# 25. Managing the Finances

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## FINANCIAL MANAGEMENT

Financial management and control is unquestionably one of the most critical challenges in the operation of social programs. Properly instituted, it is a valuable tool for achieving program goals and enhancing program performance. A competently developed fiscal management structure provides service administration and staff with a vital planning aid, impelling awareness of a program's totality and the interrelationships among its parts. It makes personnel aware that undisciplined expenditures in one area of activity reduces essential financial support for another area.

Fiscal control also functions as an evaluation and monitoring instrument, producing information that can reveal errors in program design and faulty patterns of service practice. No responsibly conducted service program can exist without this information, and the greater its accuracy, the greater are the chances for the program's success.

The administrator and his staff must also be alert to the very real possibility that instances of inept fiscal management will be exploited to discredit their program. While improper accounting is not indicative of a poor program, critics are not necessarily constrained by the niceties of logic. Those opposed to a program will not hesitate to use accounting deficiencies to generate public doubt about the validity of the program concept and performance. When subjected to such an attack, an administrator is hard pressed to defend the value of his program. The public is extremely sensitive about the handling of public funds and quick to presume that faulty accounting is uncontestable evidence of general administrative incompetence.

In the area of grant funds, preoccupation with fiscal control has intensified in recent years. Mounting concern is justifiably evidenced not only by funders but by the public at large. Too many social programs have fallen into disrepute because of apparent administrative indifference to competent fiscal accounting.

### FISCAL CONTROL PROCEDURES

Competent fiscal management consists of a set of related functions. For purposes of discussion, we will separate these into two groups: basic functions, and additional procedures.

### I. BASIC FUNCTIONS

Four interdependent functions make up the basic fiscal process: budgeting, accounting, receipt and disbursement or custodianship, and auditing. Properly integrated, the combination provides administration with a series of checks and balances for controlling the allocation and use of funds.

The process is structured differently from setting to setting, with the differences largely determined by organizational size. In very large settings where a sizeable number of fiscal transactions occur daily, each function may be the responsibility of a separate management

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unit, with segregated lines of accountability directly to the administrator or a deputy administrator. In many instances, especially in the governmental arena, the custodial function may be invested in another agency, such as the city comptroller's office.

In small organizations with a very limited fiscal flow, the natural tendency is toward the consolidation of functions in a single management unit. Even in these instances, some division of function is usually instituted to insure a proper and responsible administration of funds. For example, the director of an agency may keep the books while a fiscally experienced member of the board serves as the agency's treasurer, with the power to issue checks.

**The Budgeting Process**

The budgeting process possesses a mystique for many service personnel. Actually, there is nothing mysterious about a budget. It is a product of human analysis and judgment, and once formulated inherits no self-contained and impelling authority. Its value will be no greater than the thoughtfulness and care put into its construction and the intelligence and skill invested in its use.

An administration must avoid at all costs assuming or conveying the notion that a prepared budget is immutable. Not to adapt a budget to changing circumstances is as irresponsible as to ignore the document altogether. If correctly managed, the budget is subject to constant review and adjustment as new and anticipated events arise during the fiscal year. Otherwise, it would fail to serve its purposes of facilitating administrative decisions, guiding expenditures, and providing an accurate record that can be used for planning funding allocations in subsequent years.

Reduced to its simplest terms, a budget is an estimate of how anticipated income during a designated period of time will be distributed among competing forms of agency activity. It relates costs to categorically itemized sets of inputs or resources required in performing an activity, to the programs or services the agency provides, or to the objectives or outcomes these services are expected to accomplish. The itemization used depends on the uses of the budget and the type of information it is intended to transmit to the various organizational audiences.

When the objective is to specify the level of investment allocated to various operational divisions of an organization, a *resource budget* is prepared. When it is to define the proportion of total operational income allocated to each of the discrete programs of an agency, a *program budget* is relied upon. And when the objective is to relate cost to production or outcome of service, a *Program Planning and Budgeting System* (PPBS) is used.

The PPBS is the most sophisticated form of budgeting and is coming into increasing prominence in the social service field. Its value lies in focusing administrative attention on the crucial issue of an organization, i.e., the relationship between expenditure and what that expenditure buys in the form of benefits to clients and actual agency accomplishments.

When PPBS is properly implemented, the budget structure or categories will be stated in terms of major goals of the organization. Each goal, in turn, will be interpreted in the form of an objective or objectives, and the objectives to the extent possible translated into measurable quantities.

For example: If one goal of an Area Agency on Aging is to enrich the nutritional diet of a population of older people, an associated program may be the provision of communal eating experiences. One aspect of such a program would be the serving of congregate meals. The objective would and should be expressed in quantifiable terms: the number of meals to be provided and the number of people to be served over a definitive period of time. Other objectives of the program may not readily lend themselves to rigorous quantification, since they refer to subjective qualities such as personal satisfaction. This type of objective is translated into some approximate measure, such as the attendees' personal assessments of the program.

Implementation of PPBS has distinct implications for agency structure. It can be effectively performed only if the organization includes ongoing and integrated planning, budgeting, and evaluation functions. Through this integration the organization engages in a constant process of research and assessment directed to identifying the most cost-effective alternative means of accomplishing objectives. Cost-effectiveness pertains to the means that provide the greatest benefit per unit of expenditure.

PPBS is a highly complex process and still in a formative stage with many uncertainties, especially as applied to the social service field. Area Agency on Aging personnel are encouraged, however, to become familiar with the process as it is developed. PPBS will undoubtedly play an increasingly influential role in federal and state funding decisions.

Another type of budgeting with which personnel should become acquainted is *performance budgeting*. It is a less complicated procedure than PPBS, but retains some of the latter's advantages. Unlike PPBS, performance budgeting presents no information about accomplishments, but it does focus administrative attention on the relationship of expenditures to a program or distinct agency service. The budget structure consists of categories identified by separate areas of service: *information and referral, nutrition, home health care,* etc. In this way, as with the PPBS budget, administration can see the total costs allocated to one organization service and compare that cost with expenditures assigned to other priority services. Its value lies in ignoring the functional divisions of labor that characterize an organization, and relating every cost of a program to a specific service, regardless of the division performing it.

Every program budget eventually must be converted into a *line budget* which relates expenditure to personnel functions and activity supports. This conversion is termed a "crosswalk." In most situations, the line budget stands alone for guiding agency administrative decisions and allocations.

The reason the line budget assumes such a common and prominent position is that it is especially constructed to serve as a fiscal control document. It tells the administrator exactly what proportions of income are allocated to the various functional units or divisions comprising the organization, and tells the unit managers the cost parameters within which they must be prepared to perform. In addition, it provides accounting staff with an instrument for assessing rates of expenditure, determining which units are under- or overspending assigned allocations, and informing the administration when corrective action in relation to appropriations is required.

The line budget is familiar to most personnel. It is the form used by both public and private funding sources for grant requests, and simply stipulates how a requested amount of financial support will be invested in resources to accomplish the objectives and activities described in the narrative of the grant proposal.

The budget structure is characterized by such designations as *personnel, equipment, facilities* (rental, leases, etc.), *supplies, travel,* and other types of costs. A completed agency line budget consists of a series of subbudgets and a master budget. Each subbudget indicates the amount of income allocated to a single agency unit—the administrative staff, accounting office, information and referral unit, counseling staff, etc.—and how the money will be used. The master budget provides the representation of how total income is to be distributed among these interrelated organizational divisions.

In preparing a line budget or any other type of budget, competence is exemplified by the inclusion of all relevant detail about a category of expenditure. Under *personnel,* for instance, it is not sufficient simply to present the amount to be expended for this category. The budget should show such things as the number of persons to be paid from the allocated funds, their classification if a classification system is in effect, rates of pay, and percentage of working time each employee is to contribute to the unit. In most instances, basic information is presented on the budget sheet and an explanation and elaboration of the presentation follows on attached sheets headed "Budget Justification."

When an agency has operated for a year or more, the budget should present comparisons of the current year with past ones, providing explanation and justification for any changes. These justifications should be brief and to the point, providing administration with only the salient information needed to decide whether the change is merited and feasible in light of other budgetary demands.

Skill in budget preparation is attained only through experience. With time, those contributing to the preparation learn what to report and how much to report. They learn to avoid not only underreporting, a common error, but the even more pervasive error of overreporting. The latter error tends to occur if (a) the budget process limits communication between unit representatives in regard to the prepared budget, and does not allow for subsequent discussion of the document between administration and unit personnel, or (b) unit personnel fail to understand that they will have opportunity in a review to elaborate on information contained in their budget submission. Overreporting can be as deadly for the administrator as underreporting. It drowns him in information, often leaves him confused, and absorbs time that he could put to better purpose.

A well prepared budget submission will contain only:

1. Whatever detailed information the administrator needs to understand how requested funds will be used and how their use is expected to contribute to agency interests;
2. The information the accountants need to assess whether or not funds are being expended as mandated.

Additional clarification should be retained for presentation during review if requested.

The above discussions have touched on what are known as operating budgets. Still another type of budget is called a *capital budget.* This budget is prepared by organizations to cover long-term capital investments (buildings, expensive equipment, etc.) which are financed over many years. It is highly unlikely that area planners in aging will be directly concerned with this type of budgeting, but they should be aware of it since many of the organizations with which they deal will be involved with capital financing.



**The Accounting Function**

Accounting is the day-to-day control function of the fiscal management process and involves the maintenance of continuously updated and accurate records of the flow and relationship of income and expenditure as prescribed by the budget. Its purpose is not only to ensure that funds are spent as prescribed and that expenditures do not exceed expected or available income, but that the rate of expenditure is appropriate.

Too often the accounting procedure is misperceived; it is seen as simply a process for determining whether or not current expenditure overreaches currently available income. Competent accounting is a much more complex procedure. It entails looking ahead from any given time within the fiscal year and determining with relative assurance that expenditures and ascertained operating income will be closely in balance at the close of the year. Such forecasts are difficult because many units of an organization do not expend monies at a constant rate. The nature of their function necessitates varying levels of expenses throughout the year.

*A helpful way to visualize this differential rate problem is to think of a year-round camping program organized to serve older people during the holiday seasons. During the summer months costs will maximize, with the organization carrying a full complement of staff and expending funds for actual operation. Once school opens, cost will reduce to a low point with only a small staff and their maintenance placing a demand on income. Costs will again approach maximum during the Christmas season, then drop off until they mount again during the Easter holidays.*

Because of such fluctuations, an accountant simply cannot relax when expenditures are in a low trough. He must be constantly assessing the rate of low expenditure to determine whether it is draining off income that will be required to cover the committed level of efforts at a high point of expenditure.

Actually our example oversimplifies the forecasting task. It implies that concern is restricted to the fluctuation of aggregate expenditures for the total organization. This, however, is seldom the case. The Area Agency on Aging, like most agencies, will be administering a number of accounts reflecting the correlation of expenses and allocated income for multiple operating units. The ups and downs of the expense curves for each of these accounts will be different. Consequently, the accountant must be making multiple forecasts to ensure that the income-expenditure relationship is in alignment for each unit of an organization.

Fluctuating expenditure rates are not the only complicating factor for accounting. Income can present analogous problems, especially when agency funding is based on governmental appropriations and public and private grants.

Few social service organizations today have the luxury of depending on a single funding source. Instead they obtain their operating income from a range of governmental agencies and private grantors, from which funds are received at different points throughout the fiscal year. On occasion, expected funds are late in arrival because of delayed actions by public and private funders, and the amount received may vary from the amount anticipated. All these factors create budgeting and accounting headaches.

The budget is generally based not on money in hand but on receipts expected during the fiscal year. Invariably a degree of risk is involved in estimating income. How much risk there is will depend on administrative judgment, but the general rule is not to plan on other than reasonably certain income and to revise the budget should "possible" income materialize at a later date. A more speculative approach to budgeting can be disastrously misleading. Those responsible for accounting can become lulled into the impression that income estimates are reasonably definite, and reflect this in the allowed rates of expenditure. The error of their ways is not brought home until possible income included in the budget fails to materialize, and then a fiscal crisis occurs.

There is no easy way to handle the differential flow of income over the fiscal year. Accounting is usually denied the benefit of pooling, or *co-mingling*, funds received from different sources in order to pay bills from a central pool without regard to what agency unit contracted them. Each funding source usually sets constraints on how its funds may be used. Because of these constraints, accounting is impelled to set up and control multiple accounts and forecast the income flow for a specific account against legitimate expenditures from that account.

This structure of separate accounting for differing aspects of agency activity does not pose total inflexibility in making money transfers as conditions dictate. Government as well as many private funders recognize that agencies can be caught in fiscal binds. Income for a particular activity can be late in arrival, or a peak in expenditure can deplete income before the scheduled date of replenishment. Unless accounting can borrow from another account where funds are in adequate supply, the activity will be placed in jeopardy or terminated. Funders of the other account will usually permit this borrowing if the agency follow the funder's procedures and correctly requests permission to make a temporary transfer.

Sometimes the transfer is not between accounts but between categories within a given account, as when one category of expense has exceeded the predicted while another is running under the anticipated amount. Here again, accounting must not act without proper clearance with the funder. In all instances when requesting transfer of funds, the agency should insist on receiving permission in writing in order to avoid later misunderstandings when accounts are subjected to an outside audit.

Sometimes when an agency is short of funds in an account but in good fiscal standing, it elects to cover a momentary deficit through a bank loan against the impending receipt of income. This option should only be used when other alternatives are foreclosed, and the agency has the funder's concurrence. In most instances of this kind, the funder will not agree to paying accrued interest on the loan.

To effectively forecast and maintain fiscal control, the accountant should command information on encumbrances. Too often he does not learn of an expenditure until he receives the bill from the supplier —a month or more after the actual commitment to purchase, or the encumbrance of funds. The encumbrance of large sums without accounting's knowledge can be extremely misleading. The accountant is led to believe the unit is operating within its spending limits, only to learn after the fact that the unit has overspent. Only if informed immediately whenever an encumbrance is made can accounting provide effective fiscal control and engage in competent forecasting.

Because his function centers on control, it is evident why the accountant's role is often a source of conflict and he is seen by practitioners as an irritant if not an obstacle to service. His day-to-day interactions with other staff tend to deemphasize the values his function can contribute to organizational welfare by preventing fiscal crises and providing information and guidance for more efficient and effective provision of service.

The potential for conflict can be significantly reduced, if not eliminated, if organizations refrain from isolating the fiscal control function and concentrating it in the accounting unit. In a properly structured situation, control is a shared responsibility, with the accounting office providing only leadership and support to other units. It is incumbent on the staff of each unit to participate actively in each phase of the fiscal management process and remain in continuous communication with the accounting office. Such arrangements can dissipate the myth that service and fiscal management are disassociated functions.

### Fund Custodianship

Custodianship is a minor concern for most service organizations, since their administration rarely touches cash. In the case of federal appropriations and grants, a letter of credit is usually deposited with a local bank and the agency draws on this credit through a voucher system. These vouchers are an integral part of the accounting system and serve as back-up documentation when agency accounts are audited. Many administrators countersign each voucher, though this authority may also be vested in subordinates, because they believe the procedure adds to control and keeps them appropriately informed about the organization's fiscal activities.

Custodial procedures will of course differ with funding sources. Those mandated by federal authority are not necessarily the same for state, county, or city government, and the agency must adapt its fiscal management to conform to these variations.

While the agency is unlikely to handle large sums of money, it probably will have petty cash funds in its direct care. It is important that these funds also be subjected to accurate accounting, and petty cash expenditures periodically integrated into the appropriate program accounts.

Equally important is the administration of petty cash. Preferably it should be administered by one person, never scattered around among units or kept in easily accessible places. It should never be allowed to exceed one hundred dollars.

### The Auditing Procedure

Audits take place at intervals and involve the examination of fiscal records to determine whether expenditures have been made in conformance with appropriation regulations, are in the proper amounts, and have been properly documented. The procedure can be either an internal audit (done by the agency's accounting staff) or an external audit (done by a governmental or other outside accounting group).

Traditionally, auditing is conceived as fiscal review instituted to ascertain whether any irregularities have occurred in the handling of funds. In recent years, however, the concept of *performance audit* has been introduced. Performance audit is an evaluation process designed to assess the relationship of expenditure to the conduct of a program and the achievement of its goals. The process is obviously not as precise as financial auditing, since it entails qualitative judgments and the use of operational standards that cannot be as exact as monetary measures. Nevertheless, the process is being used more and more by federal and state funders, and administrators should be aware of the trend. It provides an additional reason why administrators must be able to effectively relate service activity and the expenditure categories discussed earlier.

## II. ADDITIONAL PROCEDURES

### Purchasing

In the course of administering a program there will be many occasions when small or large purchases must be made. Ordinarily a dollar amount is set above which purchases must be done through competitive bidding. When an item to be purchased is in this category, at least three estimates should be obtained from different vendors. All other factors being equal, the item should then be purchased at the lowest price. At times there may be reasons (better service, reputation, etc.) to purchase from a vendor whose price is not lowest, but these decisions should be carefully documented in case they are ever questioned by auditors.

Most items to be purchased fall below the price range where competitive bidding is required, but in many of these cases it is still desirable to shop around for the lowest price. If the operations of the program are located in a community where there are several competing vendors of certain items, it is advisable to alternate the choice of vendors so that no charges of favoritism can be justified.

The administrator of a program should also set internal limits as to the level of purchases made by subordinates at their own discretion. Certainly the purchase of any major items should be approved by the administrator and handled by voucher so that adequate records are kept. Where items are delivered there should always be someone able to verify the accuracy of the items against the invoice accompanying them. No items should be received C.O.D. without such verification, and certainly no vouchers should be issued for payment without verification.

A matter to bear in mind is that all purchases made by governmental bodies (federal, state, or local) are free of federal taxes. A form indicating the tax-exempt status of the organization should accompany all purchases where federal taxes are being waived.

### Supply Management and Inventory Control

Periodic inventory of major items in the possession of the program is important. Equipment such as furniture, typewriters, calculators, movie projectors, etc., should have tags affixed that are difficult to remove. Each tag should contain at least the initials of the agency and a series number for identification of the item of equipment. The list of serial numbers and descriptions of the items they identify should be checked and updated at regular intervals of perhaps six months or a year. Where items are borrowed or taken off the premises for use at another location, they should be signed out so that the location of all items of major equipment can be ascertained at any time.

In the control of ordinary supplies a good administrator should steer a middle course between petty possessiveness and frivolous waste. Ordinary items such as paper, pencils, staples, clips, ribbons, etc., should be readily available for the use of staff. Records of available supplies on hand are as much a guide for replenishing dwindling supplies as an indicator of the extent of use of these items.

### Property Management

Occasions will arise when administrators of programs will need to go out and rent or lease space for their activities. Much care should be exercised in finding



out the going rate per square foot in the area, the types of facilities available, and what services are included in the rental. Locations should be looked at in terms of easy accessibility, availability of parking facilities, closeness to other offices, restaurants, bus lines, etc. In deciding where to rent space, the procedure should be similar to that for the purchase of major equipment; that is, proof must be shown of comparison shopping, and where a place other than the lowest priced one is chosen, adequate rationale must be provided for the selection. Obviously the costs of renting space should not exceed the amount budgeted for that purpose.

In negotiating with the property owner or manager, both sides should make clear in writing the understanding reached regarding any alterations to be undertaken and who is to pay for them. Understanding should also be reached as to who is responsible for custodial and maintenance services. The longer the lease the program is able to commit itself to, the better the terms that can be negotiated. Therefore, the administrator of the program should find out from the central administrators for how long a term he is legally able to lease facilities. In no case would it be for a period of less than a year.

### Phone Service

Associated with the choice of facilities is telephone service. Adequacy of service of course depends on the number of people using it, the availability of incoming lines for people who call the agency, and the ease with which personnel can make or receive calls. These are matters that can be negotiated with the phone company and should not present much of a problem. What is of somewhat greater concern is the control over toll or long-distance calls. Careful records should be kept and turned in monthly by all persons authorized to make such calls, and these should be checked against the itemized charges made by the phone company. There may be times when greater use is unavoidable (prior to conferences and other long-distance matters), but adjustments must then be made on an annual basis so the totals do not exceed the budgeted amounts.

One item of caution regards keeping phones locked when facilities are being used by public or clientele groups without staff members present. Failure to do this has resulted in abuse and lack of control of phone service—a favorite target of outside auditors.

### Travel

Personnel of the program will on occasion travel in the conduct of their assignments or to professional meetings and other types of conferences. Allowable costs for travel in mileage allowance, air fare, lodging, meals, etc., are carefully set forth by the federal government and are altered from time to time. Where federal monies are involved, current regulations should always be followed as closely as possible. Aside from normal travel in carrying out routine duties, subordinates should never engage in trips unless they have the prior approval of the person in the program authorized to grant such approvals. And, as with all other expenditures, the amount spent for travel by personnel of the program should never exceed the amount set aside in the budget for that purpose.

### Payroll

Records should be kept of hours worked by all personnel, absences, sick leave, vacation time accumulated, etc. No payroll should be approved without the necessary documentation to back it up. Where paychecks are not mailed directly to individual recipients, but sent to the agency for disbursement, each employee should sign his name next to the appropriate date on a listing as he picks up his check.

### Record Keeping

From the start a filing system should be developed in which all receipts and other fiscal records are kept. Duplicates of all receipts given for money from individuals or groups should be available for auditing purposes, as should duplicates of all invoices, vouchers, and other records of transactions and activities of the agency.

If one must err, it should be on the side of being overmeticulous in the maintenance of good financial records. These records can be of great assistance to the Area Agency administrator in planning and evaluation, as well as providing the necessary documentation for auditing purposes.

## SUMMARY AND CONCLUSIONS

The skills involved in proper financial management are not inborn, but rather must be cultivated and nurtured. When questions arise regarding fiscal matters, an administrator should not hesitate to seek assistance and guidance.

Specific guidelines for proper financial management will be provided by fiscal officials, and an administrator should become thoroughly acquainted with them. However, if one were to extract rules of behavior for proper financial management they would be as follows:

1. Always attempt to relate financial facts and figures to the program being carried out: What has been served? What activities did the money provide? What level of services?
2. Never transfer funds from one account to another or from one budget category to another without written approval by a top fiscal official of the agency.
3. Be a stickler for adequate documentation of all financial activities—purchases, leases, payroll, travel, account transfers, budget transfers, phone usage, postage, and all other activities involving finance.

While specific details of management may differ from one organization to the other, the basic principles are fairly similar. It is the basic approach in terms of the aforementioned suggestions that an administrator should cultivate.

It is to be hoped that the time will come when programs will be judged and funded on their own merits, but in the meantime much is riding on the attention—or lack of it—paid to the more mundane aspects of financial management in the carrying out of all public programs.