Fairtrade International Training Manual 3.2

FAIRTRADE PREMIUM COMMITEE FINANCIAL MANAGEMENT

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1. INTRODUCTION

The Fairtrade Standards[1] make the Fairtrade Premium Committee (FPC) accountable for managing the Fairtrade Premium for the benefit of all workers (Standards clause 2.1.1). In particular, this means the FPC is responsible for financial management, and sound, transparent administration of the financial resources.

This manual aims to assist the FPC in this delicate task. Its purpose is two-fold:

(a) Help the FPC (and other committees dealing with finance) to understand the basic principles and procedures of financial management. The FPC should know the basic concepts of book-keeping and be able to read and understand a financial report.
(b) Guide the FPC in financial operations, particularly the treasurer and other committee members directly involved in them. The FPC should establish, know and follow procedures for ensuring transparent and safe financial administration. This includes establishing a simple system of financial records that serves as the basis for the bookkeeping.

The FPC or the treasurer are not expected to become proficient in accounting or to be able to do the bookkeeping themselves. This must be done by a professional accountant. But the accountant only enters data provided by the FPC. To do their job properly, they need full details of all financial transactions from the FPC; hence the importance of accurate record keeping. And it is not the accountant, but the FPC, that is accountable for spending the money. Since there is a fundamental difference between spending one's own private money and administrating money on behalf of an organization, the FPC must follow certain financial administration rules. This is the purpose of the financial procedures.

2. FINANCIAL PLANNING

Planning means making arrangements for the future. Financial planning is making a plan expressed in monetary terms. The main instrument for financial planning is the **budget**, usually for one year: the annual budget. Another useful financial planning tool is the **cash flow plan**, especially useful if you are running several projects at the same time.

(a) Budgeting

Budgeting is the process of drawing up a budget. A budget is the summary of a work plan expressed in monetary terms. The budget is thus an integral component of the Fairtrade Premium Plan that the FPC prepares every year (Standard clause 2.1.15)[2]. The period covered by the budget is normally one year. The budget depicts what you expect to spend (expenses) and earn (income or revenue) over a time period. It is necessary for planning any

[1] Generic Fairtrade Standards for Hired Labour. Citations of the standards in this manual always refer to these standards.
[2] For more details on the workplan see Fairtrade Training Manual *Fairtrade Premium Committee Processes*.

activity that needs to be funded, since it tells you how much money you will need for that activity.

The budget is a powerful management tool. It helps the FPC to implement its strategic decisions. It is perhaps the most efficient way of ensuring cost control and achievement of objectives.

The FPC needs to work with two kinds of budget:

1. Project budgets for each individual project, and
2. The consolidated annual budget of the organization[3] linked to the Fairtrade Premium plan. Consolidated budget means that all activities and operations are included in it.

The Fairtrade Training Manual *Premium Project Management* gives guidance on how to draw up a project budget. Here we will deal with the consolidated annual budget of the organization as a whole.

The objectives of the budget are:

(i) To know how much money you need for the actions you plan and where you get the money from: the projected expenses and income;
(ii) To monitor the financial operations and to know at any time how your financial plan is performing.

According to this double objective, we can distinguish two activities related to budgeting:

aa) Drawing up the budget

You may proceed step by step, as follows:

- Define the **activities**: The budget is based on the workplan, which should describe all projects/activities you plan for the next year. The budget 'translates' the workplan into monetary terms.

- Estimate the **expenses**. Most activities need money. Thus for each activity, you estimate how much it is going to cost (expenses). This should be relatively easy if you have already made the budgets for the individual projects, which are then integrated into the overall budget.

  If you have a business project (commercial or industrial), it should be self-sustaining, i.e. fully cover its running costs and possibly generate a small profit. These types of project must have their own business plan with the corresponding budget. The consolidated budget contains the sum of expenses and income of the project. Expenses refer to (i) the capital investment that is made with premium money to start (or enlarge) the business project and (ii) the running costs. Income refers to the revenue generated by the project.

  Besides projects, the FPC plans other activities, such as training and administration. You have also to make an estimate for the cost of these and put them into the budget. For estimating the training costs, you need to have a training plan with a budget similar to the project budgets.

[3] The term *organization* refers to the legal body entity the workforce has constituted as the owner of the Fairtrade Premium, according to Standards clause 2.1.3. It comprises all employees, not only the FPC members.

For estimating the administrative costs, you must keep in mind all cost factors and add up all items, such as stationary, purchases, depreciation and maintenance of office equipment, travel costs, salaries and personnel services (accounting), communication (phone, email), banking charges, etc. If you hire office space you will also have the costs of rent and public utilities (electricity, water). If this is not your first year of operation, you can base your estimates on the actual costs of the previous year.

- Estimate the **income** or revenue: The first item to consider is the surplus from the previous year. The main source of new income is probably the Fairtrade Premium. Maybe you have other external funding such as a donor or Government contribution to one or several projects. Also some activities/projects might generate income. A business project is expected to generate income that must be included in the consolidated budget. Or a professional training project might charge a small fee from the students. Other incomes are interest on saving accounts and investments.

- Check the **balance**: Income should cover expenditure or allow a surplus.

Table 2.1: Sample budget format

BUDGET 2015 Country: Company: Organization: Period covered by the budget: Currency:			
INCOME			
Balance from 2014	5000		
Expected premium income 2015	20,000		
Income generated by projects: Project 1 (gross income of business project) Project 3 (students' fees for training course)	 3700 300		
Donation (co-financing of project 3 by NGO)	3000		
Other income (interest, etc.)	500		
Total Income			**32,500**
EXPENDITURE			
Project 1 (running costs of business project)		3000	
Project 2 (ongoing social project)		6500	
Project 3 (new: training project)		10,000	
Project 4 (new business project: initial investment cost)		5000	
Training 1		2000	
Administration		2500	
Total Expenditure			**29,000**
BALANCE (surplus)			**3500**

You can present the budget in an Excel spreadsheet. Working with Excel allows copying of the individual budgets for projects and training directly into the consolidated budget. For FPCs with complex operations and with computer experience, it is highly recommended to use a spreadsheet. A sample format can be found in Appendix 1: Appendix 1 N°1 shows the detailed project budgets with monthly expenditure projections consolidated in one table. From this table the totals are inserted into Appendix 1 N°2, which presents the consolidated annual budget of the organization.

ab) Monitoring budget compliance

It is important to know whether the budget is met. Monitoring the budget is the tool that enables controlof budget performance and timely reaction if the budget targets are not met. Monitoring means recording the performance (actual figures on income and expenditure) and comparing it with the budget. If the actual performance is better than the budget, normally you need not worry, except if this is due to a delay in the payment of the Fairtrade Premium Plan. If performance is below expectation, you have to look carefully into the issue. The gap between budget and actual performance may be because either the expenses exceed the budget or the income lags behind. If the gap is considerable, the FPC should analyse the differences and take the necessary measures to balance the budget again. Adapting plan and budget might be necessary.

Budget control is done on two levels: on project level for each individual project and on the level of the general budget for the whole organization. The FPC should fix dates for periodic monitoring of the workplan and budget. Best practice is to make monitoring of the general budget a mandatory item of the regular (monthly) FPC meetings. Appendix 1 N°3 shows a sample form for monitoring the budget of an individual project. The form can be easily adapted for the purpose of monitoring the general budget.

(b) Cash flow planning

The term *cash flow* refers to the amount of cash being received and spent during a defined period of time. The method for calculating the cash flow is subtracting the cash disbursements from the cash receipts.

The cash flow forecast ensures that the funds are available when they are needed. It gives an estimate of the monthly cash requirement and availability. While the budget shows financial projections for the whole year, the cash flow plan breaks the budget down into monthly instalments according to the calendar of activities. The cash flow plan is the twin of the monthly workplan; the respective budget corresponds to each activity. The cash flow plan protects you from the surprise of not having liquid cash at the moment you need to make an important payment. Appendix 1 N°4 shows a sample format for cash flow forecast.

3. ACCOUNTING AND BOOKKEEPING[4]

The purpose of this chapter is not to train the reader in bookkeeping. The intention is considerably more modest. After studying the chapter, you should be able to understand what accounting is and what the basic steps involved in it are. You should also be able to understand how a financial report is constructed, what it should look like and how to read it.

The terms ***accounting*** and ***bookkeeping*** are nearly synonymous and often used alternately. Accounting means the process by which financial information is recorded, classified, summarized, interpreted, and communicated. Bookkeeping is more specific and refers only to the recording of financial transactions. A *transaction* is any exchange of economic value between business partners, such as selling and purchasing, providing services, lending money, etc.

The objectives of accounting are:

- Enabling FPC members and eventually workers to know the amount of Fairtrade Premium earned and how it was spent;
- Enabling the FPC to take financial decisions in full knowledge of the financial situation of the organization;
- Enabling other stakeholders to confirm that the funds are being utilized in accordance with the overall goal of Fairtrade;
- Meeting the legal and professional requirements.

The function of accounting is to process financial information with the purpose of knowing the financial performance of an organization. This can be a business company, a Government department, or a charity organization. Accountability for financial management is not possible without accounting. Accounting allows us to know how much we have earned, how much we have spent, where our revenue came from, how we have spent the money, and whether we did well or badly financially-speaking. In other words: whether we earned or lost money.

The accounting system most commonly used is *double-entry bookkeeping*. It consists of a chart of accounts, each of which reflects a particular aspect of the business. Some of the basic accounts you will use are:

- *Cash* = The liquid funds you have in the safe and in bank accounts
- *Accounts receivable* = The money your business partners/customers owe you for goods and services you provided for them
- *Inventories* = Stocks of products, raw materials, etc. you have in your stores
- *Equipment* = Furniture, office equipment, vehicles, etc.

} These are called *asset accounts*, because they represent economic resources controlled by your organization.

[4] For references and further study see the list of sources at the end of this manual. The procedure and tools explained in this chapter conform to International Accounting Standards.

- *Accounts payable* = The money you owe your business partners/suppliers for goods and services you received from them

This is a *liability account*, because it represents obligations of your organization to your business partners.

- *Capital* = The money owned by the organization

This is the *owner's equity account*. Its worth results from the sum of all assets minus all liabilities.

- *Income* = The money you earn. Premium income will also be recorded in this account.
- *Expenditure* = The money you spend

Normally you have several income and expenditure accounts, according to the nature of your business. You have separate accounts for any category of income and expenditure.

In double-entry accounting every transaction is recorded by entries in two accounts: As a DEBIT in one account and as a CREDIT in the other account. It is not easy to explain when an entry is made as a DEBIT or a CREDIT[5]. For practical purposes, you can follow the rule:

- DEBIT entries = increase in debit accounts or decrease in credit accounts
- CREDIT entries = decrease in debit accounts or increase in credit accounts.

Debit accounts are assets and expenditure;
Credit accounts are liabilities, capital and income.

Table 3.1 summarizes this rule (+ = increase, - = decrease):

Account	***Debit***	***Credit***
Assets	+	-
Liabilities	-	+
Capital	-	+
Income	-	+
Expenditure	+	-

<u>Note that the usage of the terms DEBIT and CREDIT in accounting is not identical to their everyday usage.</u>

The rationale for the double-entry bookkeeping system is that any transaction affects two aspects of a company. This is illustrated by two simple examples:

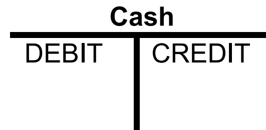
Transaction 1: The company purchases a computer. On one side, its assets increase, and this is shown by the recording in the equipment-account (DEBIT Equipment). On the other side, the computer must be paid for, and this diminishes the company's cash, which is expressed by the recording in the cash-account (CREDIT Cash).

Transaction 2: Now the opposite happens: The company sells a product from the store. On one side, its inventories decrease, which is recorded in the inventory-account (CREDIT Inventory). On the other side, cash increases, which is recorded in the cash-account (DEBIT Cash).

<u>The total of the DEBIT values must always equal the total of the CREDIT values.</u>

[5] Readers interested to understand the DEBIT/CREDIT logic in more depth are referred to Appendix 2.

Historically, DEBIT entries have been recorded on the left hand side and CREDIT values on the right hand side of a ledger account. Ledger accounts are set up as T accounts, so called because they resemble the letter T.



The accounting process is a series of activities that begins with a transaction and ends with the closing of the books. Because this process is repeated each reporting period, it is referred to as the **accounting cycle** and includes the following major steps:

(a) Preparation or collection of the **source documents** of a transaction. In financial management, a document is produced each time a transaction occurs. The records of transactions are referred to as source documents. During audits they are used as evidence that a particular transaction occurred. Examples of source documents are:

- Invoices and receipts for sales and purchases
- Income and expense vouchers (see below)
- Deposit slips for putting money into a bank account
- Cheques for payments out of a bank account
- Purchase orders
- Payment orders

Often a transaction generates more than one source document. Let's take the example of the purchase of computers by the FPC, which is paid for immediately by cheque. This transaction is recorded in several source documents: (i) purchase order, (ii) invoice, (iii) payment order, (iv) cheque, (v) receipt.

Who is **responsible** for **producing, receiving and filing the source documents**? This is clearly the <u>task of the treasurer</u>. They must prepare and/or collect and keep the source documents very carefully and make sure that none are missing. The source documents are indispensable inputs for the following step. We will discuss in more detail in Chapter 5 how source documents should be prepared. Besides the source documents, the treasurer also receives and keeps all other documentation related to the management of the accounts, such as monthly bank statements.

(b) **Entry** of the transaction in the **general journal**. The journal is the entry point of transactions into the accounting system. It is a chronological record of transactions, showing an explanation of each transaction and the accounts affected.

It takes the following form:

Date		DEBIT	CREDIT
DD.MM.YYYY	Name of DEBIT account	Debit amount	
DD.MM.YYYY	Name of CREDIT account		Credit amount
DD.MM.YYYY	Optional: Explanation of transaction		

Before the journal entry is made, the following questions must be answered:
- Which accounts are affected by the transaction?
- Which account must be debited?
- Which account must be credited?

Examples:

Transaction 1: On 3/11/2014 a premium of 1500 was received. The journal entry is:

Date		DEBIT	CREDIT
3/11/2014	Cash	1500	
	Income		1500
	Premium from customer		

Transaction 2: On 9/11/2014 a computer was purchased for 900 and paid immediately. The journal entry is:

9/11/2014	Equipment	900	
	Cash		900
	Purchase of computer		

Transaction 3: On 16/11/2014 travel expenses of 20 were paid. The journal entry is:

16/11/2014	Expenditure	20	
	Cash		20
	Travel expenses first half of November		

After the transactions have been recorded in the journal, the source documents must be kept carefully. It should be possible to check the journal entries with the supporting documents at any time. A simple way is to keep them in a file in chronological order.

Journal entries may be done continually (daily or whenever a transaction occurs). If you have only a small number of transactions, it can be done in a batch at the end of the week or even the month. This depends also on the question of who is doing this job.

Who should be **responsible** for **keeping the journal**? You have to be aware that this step is actually a bookkeeping task – in contrast to the preparation of source documents. But correct journal entries are crucial for the proper handling of the following steps. Therefore, the task of filling in the journal is normally done by the accountant, and not the treasurer. However, this depends on the capacity and willingness of the treasurer. If they have been properly trained and feel capable and comfortable of doing it, they should be encouraged to try. Of course they must be guided and coached by the accountant. Wrong entries in the journal could create confusion and make more work for the accountant than if they do it themselves. even if the accountant keeps the journal, the treasurer is still responsible for preparing the source documents, which are handed over to the accountant.

(c) Posting of journal entries to the **general ledger**. Once entered in the journal, the transactions are posted to the appropriate T accounts in the general ledger. While the journal is organized chronologically, the ledger is organized by accounts. The general ledger is a collection of accounts. The accounts of the ledger take the form of two-column T-accounts, as explained above.

The list of all accounts of the bookkeeping system is referred to as the *chart of accounts*. It must be designed by the accountant. It should not just be a replica of the system of a business company but should consider the specific nature and needs of the organization. Each account in the chart is assigned a unique *account number* or *code.*

A suggestion for an account chart is presented in Appendix 3.

To illustrate posting to the ledger accounts, we use the same examples as above. Four accounts were involved in these two transactions: Cash, equipment, income and expenditure. You post the journal entries for each transaction to the respective account:

Transaction 1: On 3/11/2014 premium of 1500 was received

Cash

Debit	Credit
3/11 1500	

Income

Debit	Credit
	3/11 1500

Transaction 2: On 9/11/2014 a computer was purchased for 900

Equipment

Debit	Credit
9/11 900	

Cash (2)

Debit	Credit
3/11 1500	9/11 900

Transaction 3: On 16/11/2014 travel expenses of 20 were paid

Expenditure

Debit	Credit
16/11 20	

Cash (3)

Debit	Credit
3/11 1500	9/11 900
	16/11 20

Note the direct mapping between the journal entries and the ledger postings. Maybe this posting of transactions that have already been entered in the journal seems redundant. However, the general ledger serves an additional function. It allows you to view the activity and balance of each account at a glance. Look at cash account (3): all three transactions have affected this account (which is not always the case, of course). After the posting the last transaction you can see at once what the cash balance is:
1500 – (900 + 20) = 580. Adding up the accounts is called *balancing*.

Steps a) – c) described above are performed at any time during the accounting period, either when transactions occur or in periodic batches (at the end of the week or month). While step a) must be performed by the treasurer, step b) might be done by the accountant or the treasurer. Step c) and all subsequent steps should be performed by the accountant.

The following steps are performed at the end of the accounting period. The accounting period means the time after which the books are closed and the financial statement is prepared. This should be done at least at the end of the business year; however, it is recommended to do it in shorter intervals, monthly or at least quarterly.

(d) Preparing the **trial balance**. The term trial balance means that it is used to test whether DEBITS equal CREDITS. Trial balance is a list of the balances of all accounts in the ledger. The amounts are copied to a two-column list: the DEBITS (the sum of all debit entries) into the left column and the CREDITS (the sum of all credit entries) into the right column, as shown in the following table:

Table 3.3: Sample trial balance

Account title	Debits	Credits
Cash	1500	920
Equipment	900	
Income		1500
Expenditure	20	
TOTAL	2420	2420

The total of the DEBITS should equal the total of the CREDITS. If this is not the case then an error has occurred that must be corrected. It could have been a maths error (in the addition), a recording error (entry of wrong numbers) or a posting error (entries in the wrong column).

(e) Preparing **adjustments**. Why are adjustments necessary? Transactions are recorded in the journal at the date when they occur. But some transactions are not applicable to the actual period and other transactions applicable to the period have not yet been recorded. There are two major types of adjusting entries:

- *Accruals* are revenues actually earned and expenditure actually incurred, but not recorded in the books. Example: Salaries for the month that will be paid at the beginning of next month.
- *Deferrals* are revenues and expenditure that have been recorded but not earned or incurred in this period. Example: Prepaid insurance premium.

The adjusting entries are posted in the ledger accounts. Then an adjusted trial balance is prepared the same way as explained above.

(f) Preparing the **financial statement**. This is the closing of the cycle. The financial statement consists of two parts: *income statement* and *balance sheet*. They are both derived from the general ledger.

- *Income statement*[6] reports what the organization has earned (income), spent (expenditure) and the resulting net income (called profit for business enterprises or surplus for not-for-profit organizations) during a period, for instance from January 1 to December 31.

Table 3.4: Sample Income Statement from … to…

	Expenditure	Income
Income		
Premium income		25,000
Donation from NGO for project		3000
Income generated by projects		2000
Financial income (interest on savings and investments)		800
Expenditure		
Project 1	4500	
Project 2	2000	
Project 3	11,000	
Training and capacity building	3000	
Administrative costs	1900	
Professional services	500	
Depreciation of equipment	250	

[6] The Income Statement is also referred to as *Income and Expenditure Statement*; for not-for-profit organizations the term *Statement of Operations* is also used.

Financial costs (bank charges)	36	
Total	**23,186**	
Net Surplus	7614	
	30,800	**30,800**

The statement can have different forms (e.g. income and expenditure in the same column) and can give more details (e.g. administrative costs by items). You can also choose to include comparative figures from previous years in an additional column in the statement.

The table shows the principle. Instead of a surplus, a loss may result, which is possible if you had high premium volumes accumulated in previous years that have now been used. The loss then would not be a cause for concern, since the purpose of a not-for-profit organization like yours is not making gains, but to use the money well.

- *Balance sheet* reports the assets, liabilities and capital. The balance sheet is a snapshot of the financial situation of an organization at a specific moment in time.
  Table 3.5: Sample Balance Sheet as at…

	Assets	**Liabilities**
Assets		
Current assets		
Cash and bank	2200	
Accounts receivable	300	
Inventories	450	
Fixed assets		
Office equipment	1350	
Equipment project 1	4700	
Long term investments	8000	
Liabilities		
Current liabilities		
Accounts payable		860
Accrued liabilities (professional services)		300
Long-term liabilities		
Loan payable		1000
Capital		
Accumulated premium funds		7226
Surplus for the year		7614
	17,000	**17,000**

Terminology:

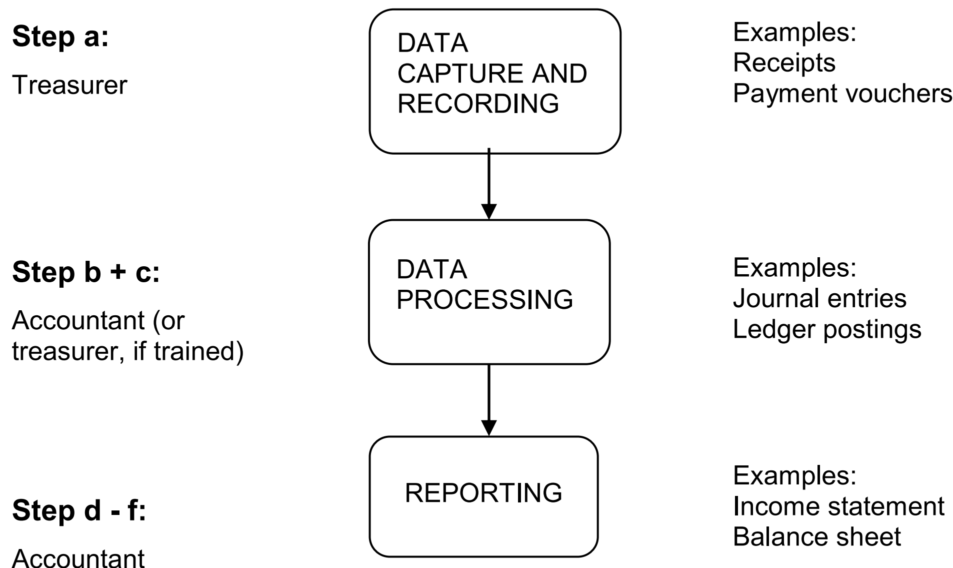
Assets are the economic resources in the control of an organization, the valuables you possess and can work with.

Current assets are assets that are in cash or can be easily converted into cash within one year.
Fixed assets are assets that cannot be easily converted into cash. They include land, buildings, machinery, equipment, vehicles, etc. Also long term investments (over one year) are recorded under this category.
Liabilities are the obligations (debts) owed to third parties (banks, suppliers, etc.).
Current liabilities are debts that must be paid within one year.
Long-term liabilities are debts due more than one year from the current date.
Capital, in business referred to as *ownership equity*, is the owners' interest in all assets after all liabilities are paid. This is the portion of the business that actually belongs to the owner. In the case of not-for-profit organizations like yours, capital refers to the accumulated surpluses (premium funds not spent). The formula says:
Ownership capital = assets – liabilities.

The generally accepted **accounting principles** underlying the financial statements are:

- Completeness
- Clarity or transparency
- Prudence
- Consistency in presentation, disclosure and evaluation
- Prohibition of netting (i.e. expenditure and income are to be presented at gross amounts, it is not allowed to offset a positive value against a negative value)

Flow chart of the accounting cycle:



Computerizing the accounting system saves a great deal of time and effort. It reduces (if not eliminates) mathematical errors and allows for much more timely information than a manual system does. It also saves some of the steps discussed above. Computerized systems usually combine step b) (Journal entry) and step c) (Ledger posting). Also the need to test if DEBITS and CREDITS are equal through the trial balance is usually not required, since most systems calculate this automatically when the data is entered. However, though the computer can handle the mechanics of the system, human judgement is still required to ensure that the data entered into the system is correct.

4. FINANCIAL REPORTING

Regular financial reporting is a central requirement of the Fairtrade standards. Information on the Fairtrade Premium amount (Standards clause 2.1.12), its administration and use must be given to the FPC itself (Standards clause 2.1.12), to the workers and to the certification body (Standards clauses 2.1.12 and 2.1.18).

(a) Information to the Fairtrade Premium Committee

According to Standards clause 2.1.12, all relevant books of the Fairtrade Premium account must be available to all FPC members. Information on premium flow and balance is a mandatory agenda point at FPC meetings. Best practice is monthly reporting. High premium income must be reported immediately, even between meetings.

The responsibility for informing the FPC on the flow and balance of the premium lies with the treasurer. In order to ensure that all receivable premium money has been accounted for, the treasurer should perform the following tasks monthly:

- Ascertain from the company's Fairtrade sales reports (to be provided by management) the amount of premium due (Standards clause 2.1.12);
- Check when the corresponding deposit is made to the premium account and compare the amount credited with the sales reports;
- Check with the bank statement to ensure that the correct exchange rate has been used to convert the amount into local currency;
- Any variances with the sales report or the bank statement must be followed up immediately for rectification. Differences must be explained (for instance, less sales income due to quality claims).
- Prepare the income voucher for the premium amount deposited in the bank account.

In the case of income from investments the treasurer needs to ensure that the interest earned is correct by checking against the rate of interest.

The report on premium income and balance takes the following form:

Table 4.1: Summary Fairtrade Premium (FP) flow report format

MONTH:	CURRENCY
Balance at beginning of the month	
Plus: Income	
Minus: Expenditure	
Balance at end of the month	

This form can be found in Appendix 4 N°1 as an Excel spread sheet. It is sufficient for FPCs with a low turnover and few financial operations.

If the FPC has a higher turnover and more intensive financial activities, another, more sophisticated format is recommended. It is presented in Appendix 5 N°1. This FP flow report form allows a complete record of all transactions in chronological order. It follows the same logic as the simpler form presented in Appendix 4 N°1. But it is structured in a more functional way, since it allows you:

- to check income and expenditure and the resulting balance at any time;

- to check expenditure and income of each individual project and other budget items (such as administrative costs) at any time;
- to produce a cash flow report at desired intervals; monthly, quarterly or whenever you wish.

The assumption is that the organization has one current account and all financial operations are handled through this account. The register is kept in local currency, except premium earnings which are registered in foreign currency and then converted into local currency[7].

It is highly recommended that the FPC uses this form, because, in addition to the above mentioned functions, it has the following advantages:

- It is easy to handle and can be managed by the treasurer after a short period of training (if they are computer-literate). It is less demanding than the journal referred to in 3b above);
- It allows daily entries and shows the daily balance of funds;
- The sums in each column can be easily transferred to a summary report;
- It is useful for FLOCERT because it allows the auditor to check at a glance the basic data on premium earnings and expenses project by project.

(b) Information to the workers

A financial report must be submitted to the workers (General Assembly) at the end of the business year (Standards clause 2.1.18). This report consists of the financial statements discussed above (see 3f):

- Income statement
- Balance sheet

These reports will normally not contain full information on individual projects, because they are summarized statements. The workers are probably interested to know the financial performance of each project. For this purpose a short summary on each project (budget – expenditure – income if applicable) should be presented. The information on project expenses and income can be easily extracted from the cash flow format in Appendix 5 N°1 discussed above.

Together with the Fairtrade Premium Plan for next year, the budget must also be submitted to the GA (2.1.15).

An annual financial report and a budget are the minimum pieces of financial information that the FPC is required to give the workers. However, it is recommended that more financial information is shared with them and done so more frequently than just once a year. For instance, the monthly summary of cash flow report (Table 4.1) may be put on the notice board. Because of the cash flow report format (Appendix 5), workers can be informed more frequently about the financial situation.

(c) Information to the certification body FLOCERT

[7] This form can be expanded, according to need. For instance, if you wish, you can insert additional columns for income in local currency: premium income, income from projects, other income (interest, etc.). The number and nature of expenditure columns depends on your projects and activities.

The financial statements and the budget established at the end of the fiscal year must also be presented to FLOCERT. The financial reports should be accompanied by the report of the external audit[8]. These documents may be handed over to the FLOCERT auditor.

The FLOCERT auditor requires updated information on premium income, premium expenditure per project and premium balance. As suggested above, the best way to have this information ready any time is to record it with the cash flow format of Appendix 5 N°1.

5. FINANCIAL PROCEDURES

This chapter aims at providing the FPC with practical guidance on central issues of daily financial administration. The intention is to make financial management more efficient and safer.

(a) Preparing the source documents on income and expenditure

The importance of written documents on all transactions has already been stressed in Chapter 3a. The FPC and particularly the treasurer must follow very strictly this rule: No financial transaction without a document. In this section we will discuss the main types of documents and the minimum requirements they should comply with. We will also make suggestions for some forms for the FPC to use.

As a minimum, each source document should include:
- The date
- The amount
- A description of the transaction

Where practical, beyond these minimum requirements, source documents should contain the name and address of the other party to the transaction.

When a source document does not exist, e.g. when a cash receipt is not provided by a vendor or misplaced, an internal document should be generated immediately after the transaction (vouchers as described below).

To make sure that any transaction, either income or expenditure, is properly documented, the use of a system of vouchers is recommended. These vouchers, numbered and filed in chronological order, facilitate the job of the accountant. The voucher contains the information necessary for the accountant to know which accounts are affected by the transaction. Two different forms are used[9]:

- An **Income voucher** is generated any time the organization receives a payment: premium transfer, interest payment, income generated by premium projects (sales, provision of services, loan repayments, etc.). The voucher is made independently from the form of payment, whether it is in cash, by cheque or a bank remittance.

  See model Income voucher in Appendix 4 N°2

[8] See below Chapter 6c
[9] If you decide to use these forms, it is useful to have them printed with the letterhead of the organization.

The voucher has two parts: the upper part is for the information on the nature of the transaction:

- Number, date and amount
- Received from: name and address of the payer
- Amount in words
- Description of transaction
- For project: if payment is destined for one or several specific projects, or for administration
- Form of payment: cash, cheque or bank remittance
- If cheque: cheque number and bank
- If amount has been deposited in a bank account: account number and bank

This part of the voucher must be filled in by the treasurer. It should then be revised by a workers' representative on the FPC and by a management advisor

The lower part of the voucher is for the use of the accountant. After registering the transaction in the books, they fill-s in the corresponding boxes in the voucher.

- An **Expense voucher** is generated any time the organization makes a payment by cheque (for cash payments a different voucher referred as petty cash voucher is used; see below 5d).

  See model Expense voucher in Appendix 4 N°3

  The form is very similar to the income voucher. It should be filled in in the same way by the treasurer and revised by a workers' and a management representative. The box 'Supporting document' refers to the invoice and/or receipt provided by the supplier.

These vouchers are not meant to substitute for the supporting documents provided by the business partners, such as invoices, receipts, credit notes from the bank, etc. The original receipts must always be attached to the vouchers.

(b) Payment procedure

The FPC must issue a payment procedure. For any payment to be made, the payment procedure has to be strictly followed. The procedure must regulate:

- What requirements must be fulfilled prior to payment
- Form of payment (e.g. amounts exceeding 20 USD only by cheque)

The purpose of the payment procedure is transparency and security.

The following steps should be followed in the payment procedure:

- All payments must be based on a FPC decision and – if applicable – have followed the regulations on procurement (procurement procedure, see below 5e).
- Except for petty cash expenditure, the treasurer issues a payment order with all the information necessary to check whether payment is based on an FPC decision and the procurement procedure. See payment order form in Appendix 4 N°5.
- The payment order is checked and payment authorized by at least two people: a workers' representative (according to the internal regulations this can be the FPC chairman or another FPC member) and a management advisor. Preferably the authorizing people should not be signatories of the account.

- Amounts exceeding the limit fixed by the FPC must always be paid by cheque or bank remittance. Only small amounts can be paid cash.
- When authorization of the payment order is complete, the treasurer issues the cheque and presents it to the signatories of the account together with the payment order. Signatories must check the payment order (and supporting documents) before signing the cheque.
- Payment is made against receipt.

(c) Bank account management

The organization must open a bank account for receiving and administering the premium. The joint signatories must be at least one workers' representative and one management advisor (Standards clause 2.1.5). The FPC may specify this requirement or make it stricter (for instance, two workers plus one management representative) but not loosen it.

Current account: It is recommended that for the day-to-day operations a current account is used. In a current account usually no interest is earned. But the money is deposited and withdrawn easily at any time. The main advantage of the current account is the cheque book, which is issued to enable the account holder to make payments and withdraw money. Payments made by cheque are safer than cash and can be easily traced. The current account should be the only account used for payments.

The chequebook must be kept by the treasurer in a safe place under lock and key. Cheques should never be signed blank or post-dated. Date, payee and amount should always be filled in before a cheque is signed.

High premium balances, which are not needed for meeting shortterm obligations, should be invested in interest-earning but safe financial instruments. These may be, for instance, savings accounts or fixed deposits[10].

Records: The treasurer should keep an updated record of all transactions (deposits, remittances, payments) on the current account. The information on the bank balance must be readily available at any time. As soon as the transaction is carried out, it should be registered in the corresponding book. According to your recording practice and your accounting system, you have the following possibilities:

- The transaction is recorded in the cash flow report form (Excel spread sheet) suggested in Appendix 5 N°1. This is the most efficient way.
- If your entire accounting system is computerized, the entry can be made directly into the system (you have to know which account is to be debited and which one credited). This is more complicated and requires that the treasurer is familiar with how to use the system.
- If you have neither of these two possibilities, the treasurer should have a separate cash book where the transactions are registered manually or by computer if the treasurer is computer-literate.
  The form of the cash book is very simple, as shown in the following table:

  Table 5.1: Sample form of cash book

[10] A fixed deposit is an account where money is placed for a specific period of time, say one month, three months, six months etc. Funds in such an account cannot be withdrawn before the time period expires or with a penalty such as losing the interest due. Normally a fixed deposit account earns slightly higher interest than a savings account.

CASH BOOK							
Name of organization							
Bank and Current Account N°							
Date	*Cheque N°*	*Voucher N°*	*Payee or payer*	*Description*	*Income*	*Expenditure*	*Balance*

Bank statement: The bank sends a monthly statement to the account holder, which shows the following information:

- Deposits, remittances and interest earned (called credits by the bank = income)
- Payments and bank charges (called debits by the bank = expenditure)
- Balance at the end of the month.

If the statement is not sent, inquire why and ask the bank to send it regularly. It must go to the treasurer, who checks the statement and compares it with their own records.

Bank reconciliation: Comparing the figures from the books (your records of the bank account) against those on the bank statement is called bank reconciliation. <u>This is a very important task to be performed at the end of each month by the treasurer (or the accountant).</u> The balance of the bank account record should reconcile (match) with the balance of the bank statement. If this is not the case, there might be an error from either side, yours or the bank's. But more probably the difference is due to a time lag between banking operations and accounting. Differences may be explained because:

- Cheques drawn and registered in your books as expenditure have not yet been presented to the bank for payment and consequently have not yet been debited from your bank account;
- Cheques deposited at the bank and registered into your books as income have not yet been credited by the bank;
- Bank charges and interest have been entered onto the bank statement but are not yet recorded in the account.

The treasurer should, therefore, prepare at the end of every month a **bank reconciliation statement.** You can establish the statement both ways, either adjusting the balance per bank or per books. The method proposed here is adjustment per books. That means you start from the balance recorded in your books which is equal to the balance in the bank statement. You proceed by the following steps:

1) Compare the balance in your books (bank account record) with the bank statement balance provided by the bank.
2) If there is a difference, search for any item that does not appear in one of both records (your books and the bank statement).
3) Items missing in the bank statement:
    - Add all outstanding cheques (cheques that you have drawn and recorded as payment but that were not cashed by the beneficiary)
    - Deduct all deposits in transit (deposits you made that have not yet been credited by the bank)
4) Items missing in your books
    - Add all credit notes from the bank not registered in your books (e.g. interest)
    - Deduct all debit notes from the bank not registered in your books (e.g. bank charges)
5) The result of these operations should be equal to the balance in the bank statement.
6) In case you have more than one bank account, repeat the steps for all the bank accounts held by the organization in the period under review.

Table 5.2: Illustration of bank reconciliation statement

Balance as per books	**1300**
Add: Outstanding cheques (cheques not cashed)	+ 300
Deduct: Deposits in transit	- 150
Add: Credit notes (interest)	+ 20
Deduct: Debit notes (bank charges)	- 10
Balance as per bank statement	**1460**

You may also use the electronic format in Appendix 4 N°6

(d) Petty cash management

Petty cash is used only for payments of small amounts (e.g. less than 20 USD) where it is not practical to use a cheque. It is preferable that the petty cash is not administered by the treasurer or the chairperson. The FPC should appoint another FPC member to administer the petty cash under the supervision of the treasurer. This person is referred to as the petty cash custodian.

The initial petty cash fund is created by issuing a cheque. This is called the **imprest system**. The FPC decides on the imprest level. Usually 100 USD would be sufficient for most small business needs. The initial funding and all refunding transactions are recorded as debit in the petty cash account and as credit in the bank account.

All petty cash expenditure must be recorded on a petty cash voucher; this is similar, but not identical, to the expense voucher referred to in 5a for cheque payments. Like the expense voucher, the petty cash voucher is a source document used for registering the transaction in the books. Original receipts from the supplier must be attached to the voucher.

See model petty cash voucher in Appendix 4 N°4.

All petty cash vouchers must be recorded in a separate book: the petty cash book. The simplest way is to use a book similar to the bank cash book suggested above, as the following table shows:

Table 5.3: Sample of petty cash book

PETTY CASH BOOK						
Name of organization						
Date	*Voucher N°*	*Payee*	*Description*	*Income*	*Expenditure*	*Balance*

You may also use an electronic petty cash book, such as that in Appendix 5 N°2.

When the petty cash funds have been nearly spent, they are refunded on request by the petty cash custodian by the exact amount that has been spent. Thus the petty cash balance is restored to the original amount.

Control of petty cash is important because of potential abuse. Prior to refunding, the petty cash book and the vouchers should be checked by someone other than the petty cash custodian. Additionally there should be a routine control check at the end of each month.

It might happen that the organization also *receives* cash payments, for instance, loan repayments (if you have a loan scheme) or repayments of credits granted on sales of goods (if you have a grocery store, etc.). These transactions should be handled separately and not mixed with the petty cash. Each project that receives cash payments must issue special vouchers and open separate petty cash books to manage these transactions. Cash received should be deposited as soon as possible into the bank account, in order to avoid accumulating high cash balances. The forms and controls used for these transactions should be similar to those described in this section for petty cash management.

(e) Procurement procedure

Procurement is the process of acquiring goods and services by an organization. The objectives of procurement are:

- Obtain the best in terms of quality, quantity, timeliness and cost of delivered products or services;
- Conduct business with integrity, transparency, professionalism and fairness.

For hiring personnel, contracting consultants and contractors as well as for procuring material and equipment, the FPC should establish and strictly observe a procurement procedure.

The procurement process depends on the complexity of the issue and the amount involved. The FPC can fix a threshold value (e.g. 500 USD) under which a **short** procurement procedure can be followed. We call it **procurement procedure A**. The steps to follow are:

1. Approval of the expenditure by the FPC as recorded in the minutes. If the expenditure is contained in a project budget already approved, there is no need for an additional decision.
2. Obtaining of at least three quotations for the products required
3. Tabling of quotes in FPC meeting and approval of supplier, recorded in minutes
4. Issuing of written purchase order, which must be authorized by FPC chairperson. For the purchase order, you should use a printed standard form.
5. Payment is made simultaneously with the purchase or subsequently, according to the terms of payment agreed with the supplier. For the payment, a payment order must be issued.

A sample purchase order form is proposed in Appendix 4 N°7

For more **complex** procurements (service contracts) and with amounts exceeding the threshold, a more elaborate procedure must be used. We call it **procurement procedure B**. The steps to follow are:

1. The first step is the same as in procedure A: The expenditure must be approved by the General Assembly or contained in a budget that has been approved by the GA. The decision must be clearly expressed in the minutes of the relevant meeting.
2. Definition of the terms of reference (in case of contracting), technical requirements and product specifications (in case of purchase) by the FPC or the sub-committee responsible for the project. Independent professional technical advice in this step is highly recommended.
3. Tendering: At least three bids must be obtained through a tendering process.

Generally tendering should be open, i.e. inviting potential bidders publicly through the media. Restricted tendering (only a limited number of suppliers are invited) can be used in special circumstances, e.g. when contractors or suppliers have already rendered their services or sold their products in a satisfactory way. But even in cases of restricted tendering, at least three bids must be obtained.

4. The bids should be examined by a procurement committee of at least three members appointed by the FPC. One committee member should be a management delegate.
5. All bids must be opened in the presence of the full procurement committee and recorded in the minutes of the committee meeting.
6. The procurement committee pre-selects three bids and makes a recommendation to the FPC, giving the reasons for its selection.
7. The FPC takes the final decision, which must be clearly recorded in the minutes.
8. The purchase order is issued as in procedure A or the contract is formalized.
9. Payment is made as in procedure A on the basis of a payment order.

(f) Fixed assets management

The objective is to have full control over fixed assets, to ensure maintenance and prevent unauthorized disposal or theft, as well as proper depreciation. The following rules to safeguard fixed assets should be observed:

- All fixed assets belonging to the organization are the responsibility of the FPC. The FPC should appoint an FPC member to look after the care and administration of fixed assets.
- Immediately after acquisition, each item should be numbered and tagged with its ID-number.
- The FPC should maintain a fixed assets register, with the following information:
  - Identification number
  - Description of item
  - Date of purchase
  - Purchase price
  - Annual depreciation and actual value

Table 5.4: Sample form for Fixed Assets Register

FIXED ASSETS REGISTER							
Name of organization							
ITEM N°	DESCRIPTION	DATE OF PURCHASE	PURCHASE VALUE	ANNUAL DEPRECIATION	ACCUMULATED DEPRECIATION	ACTUAL (WRITTEN DOWN) VALUE	COMMENT (REPAIR, DISPOSAL, ETC.)

- Every reasonable care and attention must be exercised to ensure that:
  - Fixed assets are maintained in good working order
  - No assets ‘disappear’ or are disposed of in an unauthorized manner
- Regular physical inspections of fixed assets are required to be carried out by the FPC and the auditors.
- Any time a new FPC is elected the old one must hand over fixed assets by inspecting and writing down the status of each.

- *Depreciation* must be carried out according to good accounting practice. Depreciation is the reduction in value of an asset in the books as a result of wear and tear. An asset loses value over time and depreciation ensures that such a loss is recognized in the accounts. There are different methods of depreciation. The simplest is the straight-line basis method, which is recommended for normal practice. In the straight-line basis method, the asset is depreciated in equal instalments over the period. The duration of the period depends on the life of the asset. For example, a computer is estimated to have a three-year life value. If the computer was purchased for 900 USD, the depreciation will be at the rate of 300 USD per year for three years. After this period, the asset is 'written off', i.e. its *book value* becomes a symbolic 1 USD, although its *real value* is higher. Written off assets must be maintained in the register as long as they belong to the organization.

6. CONTROL / AUDITING

We distinguish three levels of control:
- Internal control
- Internal audit
- External control

(a) Internal control

Internal control refers to the mechanisms ensuring that the organization's resources are managed carefully and transparently. It comprises all measures adopted to safeguard its assets, check the accuracy and reliability of accounting data, promote operational efficiency and encourage adherence to management policies, decisions and procedures. Internal control mechanisms are preventive, i.e. built into daily operations to minimize risk before it occurs.

The objectives of internal control are:
- To ensure efficiency and effectiveness of operations
- To avoid transaction risks (risk of financial loss due to negligence, mismanagement, systems error or human error)
- To avoid fraud risks (risk of loss resulting from theft of funds and other assets, from creation of misleading financial data, reports and financial statements)
- To ensure that financial information is complete, timely and reliable
- To ensure compliance with the law and internal regulations, policies and procedures.

Common internal control measures are:

- **Segregation of duties** involves the separation of responsibilities for two or more tasks that could result in error or encourage dishonest behaviour if handled by one person. For example, assigning responsibility for procurement and cheque writing to two different people.

- **Cross-checking and counter-signing of financial documents** by people not involved in the preparation of the documents: This refers to:
  (i) financial reports such as the bank reconciliation statement or the monthly cash flow report

(ii) documents giving proof of financial transactions such as income and expense vouchers
(iii) documents authorizing financial transactions such as purchase orders and payment orders.

These documents are normally prepared by the treasurer and should be reviewed by two other FPC members: a workers' representative and a management advisor. The workers' representative can be the chairperson, but also another FPC member appointed by the FPC for this responsibility. The management advisor should be appointed by management (if more than one management advisor sits on the FPC).

All the documents mentioned above should have a section at the bottom that contains the following information on internal control:

PREPARED BY	AUTHORIZED or REVIEWED BY (WORKERS' REPRESENTATIVE)	REVIEWED BY (MANAGEMENT ADVISOR)	If applicable: PROCESSED BY (ACCOUNTANT)

The treasurer must make sure that all documents are duly signed prior to the transactions and/or before they are handed over to the accountant.

- **Setting limits on expenditure**: The FPC defines categories of expenditure within amount ranges. For each category a slightly different procedure is used. The higher the amount, the stricter the control mechanisms are. For example, a threshold value is set for cash expenditure, let's say 20 USD per transaction. The next category, ranging from 20 USD to 100 USD can be spent with a normal payment order. Above this threshold, the procurement procedure as described in 5e) above applies.

  Table 6.1: Sample of threshold setting for expenditures

Range in USD	Payment procedure
0 – 20	Cash payment allowed
> 20 – 100	Cheque payment, normal payment order
> 100 – 500	Cheque payment, short procurement procedure (A)
> 500	Cheque payment, full procurement procedure (B)

- **Signature requirements** to protect the organization from unauthorized transactions. The signature requirement as set out in the Fairtrade standards (Standards clause 2.1.5) falls into this category of control mechanisms.

- **Physical controls** are measures taken to verify the existence of assets as reported. For example, counting the cash in the petty cash box and reconciling it with the amount recorded in the petty cash book on a regular basis. Or periodically checking fixed assets (e.g. office equipment) against the register.This should be done at least once a year.

If your operations are computerized, the FPC exposes itself to two types of risk that require additional controls: integrity risk (the risk that non-authorized individuals will gain access to sensitive data), and management information systems risk (the risk of losing key information in the event of the system crashing).

The following measures can be taken to avoid computerized risks:

- **Integrity risk controls**: Creating levels of access and computer access codes usually controls integrity risks. For example, the computer system can be designed so that each person only has access to the items in the computer that are directly related to the scope of their work. Furthermore, each user can have a secret password that allows access. The computer can track which user made which entries into the system.

- **Management information system risk control**: Organizations mitigate the risk of losing key information from the computer database by creating back-up files and storing them at one or more locations, such as in a safe deposit box or at another office.

(b) Internal auditing

Organizations are encouraged to establish internal control bodies constituted by people not involved in the business operations (not FPC members or FPC employees). Such a body is the Internal Audit Committee (IAC) as referred to in the guidance to standard 2.1.12. Though not mandatory, the establishment of an IAC is highly recommended for mid-sized companies, and it is best practice for organizations with a large number of members (100 and above) and/or a high premium turnover. Guidance on establishing an IAC can be found in the Fairtrade Training Manual *Fairtrade Premium Committee Principles.*

According to its terms of reference (TOR) or job description, the IAC may have functions that go beyond the scope of financial auditing. The following recommendations and suggestions refer only to the financial auditing function of this body.

The role of the IAC is **not** to carry out internal control tasks as described above in Section 6a). These are the exclusive domain of FPC members.

The role of the IAC is to oversee the financial management of the FPC to ensure that:
- It serves the best interests of the workers and other beneficiaries
- It complies with the law, the Fairtrade standards, and all provisions of the organization (constitution, rules and regulations, procedures, etc.)
- The internal control mechanisms are adequate and strictly adhered to in practice.

The IAC should perform its role by:
- Continuous monitoring of the FPC's financial performance, particularly its adherence to the procedures and the functioning of internal control mechanisms;
- Periodic review of key documents such as petty cash reports, monthly cash flow reports, bank reconciliations, budget monitoring, financial statements.

(c) External financial audit

An external audit is an independent audit function that provides reasonable assurance that financial reports are free from material mis-statement and are in accordance with legislation and relevant accounting standards. In particular, it should examine the effectiveness of internal controls, the accuracy and timeliness in recording transactions, and the accuracy and completeness of financial reports. It is normally conducted at the end of the business year, when the financial statements are finalized. But it can be ordered at any time in case of suspicions of mismanagement or fraud.

Only qualified and registered auditors complying with the legal requirements can provide external audit services. The independence of the auditor is crucial to a correct and thorough appraisal.

Sources used in the elaboration of this manual

Accounting Manual for JB Members and Internal Auditors elaborated in the frame of the flower programme of Max Havelaar Switzerland by Janet Okanga (Kenya)

Manual de Tesorería elaborated in the frame of the flower programme of Max Havelaar Switzerland by Gloria Rueda (Ecuador)

The formats in Appendix 1 have been adapted from forms elaborated by Julia Malquin, Fairtrade Liaison Officer for the flower sector in Ecuador and Colombia.

The formats in Appendix 5 have been developed by the flower programme of Max Havelaar Switzerland.

The main source used for describing the accounting cycle in Chapter 3 Accounting and Bookkeeping was:
http://www.netmba.com/accounting/fin/process/

For accounting principles and standards the main source used was:
SWISS GAAP-FER – Accounting and Reporting Recommendations, particularly Chapter 21 on Accounting for charitable, social non-profit organizations.

For generally accepted accounting principles:
http://en.wikipedia.org/wiki/Generally_Accepted_Accounting_Principles

For international financial reporting standards and international accounting standards:
http://en.wikipedia.org/wiki/International_Financial_Reporting_Standards

For technical terminology on finance and accounting:
http://en.wikipedia.org/wiki/Accounting

APPENDIX :

APPENDICES 1-5 present examples and can be downloaded as separate documents from our webpage

APPENDIX 6: Proposed text elements for a master presentation

1 Financial Planning

Budget and budgeting

A budget is a work plan expressed in monetary terms
It shows what you expect to earn (= income) and to spend (= expenditure)
The budget has two objectives:
First, to know how much money you need for a specific undertaking (project)
Second, to monitor financial performance in the course of project implementation
This chapter is about the overall budget of the organization, not about individual projects

The steps in budgeting

Define activities, as described in the yearly work plan
Estimate expenses for projects, capacity building and administration
Estimate income: surplus from previous year, Premium income, income generated by projects (if applicable) and other income (donations from third parties and interest on savings and investments)
Check the balance: income should cover expenses
(Explain 2.1 Sample budget)
The cash flow forecast ensures that money is available at the right moment

2 Accounting and bookkeeping

Function of accounting: to process financial information in order to know the financial performance- amounts earned and spent and the resulting surplus or deficit
The accounting system commonly used is double-entry bookkeeping
Each transaction is recorded twice, as DEBIT and as CREDIT
(to explain how this actually works, please refer to p. 9 of the module)
The total of debit values must always equal the total of credit values
The **accounting cycle** refers to the whole process from the transaction to the closing of the books
It has the following steps:

- Preparation of **source documents** = supporting documents that show that a transaction has taken place (invoice, deposit slip, etc.)
  This step must be done by treasurer
- **Journal entry** = transaction is recorded in chronological order in a book
  Entries are made as debit in one account and credit in another account
  This and the following steps are usually performed by the accountant (a professional)

- Posting of journal entry in **general ledger** = a record of transactions organized by accounts. Accounts have a T – form (see examples on pp. 11-12)
- **Trial balance** = the sum of all debits and all credits of the ledger accounts, it must be equal
- **Adjustments** = entries in the ledger accounts to give the real picture of all transactions affecting the current business year
- **Financial statements** = the financial summary after closing the books (end of cycle)
  Financial statement consists of two parts:
  Income statement = the sum of all income and expenditure during the year (usually Jan 1 – Dec 31)
  Balance sheet = a list of all properties and debts and the capital owned by the organization at a specific moment (usually end of month or end of year)

3 Financial reporting

- Information to the **Fairtrade Premium Committee**: responsibility of treasurer
  Must inform FPC meetings on Premium income, expenditure and balance
  Best practice is monthly reporting
  Explain reporting formats proposed (Appendices 4 N° 1 and 5 N° 1)
- Information to **workers**: responsibility of FPC, not only treasurer
  Annual financial report (income statement and balance sheet) to GA
  Annual presentation of the budget (together with work plan) to GA
  More frequent reporting is recommended, e.g. monthly report on Premium income and expenditure on notice board
- Information to **Flocert**: responsibility of FPC
  Annual financial report and budget as presented to GA
  Updated information on Premium income, expenditure and balance to inspector during inspection

4 Financial procedures

These procedures should be followed by the FPC and especially the treasurer

- **Preparing source documents** (by treasurer)
  Income voucher for each income (Premium income, repayments of debts, etc.)
  Expense voucher for each expenditure (purchases, disbursement of loans, etc.)
- **Payment procedure** (by treasurer and all FPC members handling funds)
  Describes and regulates the steps to be followed prior to making payments
  System of checks and balances for transparency and security
  (Explain steps of procedure as on p. 17)
- **Bank account management** (by treasurer)
  Recommendation: have **one** current account for all regular operations
  Treasurer must keep record of all transactions affecting bank account (cash book)
  Bank must send monthly statement of current account
  Treasurer must compare records in cash book with bank statement
  If balance is not equal, verify reasons
  Probably bank reconciliation is required to equal balance (please refer to p. 22)
- **Petty cash management** (by petty cash custodian, someone other than the treasurer or the chairperson)
  Petty cash is used only for payments of small amounts
  Petty cash is established by issuing cheque for the amount defined by FPC (imprest level)
  When petty cash is nearly spent, it is refunded to restore the imprest level

All cash payments are recorded in the petty cash book

- **Procurement procedure** (to be followed by all FPC members involved in procurement)
  Procurement is the process of acquiring goods and services
  Organization should strive to get best product or service at best conditions
  Procurement procedure should ensure best results and transparency
  (explain steps described on pp. 24-25)
- **Fixed assets management** (to be followed by treasurer or assets manager)
  Objective is to have control of fixed assets, ensure maintenance and prevent theft
  (explain rules on pp. 25-26)

5 Control / auditing

- **Internal control** = mechanisms for self-control established by FPC for FPC
  Separation of duties
  Cross-checking and counter-signing of financial documents
  Setting limits on expenditure
  Signature requirements (e.g. joint signatories, worker and manager)
  Physical controls
- **Internal auditing** = control by a body of the organization different from FPC
  Best practice is establishment of Internal Audit Committee (IAC)
  It is elected by GA and accountable to GA
  Role is to supervise and control financial management performed by FPC, especially compliance of norms (standards and internal procedures)
- **External audit** = financial control by a professional auditor independent of organization is best practice for organizations with high premium volumes
  Recommended for all other organizations
  Auditor checks books and financial statement at the end of fiscal year
  Can be called any time in case of suspicion of fraud or mismanagement

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