Best practice in Management Accounting

Importance of management accounts

A charity will only succeed in meeting its aims if it manages its finances properly. There are a number of aspects to strong financial management and one of these is the regular preparation and review of management accounts. Not everyone on the Board of trustees or Senior Management team will have a strong understanding of management accounts.

Therefore the role of management accounting is crucial for understanding the status of accounting reports, and for strategic level decision making. Other reasons why management accounts should be prepared are as follows;

- Accurate management accounts enables good management – it allows trustees to scrutinise the financial position which aids good governance.
- They are a powerful source of information, actual results can be compared to budgets to establish over / under spends, allowing for an effective review of the forecast for the year.
- They help understand why variances have arisen and if action can be taken to reduce variances.
- They provide details as to whether the level of costs is reasonable and sustainable in relation to income levels.
- It is more likely that the charity will meet its long term strategic plans.

Steps to producing management accounts

The actions in the checklist below should be completed prior to producing a set of management accounts

Checklist

Action required	Completed
Reconciliation of the bank accounts (including credit cards)	Yes/No
Reconciliation of the VAT account	Yes/No
Reconciliation of payroll. If payroll is calculated by an external provider, have the journals for the month been reviewed and signed as authorised?	Yes/No
Calculation of necessary prepayments/accruals. Have the relevant journals been entered onto the finance systems?	Yes/No
Reconciliation of debtors and creditors account. Print aged debtors/aged creditors report	Yes/No
Is the fixed asset register up to date? Has depreciation been calculated for the month and a relevant journal been entered onto the system?	Yes/No
Run a trial balance	Yes/No
Run an income and expenditure report	Yes/No
Run a balance sheet report	Yes/No

Format of management accounts

Many finance packages have an inbuilt feature for preparing monthly management accounts and this should be utilised to make the process as automated as possible.

As a minimum, management accounts should include an income and expenditure account, balance sheet and cash flow and commentary explaining significant variances. It is important to note there is no prescribed format of management accounts, data should be presented in a way that works for the entity and users of the management accounts. Information should be presented in such a way that it enables effective oversight.

Income and expenditure account should include:

- budget for the month just ended against actual results for the month, and variance (value and percentage)
- budget for the year to date against actual results to date, and variance (value and percentage)
- budget for the full year against latest forecast outturn for full year, and variance (value and percentage)
- a supporting narrative which adequately explains the reasons for any significant variances from the budget

Balance sheet - areas to review:

- debtors – this figure should represent monies due to the charity but not yet received. Ensure that a separate "aged debtor" analysis of this figure is provided and that appropriate action is being taken to pursue significant overdue amounts
- cash at bank - check that the actual cash at bank physical balance is not overdrawn. If it is overdrawn, ensure it is within agreed overdraft limits.
- creditors and accruals – these should include invoices received and payable plus commitments made where the invoice has not yet been received.
- net current assets (current assets minus current liabilities) – check that these are positive. A negative balance is indicative of potential cash flow problems
- pension scheme liabilities – if you have a defined pension scheme, the pension scheme actuary should be asked for a statement of liabilities each year when the annual accounts are being produced. Ensure that the impact of any change (for example, a revised monthly pension contribution rate) is reflected in the income and expenditure budget. Since pension costs are outside the control of the entity, it may be better to consider excluding the overall liability from management accounts.

Cashflow Statement:

A cashflow statement can be the most difficult part of producing management accounts, but it is an important tool in understanding where cash is being spent, whether the trust has the potential to run out of cash during the year and identifying any months in which the cash balance could be low.

Distribution of management accounts

Consideration should be given to how often management accounts are prepared and to whom they are circulated.

If the charity is in a financially stable position with no going concern issues with activities remaining similar, then best practice would be to circulate management accounts on a quarterly basis or to coincide with trustees' meetings.

However, if there is a significant project in progress, a number of restricted funds or cashflow issues then monthly management accounts would be pertinent.

Management accounts should be issued to heads of departments and those individuals who are included in making key decisions for the charity. In addition they should be included in the papers for trustees.

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