



## ACCOUNTING SYSTEM AND DUE ACCOUNTABILITY FOR A NONPROFIT ORGANIZATION

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### **Introduction:**

Non-Profit organizations require proper accounting system even more than business organizations. Because they lack the innate oversight mechanism of businesses, paying customers and owners, non-profit organizations need managerial accounting information to help them plan and evaluate their activities more intensely than business. Many of the non-profit organizations are hardly in a position to press for accountability. All the oversight groups involved with non-profit organizations acutely understand this accountability shortcoming.

### **Characteristics of Nonprofit Organizations:**

Entities engaged in business transactions may be classified as profit making or nonprofit. Profit-making organizations respond to a demand for a product or a service with the expectation of earning net income. The distinguishing characteristics of non-profit organizations are: 1) there is neither a conscious profit motive nor an expectation of earning net income, 2) no part of any excess of revenues over expenditures is distributed to those who contributed support through voluntary donations, and 3) any excess of revenues over expenditure that results from operations in the short run is ordinarily used in later years to serve the purposes of the organization.

Nonprofit organizations provide services that fulfill a social need, often for those who do not have the purchasing power to acquire these services for them. With the increase in the sense of social responsibility in society has come a corresponding increase in the number of nonprofit organizations and in the volume of their activities. The members of such institutions do not gain any monetary reward for their membership in the form of dividends or share of profit. Such institutions provide their members with cultural or sporting benefits and the like, or with services, and the surpluses arising from these are applied to the furtherance of their objectives.

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### **Accounting for Nonprofit Organizations:**

The accounting system for nonprofit organizations must provide financial data to internal management for use in planning and controlling operations and to external users donors government regularatory bodies, loan provider etc. for use in appraising the effectiveness of operations. The basic double- entry system, an effective system of internal control, and the periodic determination of financial position and results of operations are essential for nonprofit organizations. In addition, accounting systems for nonprofit organizations should include mechanisms 1) to ensure that management observes the restrictions imposed upon it by law, bye –laws etc. and 2) to provide for reports to donors that such restrictions have been respected. For these reasons, a nonprofit organization often employs the concept of “Fund Accounting” in conjunction with a budget and appropriation techniques to account for the assets received by the organization and to ensure that expenditures are made only for authorized purposes.

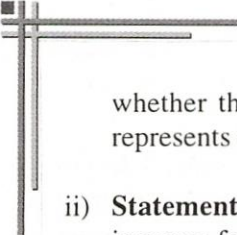
### **Budgeting:**

Budgeting is an integral part of an accounting system for nonprofit organizations. The budget is prepared by management and subsequently reviewed , revised, and approved by the governing body or trustees etc of the organizations. The budget establishes the specific goals for the fiscal period and through appropriations, designates the manner in which the revenues of each fund are to be used to accomplish these goals. The estimated revenues may be viewed as potential assets and the appropriations as potential liabilities. A nonprofit organization should prepare interim statements comparing actual revenues and expenditures with the related budgeted amounts. Variance between the two should be investigated immediately to determine their cause and to consider possible corrective actions.

### **Financial Statements:**

The principal financial statements prepared at the end of each fiscal year are-

- i) **Statement of Receipt & Payments:** Receipts and Payments Account statements are simply a summary of the Cash Book, i.e., of all cash transactions of a particular period, analyzed or classified under suitable headings. It shows on the debit side the opening cash and bank balances at bank and all items of receipts during the period irrespective of whether they are of a capital or revenue nature and whether they relate to the period or not. Likewise it shows on the credit side opening overdraft and all items of payments actually made during the period, irrespective of whether they are of capital or revenue nature and



whether they relate to the period or not. The final balance of the account represents the closing balance of Cash in hand and Bank or overdraft at Bank.

- ii) **Statement of Income & Expenditure:** This statement includes all revenue incomes for the period to which it relates. Similarly it shows all the expenses of revenue nature for the period. In the case of both incomes and expenses, adjustments are to be made if necessary for amounts due and amounts prepaid, so that the exact amounts pertaining to the period is stated in the account. The final balance of the account represents a surplus of income over expenditure or a surplus of expenditure over income for the period. This is added to or deducted from an account called 'Capital Fund' or 'General Fund'.
- iii) **Balance Sheet:** The Balance Sheet depicts the overall status of finances at a fixed point in time. It totals all assets and subtracts all liabilities to compute overall net worth ( or net loss ).

### **What is Accountability?**

It is possible to categorise accounting on a temporal basis:

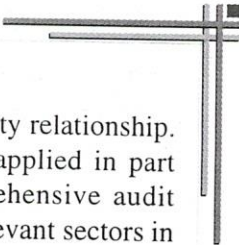
- i) Ex ante accounting – predictive information used for decision-making.
- ii) Ex post accounting- historic accounting information used to establish accountability for actions performed.

Thus accountability may be seen as the process of presenting information so that those in authority may be required to account for their stewardship of assets.

In the words of Robert Tricker – “Accountability involves a requirement to give an account of actions taken. It represents a feedback mechanism by those held responsible for activities. Two parties are involved-the one with the right to demand accountability and the other with the duty to be held accountable.”

Accountability involves more than a reporting of what has been done: it includes a requirement to say why and face the consequences. Accountability implies some degree of participation. Accountability is not discretionary. It involves rights and duties, not interests and opinions. To be able to demand accountability presupposes the potential to exercise power- whether it is based on legitimate authority or on wielding of some sanction.

To render accountability truly effective for a non-profit organization in the present day context of Bangladesh, the following suggestions are offered for early consideration and necessary implementation by the authorities concerned:

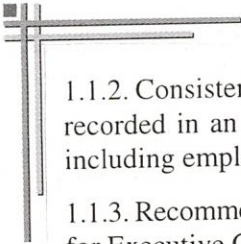
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- a) Audit is a process that is superimposed on an accountability relationship. However, the effectiveness of the audit process when applied in part becomes somewhat restricted in achieving the comprehensive audit objective, which is to examine and comment on all the relevant sectors in the organizational process. Full accountability implies a detailed disclosure of, as well as effective compliance with, the way in which the responsibility has been carried out. Assessing the appropriateness of the arrangements made for appropriate accountability is essentially a matter of determining whether responsibilities and expectations are clearly set out, understood and whether accurate, adequate and timely information is provided on which a valid assessment of performance is made.
  - b) Qualified audit reports should be regarded as unacceptable and remedial action required.
  - c) Accounting standard should be followed in preparing financial statements.
  - d) Authorities should be required for various financial statements periodically prepared by the accounts division along with budget to analyze the variance and the division should be asked to clarify the reasons behind the variance.
  - e) A body representing the authority to run the financial activities of the organization relevantly and appropriately should develop accounting manual or complete financial rules.
  - f) The authority to preserve a good accounting system should implement a complete and effective internal control or internal check system.
  - g) As a protective and constructive arm of management there is no alternative of an effective internal audit.

**Policies for Financial Accountability:**

The Executive Committee should adopt the following Accounting and Control policies and the Treasurer will monitor and evaluate compliance with these policies for the Executive committee-

**1.0. Control Policies:** In order to ensure that the assets of Non-Profit Organization are used in accordance with the legal restrictions and the purposes designated by the Board:

1.1 The Treasurer, directly or through the Finance Committee, shall:



1.1.2. Consistently follow to ensure that financial transactions are consistently recorded in an accurate fashion. These controls also help to minimize risk, including employee theft.

1.1.3. Recommend the Board Designation of any-accumulated operating surplus for Executive Committee approval.

1.1.4. Report to the Executive Committee on the status and disposition of Board Designated and Donor Restricted Net Assets.

1.1.5. Account for Donor Restricted and Board Designated funds separately from General Operation Funds.

1.1.6. Clearly define the restrictions applicable to these funds.

1.1.7. Report the financial results of organization operation on the basis established by the Audit Committee in consultation with the organization's external auditors, including a) GAAP (generally accepted accounting policies) b) IAS (international accounting standard) c) Accrual accounting and d) Fund accounting.

**2.0 Financial Policies:** In order to ensure that the ongoing financial condition of Nonprofit Organization is consistent with the priorities approved by its Board of Trustees, the Accountant shall:

2.1. Report quarterly to the Treasurer on the financial position and financial operation results of the organization's activities.

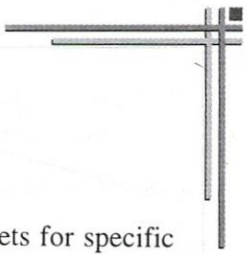
2.2. Pay all debts and file required reports in a timely manner.

2.3. Plan and control organization operations so as to work within approved budget amounts reporting to the Executive Committee any line-item expenses variances in excess of budget and the reason for these variances.

2.4. Require a minimum of five competitive bids before making purchases where appropriate through purchase committee and due section of finance committee. Avoid conflicts of interest in purchases and in all other uses or disposition of assets.

2.5. Make no contractual commitment for bank loans or for real estate lease or purchase without the approval of the Board.

**3.0. Budgeting Policies:** In order to ensure that planned activities minimize the risk of financial jeopardy and are consistent with Board-approved priorities, long range goals, and specific five-year objectives, the accountant of Non Profit Organization, shall:



3.1 Maintain a budget schedule that will include:

3.1.2 Deadlines for submission of five-year budget plans.

3.1.3. Timelines for submission of preliminary and final budgets for specific fiscal years.

3.1.4 Submit operating and capital budgets to the Treasurer.

3.1.5. In time for reasonable approval by the Board of Trustees prior to each fiscal year.

3.1.6. Which limit expenditures in any fiscal year to no more than amounts the Administration has reasonably qualified and reasonably expects to receive during that fiscal year or accumulated in advance.

3.1.7. Supported by sufficient information to provide reasonably qualified projection of revenues and expenditures.

3.1.8. Support organizational capability to achieve the approved goals in future years.

**4.0. Asset Protection Policies :** — In order to ensure that the assets of Non Profit Organization are adequately protected and maintained, the Accountant of Non Profit Organization shall :

4.1. Insure against theft and casualty losses to the Company and against liability losses to board members, staff or the company itself to levels indicated in consultation with suitable professional resources.

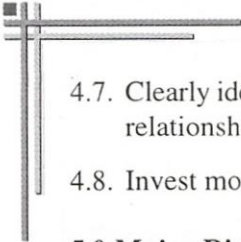
4.2. Enforce industry-standard controls (as confirmed by the Audit Committee in consultation with the Company's external auditors) over access to material amounts of funds.

4.3. Plan and carry out suitable protection and maintenance of property, plant and equipment.

4.4. Avoid actions that would expose the Organization, its Board or its staff to claims of liability.

4.5. Protect intellectual property, information and files from unauthorized access, tampering, loss, or significant damage.

4.6. Receive, process and disburse funds under controls that are sufficient to meet the Board-appointed auditor's standards.

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- 4.7. Clearly identify personnel authorized to establish accounts and contractual relationships with vendors and other outside organizations.
  - 4.8. Invest money in accordance with Board-approved investment policies.

**5.0 Major Risk Policies:** In order to ensure that the Organization is suitably prepared to face the following significant risks –

- 5.1 The Executive Committee shall promptly meet to take appropriate action in the event that the following operational risks emerge:
  - 5.2. Loss of Key personnel, such as General Director, Administrative Director, Director of Education and other department Directors.
  - 5.3. Loss of key performance or administrative facilities.
  - 5.4. Labor disruption.
  - 5.5 The Finance Committee, directly or through its investment sub-committee, shall promptly meet to take appropriate action in that a significant risk in the financial market develops
  - 5.6. The Finance Committee, shall provide in the annual revision of the long range plan for the following strategic risks:
    - 5.7. Succession planning.
    - 5.8. Revenue diversification.
    - 5.9. Reserve suitable to the Organization's goal and plans.

**Conclusion:**

Non-profit leaders and managers have to develop at least basic skills in financial management. They should soon go on to learn how to generate financial statements to control overall organizational activities and to observe the reality. So, an effective accounting system and due accountability is required for a non profit organization to understand whether they have achieved their goals effectively, efficiently in relationship to their resources, whether they have appropriately matched the organization's activities and the resources they use and whether they have diversified sufficiently to sustain their activities and whether they have been fair to different generations and types of people.



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