

Project budgeting John Cammack

How To guide
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Why bother with budgeting?

Budgeting is one of the best tools for planning and monitoring. It keeps our finances in good order and, more importantly, helps us to achieve our programme objectives. Simply put, good budgeting means good development.

If the project or organisation relies on outside funding, budgeting is essential. A funding proposal will require a planned budget, and most donors want to see regular monitoring reports.

Budgets are used to:

- Plan and implement our objectives
- Calculate estimated income and expenditure
- Maximise donor funding
- Co-ordinate activities
- Communicate plans
- Set clear targets
- Quantify the resources and people needed to achieve them
- Monitor, review and evaluate actual performance
- Be accountable to partners, beneficiaries and donors

Who is responsible for a budget?

Managers and staff responsible for the activity should prepare and monitor budgets and see **detailed** transactions. Finance staff are a technical resource, who often provide information and make sure that the process is completed professionally.

Trustees should monitor a **summarised** version of the budget and ask questions about the big picture.

Planning a budget

There are seven simple stages:

1. Identify project or organisational objectives

Involve a range of staff and stakeholders in this.

2. Decide on limitations

Identify any limits to resources and funds available at the start.

3. Gather data

For example:

- Previous year's budget and latest information on actual income and expenditure
- Estimates of running costs, income and grants
- External factors influencing income and expenditure (such as exchange rates, predicted inflation)

4. Decide how much will be received (income)

Be as realistic as possible. Show lower estimates of donations and charges. Only include guaranteed grant income.

5. Decide how much will be spent (expenditure)

Separate items into types. This may need to follow your own organisation's and/or your donor's standard list of budget headings.

6. Construct the budget

List the budget item by item, making sure that income is at least as much as expenditure. Provide a note of calculations to justify them.

7. Obtain approval

Obtain approval from your own organisation's trustees and any donors involved.

Monitoring a budget

After approval, and before the period starts, tell everyone who needs to know the budgeted figures. If funded by an outside donor, make sure you will be able to report in their format.

If you have several donors, consider producing a 'donor funding grid', a convenient way of maximising and managing donor funding. For more details and a spreadsheet template for a donor funding grid: www.johncammack.net/ (click on Resources/Project budgeting).

After you start receiving and spending money to implement your programme, it is essential to monitor regularly how close the actual income and expenditure is to the budget.

The stages are:

1. Prepare or receive the information comparing the budget with 'actual'

A comparison of the budget to 'actual' income and expenditure is normally prepared monthly or quarterly. It is sometimes called a 'budget and actual' statement (see Figure 1), 'management accounts', 'budget report' or 'variance report'.

2. Monitor and review the 'budget and actual' statement

Those responsible should identify any difference between each budget and actual income and expenditure item – 'the variance' – and be able to explain the reason(s) for this. Add notes to the statement to show why there are differences. Notes are helpful when working with partners at a distance.

Figure 1

Example of a budget and actual statement with notes for the first three months of the year

Western Province Health Centre Budget and Actual Statement

	Annual budget 12 months	Budget (Jan-Mar) 3 months	Actual (Jan-Mar) 3 months	Variance 3 months	Variance/ budget % 3 months	Notes
Income (£)						
Grants	505,000	182,000	152,000	(30,000)	(16%)	1
Fee income	58,600	14,650	15,247	597	4%	
Bank interest	2,000	0	10	10	0%	2
Other income	26,000	6,500	9,059	2,559	39%	3
Total Income	591,600	203,150	176,316	(26,834)	(13%)	
Expenditure (£)						
Salaries	262,680	65,670	68,309	(2,639)	(4%)	4
Recruitment costs	4,990	3,000	50	2,950	98%	5
Medical supplies/drugs	254,000	63,500	83,393	(19,893)	(31%)	6
Rent	49,000	24,500	25,790	(1,290)	(5%)	7
Insurance	3,880	3,880	530	3,350	86%	8
Telephone/electric/water	6,030	1,508	1,461	47	3%	
Office costs	6,760	1,690	1,538	152	9%	
Other expenses	4,260	1,065	1,809	(744)	(70%)	9
Total expenditure	591,600	164,813	182,880	(18,067)	(11%)	
Income less expenditure	0	38,337	(6,564)	(44,901)		10

(-) shows more budget than actual for 'income' items, and more actual than budget for 'expenditure'.

Explanatory notes for the budget and actual statement

Note	
1	Slightly more of the annual grant budget is due in this 3 month period. However, one grant of 30,000 did not arrive. We have contacted the donor who will pay us in April.
2	Bank interest is credited in June. The £10 was in compensation for a bank error.
3	Other income from local fundraising was more than expected this quarter.
4	Due to an outbreak of typhoid we paid medical staff overtime to immunise children in three areas of the province.
5	We expected two staff to leave in February, however this did not happen. The 50 shown as an actual figure is an error and will be corrected in April.
6	We have bought medical supplies in advance for the next two months at a discount.
7	We have paid rent as expected. The 1,290 was a deposit which we will get back when we leave at the end of the year.
8	We now pay insurance monthly rather than annually. However, this statement highlighted that we have not paid the public liability insurance premium. We paid this in early April.
9	Other expenses included annual professional subscriptions. These are not due again this year, and so the actual will correct itself through the year.
10	Overall income is 26,834 less than expected (due to not receiving the 30,000 grant), and the expenditure is 18,067 more than expected (mostly due to buying medical supplies in advance). Therefore we are 44,901 less than we thought at this point. We will receive the 30,000 during April (note 1) and we will not now spend money on medical supplies over the next two months (note 6). We have enough money in the bank for this at present, but have arranged a temporary overdraft in case this happens again later in the year.

3. Ask questions and take action

The notes with the budget and actual statement (Figure 1) provide an explanation for some of the differences.

The variance/budget % column shows how important the difference is. As a guide, if this figure is over 10%, or if below 10% and a large amount, it is worth asking for a reason if not explained in the notes.

In this example, the following questions could be raised:

- How certain is all the estimated grant income to come in during the year?
- What does 'other income' include other than fundraising?
- Why was fundraising income more in this quarter? How likely is this to continue at this level over the rest of the year?
- What are the 'use by' dates of the medical supplies/drugs bought in advance?
- What will you do in future to remember to pay insurance premiums when due?

- What does 'other expenses' include other than subscriptions? How well do you control this budget item?
- What will the donors say about under/over budget items?
- Can you afford to cover the delays in receiving funding? Have you produced a cash flow forecast?

In all budgets:

- Ask why each actual figure is different from the budget. Predict what would happen if the current trend continues for the rest of the budget period
- If necessary, reduce costs, cut back on, or expand a planned programme, increase fees or fundraising
- If spending too much or too little, talk with your donor, otherwise the donor may not release all the money promised
- Take no action if the actual figure is temporarily incorrect, but will right itself in the next period, but make sure it does
- Continue monitoring the budget and make sure any action has been effective

Preparing a cash flow forecast

A budget tells you if the money coming in covers the money going out. It does not tell you if you will have enough money at a particular time.

The example in Figure 1 shows that the annual budget income is exactly enough to cover expenditure. However we can see that because one of the grants has not arrived on time, and medical supplies have been bought in advance, we may be temporarily short of money.

A cash flow forecast will show:

- When the money will be received and paid
- Whether there will be a positive or negative bank/cash balance over each month of the period
- If you need to plan to cover a shortfall, or invest a surplus

To compile a cash flow forecast you need to:

1. Use the organisation's budget
2. Decide when each budget item will be received or paid. Some may be received in a single amount (for example a grant), others may be paid equally each month (for example salaries)
3. Write down each item, as shown in Figure 2. Enter each item when you expect it will be received or paid, regardless of when it is due
4. Include the expected bank and cash balance at the beginning of the period as your starting point
5. Calculate the amount for each month by taking:
 - The opening balance for the month
 - Plus the money estimated to come in during the month
 - Less the money estimated to go out during the month

- This equals the balance left at the end of the month (and the opening balance for the next month)
- 6. Improve your cash flow by considering whether any ‘money coming in’ can be received earlier, or any ‘money going out’ can be paid later
- 7. Update the forecast as new information becomes available

Figure 2

Example of a cash flow forecast for the six month period 1 January to 30 June

Western Province Health Centre Cash Flow Forecast

	JAN	FEB	MAR	APR	MAY	JUN	TOTAL
Money coming in (£)							
Grants	50,000	10,000	122,000		5,000	100,000	287,000
Fee income	4,883	4,883	4,883	4,883	4,883	4,885	29,300
Bank interest							0
Other income	2,167	2,167	2,167	2,167	2,167	2,165	13,000
Total money coming in [B]	57,050	17,050	129,050	7,050	12,050	107,050	329,300
Money going out (£)							
Salaries	21,890	21,890	21,890	21,890	21,890	21,890	131,340
Recruitment costs		3,000					3,000
Medical supplies/drugs	50,000	6,750	6,750	50,000	6,750	6,750	127,000
Rent	24,500						24,500
Insurance	3,880						3,880
Telephone/electric/water		1,006	500		1,006	503	3,015
Office costs	563	563	564	563	563	564	3,380
Other expenses	860	310	310	310	310	310	2,410
Total money going out [C]	101,693	33,519	30,014	72,763	30,519	30,017	298,525
Summary (£)							
Opening balance [A]	41,000	(3,643)	(20,112)	78,924	13,211	(5,258)	
Plus total money coming in [B]	57,050	17,050	129,050	7,050	12,050	107,050	
Less total money going out [C]	101,693	33,519	30,014	72,763	30,519	30,017	
Expected closing balance [A+B-C]	(3,643)	(20,112)	78,924	13,211	(5,258)	71,775	

() shows an overdrawn bank balance.

[A] = the amount held at the beginning of each month.

[B] = the monthly total of money coming in.

[C] = the monthly total of money going out.

For a spreadsheet template for a cash flow forecast:

www.johncammack.net/ (click on Resources/Project budgeting)

Producing documents at year end

At the end of the financial year, the 'actual' part of the final budget and actual statement becomes the basis of the annual accounting statements.

Internationally two statements show what has happened during the year:

- **Receipts and payments account**

This shows what has been received and paid, without adjustment for what is outstanding or paid in advance. At the end of the year it will show how much money remains in cash and at the bank. It is relatively simple to prepare but only suitable for small organisations.

- **Income and expenditure account (Income statement)**

A more technical document, which uses the 'actual' information and adjusts it for outstanding items, payments in advance and other items (see Figure 3). The aim is to produce a document which covers twelve months' income and expenditure. It compares like with like, and the account can show whether there is a 'surplus' or 'deficit'.

In the UK larger charities have to produce a Statement of financial activities (SOFA). It uses the same principles but provides more detailed information.

Figure 3

Example of an income and expenditure account with comparative figures for the previous year

Western Province Health Centre Income and Expenditure Account

	Annual Budget Year 2	Annual budget Year 1
Income (£)		
Grants	505,000	384,000
Fee income	48,238	43,938
Bank interest	1,685	1,893
Other income	35,201	41,598
Total Income	590,124	471,429
Expenditure (£)		
Salaries	285,029	228,387
Recruitment costs	2,498	469
Medical supplies/drugs	238,883	166,134
Rent	50,290	49,000
Insurance	3,429	2,950
Telephone/electric/water	6,398	4,148
Office costs	6,209	5,847
Other expenses	5,530	2,936
Total expenditure	598,266	459,871
Excess of income less expenditure – surplus		11,558
Excess of expenditure less income - deficit	(8,142)	

Any surplus will be added to, and deficits deducted from, previous years' surpluses. A summary of this calculation goes into the Balance sheet showing the organisation's overall financial position.

Budgeting checklist

- Involve a range of staff and stakeholders in the planning stage
- Use objectives as the starting point
- Add notes to explain and justify calculations
- Be as realistic as possible
- Prepare well before the start of the period
- Check that your accounting systems can produce donor reports
- Get authorisation for the budget from your organisation and donors
- Communicate budget information to everyone who needs to know
- Produce 'budget and actual statements' quickly after period end
- Add notes to the statement to explain variances
- Monitor regularly, review and take action
- Negotiate with donors as soon as any under/over spending is likely
- Produce a cash flow forecast
- Compare the budget to the income and expenditure account figures

Further reading

John Cammack (2007), *Building capacity through financial management*, Oxford: Oxfam

John Cammack, Tim Foster and Simon Hale (2005), *Financial Management for Emergencies*, www.fme-online.org

John Cammack (2000), *Financial management for development: accounting and finance for the non-specialist in development organisations*, Oxford: INTRAC

Kate Sayer (2007), *A practical guide to financial management*, London: Directory of Social Change

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