization for the following year.
2. Estimate the cost of each objective or goal.
3. Forecast the expected income of the organization over the time period of the budget - usually one year.
4. Compare the total expected revenue to the expenses for the overall goals.
5. Present the budget to the board for ratification or approval.

Realistic estimates are essential in budget preparation. For example, if the estimated revenue is far in excess of what can realistically be expected, the organization could end up “in the red,” with more expenses than revenue.

## Monitoring the Budget

Once the budget is approved, it must be divided into time-based segments (usually monthly or quarterly). This is to allow ongoing monitoring of revenues, expenses and their variance from budget.

The board must decide on the frequency and the format of the financial reports it will use for monitoring. The reports must show the revenue and expenses for the time period, as well as any variance between them. This alerts the board to potential adjustments to the budget. For example, if revenues from donations are much lower than expected, the board will have to either raise revenue in some way, or lower expenditures to stay on budget. Timely monitoring allows the board to make these adjustments before a crisis is reached.

## Basic Bookkeeping

### Internal Control

Internal control is a system adopted by the organization to prevent fraud and detect errors, and to ensure the timely and accurate reporting of financial information. One of the basic elements of internal control is that no individual should handle all aspects of a financial transaction. This is referred to as segregation of duties; it creates an internal system of checks and balances.

### Opening a Bank Account

The board must make a motion to authorize the opening of a bank account. The board determines who will have signing authority; however, each cheque must be signed by two individuals. This ensures that the expenditure is reviewed by two people who must ensure it is in line with board policy and the budget.

### Reconciling a Chequing Account

Reconciling means checking the bank statement against the chequebook records. Banks occasionally make mistakes on the statement and this review can identify any such mistake.

### Financial Records

Most organizations will need to keep two types of records: the Cash Receipt Journal (a record of all cash receipts organized by date and category) and the Cash Disbursements Journal (a record of all expenditures organized by date and category).

### Petty Cash

Petty cash is an amount of cash kept on hand in an envelope or box so small purchases do not have to be paid for by cheque. All expenditures should be proven by receipts.

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### An Example of Internal Control

*The person who approves a bill to be paid should not be the same person who signs the cheque to pay for it.*

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### A Word to the Wise

*If you approve the Financial Statements at a board meeting, it means you understand and agree with the information presented. Take the time you need to understand the statements before you approve them.*

### A Basic Accounting Rule:

*Assets = Liabilities + Equity*

## The Financial Statements

The Financial Statements are made up of three reports: the Revenue and Expenditure Statement, the Balance Sheet, and the Statement of Changes in Financial Position. They provide a clear picture of the organization's overall financial health.

The information that is gathered and monitored over the course of the year is fed into these reports. This is why accurate bookkeeping and internal control are so important. The quality of the Financial Statements depends on the quality of the data collected throughout the year.

### Revenue and Expenditure Statement

Sometimes called the Operating Statement, Revenue and Expense Statement or the Profit and Loss Statement, this report shows the amount of income received over a period of time (usually a year) and the amount that was spent. There will be one of three outcomes: revenues and expenditures will balance (be equal), there will be a surplus (more revenues than expenses) or a deficit (more expenses than revenue).

### The Balance Sheet

This report shows the total assets, liabilities and equity of an organization at a fixed point in time. Assets are what the organization owns or is owed. Liabilities are debts the organization has not paid. Equity is what is left after the liabilities are subtracted from the assets, plus any reserves.

### Statement of Changes in Financial Position

This report shows all the funds flowing into the organization and flowing out of it during a certain period of time. It shows funds other than revenue such as a bank loan or money raised in a fundraising campaign. It also shows payments that are not recorded on the Revenue and Expenditure Statement such as a bank payment or an investment in bonds.

## The Audit

The word "audit" strikes terror into the hearts of many people. For an organization, the audit is another financial tool. An audit is an independent study of the accounting records and systems of an organization to determine if its financial statements are fair and reliable. The auditor gives a professional opinion of the extent to which the organization's financial activities followed "generally accepted accounting principles." The auditor will point out instances where these principles were not adhered to and the board will need to take corrective action.

## “Auditing” continued

A full external audit done by a professional accountant (Chartered Accountant - CA, Certified Management Accountant - CMA, or Certified General Accountant - CGA) can be very expensive. If your organization does not require an external audit, the board may want to consider an informal audit by either the Financial Committee or several Society members who have the appropriate knowledge.

## Financial Management Checklist

The following list can serve as a guide for policy review or updating:

- Has the board adopted a written policy stating the responsibilities and authorities it has delegated?
- Does the board periodically review the activity of the individual(s) who have been assigned financial duties to ensure they have not exceeded the scope of their authority?
- Does the board review the financial statements of the agency on a regular basis?
- Is your organization required to file annual reports to Revenue Canada or with any other government agency? If so, are they filed on a timely basis?
- Has the board of directors given all agency banks resolutions authorizing bank accounts and designated cheque signers?
- Does the board determine that agency activities remain consistent with those indicated in its operating budget?
- Is your current budget consistent with your organization’s goals and plans?
- Do you review on a monthly or quarterly basis actual income and expenditures compared with your current budget?
- Does the board approve the operating budget and the capital expenditures of the agency?
- Must the board give its approval before the budget can be exceeded?

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### Financial Policy Checklist

*Does your organization have policies for the following?*

- *Budget Responsibilities*
- *Budget Monitoring*
- *Cash Management*
- *Banking*
- *Accounting*
- *Finance Committee*
- *Money Management*
- *Fund Development*

## Board Development: Financial Responsibilities of Not-for-Profit Boards

### Charitable Receipts

*If your organization is a registered charity, you must have fully controlled receipts for donations.*



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### “Checklist” continued

- Does your organization prepare a cash flow budget to predict cash flow problems? Do you know how “deficit” periods are dealt with?
  - Have your organization’s books been set up by a competent bookkeeper or accountant?
  - Are funds donated for special purposes kept separate from the general funds?
  - Is your organization eligible for “registered charity” status under the Income Tax Act? If so, has a “tax number” been applied for and received?
  - 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?
  - Are voided cheques preserved and filed after appropriate mutilation?
  - Has the board 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?
  - Is adequate supporting documentation required for all petty cash disbursements?
  - Is access to cash limited to one person?
  - If the board has established a dollar limit on petty cash disbursements, is such a limit being observed?
  - Do you get proper financial statements frequently enough to present an accurate picture of the financial health of the organization?
  - Does your agency require Workers’ Compensation Board (WCB) insurance?
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