Purpose of consolidated accounts

This note describes why a consolidated accounting statement is appropriate to have as an organisation and how it can be useful for a partner. The document describes the importance of accountability, and the nature of financial statement and of financial management.

**Accountability**Accountability is an assurance that an individual or an organization will be evaluated on their performance or behaviour related to something for which they are responsible.

The term is related to responsibility but seen more from the perspective of oversight. An employee may be responsible for ensuring that XX meets all the stipulated requirements. In the event that the task is not performed satisfactorily, there may or may not be consequences. Accountability, on the other hand, means that the employee is held responsible for successfully completing the task and will have to at least explain why they failed to do so.

Organisational accountability involves being answerable to all an organization’s stakeholders for all actions and results. Through performance and accountability reporting, an organisation compiles and documents factors that quantify its economy, efficiency and adherence to budget, comparing actual results against original targets. The performance and accountability reporting process is usually carried out quarterly, and audited once per fiscal year, although in some cases it is done more often.

Why is downward accountability to beneficiaries important?
It is widely recognised that OPDs are most effective when they are accountable to the persons they aim to help. This means explaining their work to local people and involving local people in making decisions about their activities known as ‘participation’.

Why is upward accountability to funding partners important?
Funds are ultimately given to beneficiaries, not to organizations for the organizations' own sake. The organisation has a responsibility to make sure that it is as useful to beneficiaries as possible. The verifiable reporting format for this is the audited financial statement.

**Financial statements**
Financial statements are produced from the organisation's accounting records. They are a summary of all the transactions for a specified period of time and show the financial position of an organisation. In particular, the financial statements tell us:

* where the organisation's money came from
* how the money was used up
* the financial outcome for the period, ie a surplus or deficit
* what the organisation is worth (on paper).

Financial statements can cover any period of time – for example, a month, a quarter or one year. The annual financial statements are used as the basis for the annual accounts and external audit.

**Financial management**
Many people have the impression that financial management is just about keeping accounting records. In fact, it is an important part of programme management and must not be seen as a separate activity left to finance staff. Financial management **entails planning, organising, controlling** and **monitoring** the financial resources of an organisation to achieve objectives.

Financial management to a OPD is rather like maintenance is to a vehicle. If we don’t put in good quality fuel and oil and give it a regular service, the functioning of the vehicle will suffer and not run efficiently. If neglected, the vehicle will eventually break down and fail to reach its intended destination.

At the heart of financial management is the concept of financial control. This describes a situation where the financial resources of an organisation are being correctly and effectively used. This will only happen if strong and relevant financial policies and procedures are put in place.

Poor financial control in an organisation means that:

* assets will be put at risk of theft, fraud or abuse
* funds may not be spent in accordance with the OPD’s objectives or funding partners’ wishes and
* the competence of managers may even be called into question.

OPDs operate in a rapidly changing and competitive world. If they are to survive in this challenging environment, they need to develop the confidence and skills to manage their financial resources and achieve more with their money.

Good practice in financial management will:

* help managers make effective and efficient use of resources to achieve objectives and fulfil commitments to stakeholders
* help OPDs to be more accountable to funding partners and other stakeholders
* gain the respect and confidence of funding agencies, partners and beneficiaries
* give the advantage in competition for increasingly scarce resources
* help OPDs prepare themselves for long-term financial sustainability.

What are consolidated financial statements?
When an organisation runs multiple projects and departments, managers need a way to easily combine - or consolidate – multiple financial statements into one table, to give a useful overview at the programme or organisation levels, including the core costs/central support costs.

The consolidated financial statement will support the management, beneficiaries, funding partners and other stakeholders with the full, holistic picture of the organization instead of only having access to information about part of the it.

It will show the overall performance of the organisation, and its financing, strengths, weaknesses and vulnerabilities will be highlighted, and synergies between projects will be clarified.

The donor diversification may be highlighted through an income and expenditure specification. A funding grid may provide an overview of who is funding what at project, programme or organisation -wide levels. It will be clarified with what financial strength the individual funding partner's opinions and attitudes weigh in the total sum of influence.

An issue for additional attention and vigilance in the consolidated statement will be ***Accounting for shared costs.***

Some costs cover more than one project or activity. In this case, it is important to identify which activities the costs should be charged to. There are two types of shared costs:

* Those that are truly **direct costs** and belong to two or more projects
* Those that are truly **indirect costs** that must to be shared across all projects in the organisation.

For truly direct project costs – e.g. the cost of fuel using a shared vehicle for project activities – these must be **allocated** according to actual use to the relevant project cost centre (a cost centre is the lowest cross cutting dimension on which registration takes place, e.g. on project or department.). It is best to make the allocation when the transaction is entered into the accounting records.

For truly indirect costs – i.e. core costs such as the central office running costs or the annual audit fee – these must be **apportioned** in a *fair* and *justifiable* way across all cost centres.

Core costs are often shared out between cost centres in a pre-arranged ratio. This is more commonly entered in the accounting records at the end of the reporting period by making one adjustment entry.

The decision on how to apportion costs between cost centres can be based on different criteria according to what is known as the *cost driver*, e.g.:

* Full-time equivalent staff

Example of the difference between direct and indirect costs using a car:

Fuel for a project visit will be a direct cost and it will be allocated on the project according to fuel bill or kilometers, whilst fuel for a general bank visit will be indirect cost to be apportioned later on the basis of the agreed key/cost driver.

* Number of cost centres
* Size of each project budget
* Project staff costs
* Amount of space used by a department.

There is no hard and fast rule for apportioning core costs to projects. It should however be **logical, transparent and consistently** applied.

Genuine model for a consolidated financial statement is illustrated below:

