

PROBLEMS OF MAINTAINING ADEQUATE ACCOUNTING RECORDS FOR A NON-PROFIT ORGANIZATION IN SUB-SAHARAN AFRICA

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ABSTRACT

This paper looks at the accounting challenges faced by a small-scale non-profit organization operating in sub-Saharan Africa. We will look at the case of Enright Flight Ministries, Inc. a 501(c)3 non-profit organization based in Florida that carries out evangelical and humanitarian aid projects in Zambia. Building upon field interviews with administrative staff and project managers, we analyze the various problems facing the organization in maintaining adequate accounting records. After looking at both external and internal problems, we investigate the solutions employed by Enright Flight Ministries to maintain the integrity of accounting systems to derive best practices for the small-scale international non-profit organization.

JEL: M41, M42

KEYWORDS: Accounting Records, Non-profit, Statements

INTRODUCTION

Issue proliferation in the development sphere has given rise to thousands of non-governmental organizations (NGOs) aimed at improving lives in the world's poorest regions. No matter if an NGO seeks to address gender equality or environmental degradation, each requires a stringent and sound accounting system if the organization is going to be seen as legitimate and transparent. Designing such an organizational accounting system that stands up to the challenges of working in sub-Saharan Africa is difficult and costly for any entity, especially a small-scale non-profit organization.

This analysis seeks to identify some of the challenges of maintaining adequate accounting records in sub-Saharan Africa as well as to propose solutions for overcoming these difficulties. This analysis will focus upon the case of Enright Flight Ministries, Inc. (EFM), a 501(c)3 non-profit corporation which aims to promote Christian evangelism and economic development in Central Africa. Through the study of EFM activities, we intend to derive a set of best practices to assist small-scale aid organizations operating in similar environments.

Founded in 1992, EFM was designed to be a vehicle through which retired missionaries could continue their work in both Zambia and the Democratic Republic of the Congo with the support of private individuals across the United States. EFM operates out of Daytona Beach, Florida where two non-paid administrators reside. The third administrator is based in Zambia. The Chief Operating Officer (COO) is also stationed in Zambia to oversee all daily operations and the 7 additional EFM employees engaged in project support and development. In addition to these individuals, the various field projects employ approximately 150 local Zambians at any given time.

The business investments undertaken by EFM are designed to provide goods, services, and training to local populations. Revenues generated from the project portfolio are used to supplement private donations in the support of continued business investment, church building activities, and an intensive annual training program for pastors. The major project activities are focused on 6 distinct areas: woodworking

factory, aloe vera production, banana production, organic honey apiaries, tilapia fisheries, and poultry/beef production.

This analysis contributes to the existing body of literature by identifying the specific external and internal challenges faced by a non-profit organization in the implementation of an adequate and transparent accounting system. Where other studies have identified the challenges to accounting systems at a national or regional level, we have found few references to specific cases in the literature. Our analysis also extends the literature by addressing potential solutions to accounting problems that can be implemented at the managerial level to allow organizations to more effectively carry out adequate accounting practices in difficult environments.

We begin our analysis by looking at the relevant body of financial research which addresses the maintenance of adequate accounting records in developing countries. This is followed by a discussion of the value which accounting records provide to EFM. We then draw on field interviews with the administrators of EFM and project managers to identify external and internal challenges to good accounting practices and the solutions which have been tested by EFM. Finally our conclusions seek to extend the solutions employed by EFM to other NGOs that may be operating in similar circumstances.

LITERATURE REVIEW

Research focusing on the challenges of maintaining adequate accounting records in sub-Saharan Africa, and developing countries in general, constitutes a relatively new area of work in the field of international finance. Because businesses in developing countries have historically represented such a small part of the global economy, the study and application of management accounting principles in these regions have been “marginalized” in favor of case studies from developed countries (Alawattage, 2007). This body of literature widely focuses on three main issues: the need for continued development of accountancy in Africa, the challenges to implementing a Western accounting regime, and the contributions of good accountancy to greater development goals.

Organizations operating in sub-Saharan Africa are at a significant disadvantage for maintaining adequate accounting records due to a thin market of accountancy skills and talent throughout the region. Koth (1992) draws on survey reports from the UN Center on Transnational Corporations to describe “a scarcity of fully qualified accountants” and “inadequate accountancy training.” Of 37 countries surveyed in the region, only 3 had more than 1000 qualified accountants (Koth, 1992). Koth finds that there needs to be greater general attention to the training of accountants within sub-Saharan Africa and less reliance on external talent if the field is to grow. Not only does this lack of accounting talent show the need for continued growth, but it also presents a challenge to Western auditing practices which can require many individuals with accountancy skills at different levels of this business. Johnson (1992) also cites low development in accountancy for fostering “informal ways of getting things done” that are currently much more important to organizations in Africa than ensuring adherence to proper documentation and standards.

Of particular emphasis is the identification of cultural and anthropological barriers which can prevent the implementation of adequate accounting procedures. Johnson (1992) draws upon her experiences with the Bank of Sierra Leon to discuss auditing as an “alien phenomenon” throughout much of Africa. Many African cultures discourage “probing” questions and demand that elders, and their business affairs, are respected by all (Johnson, 1992). This presents a unique problem for auditors who, by their very job description, are charged with asking questions to certify accurate accounting records. Societies in sub-Saharan Africa, especially true for Zambia and the operations of Enright Flight Ministries are organized around tribal and familial structures. Johnson recognizes that these close relationships can compromise the objectivity of an auditor or accountant and make it difficult to enforce adequate accounting standards.

Improved accounting practices are directly related to wider development goals. Chung (2012) concludes that basic education in accounting principles and standards are beneficial at the rural level because it would impart skills such as budgeting to local populations that could result in improved savings for future agricultural investment, greater use of financial services, etc. Additionally, Chung (2012) suggests benefits for local participation in civil society because individuals are more apt to participate in political, social, and religious discussions of financial management if there is a common set of accounting principles and standards that can be understood by the general public.

Taking cues from the relevant literature, this study contributes to our understanding by analyzing the challenges faced by EFM to maintain adequate accounting records in daily operations. Furthermore, this analysis recommends solutions to these challenges and best practices that can contribute to the development of strong and reliable accounting standards across sub-Saharan Africa.

THE NEED FOR GOOD ACCOUNTING RECORDS

Maintaining adequate accounting records is an imperative for any business organization that aims to be profitable, accountable, transparent, and legitimate. For most project managers, having solid and dependable information is the key to profitability. Good accounting practices ensure that the managers are provided with current records about the state of operations so that the correct business decisions can be made. Because of the diverse portfolio of Enright Flight Ministries (EFM) investments, each business venture is responsible for maintaining complete accounting records under the supervision of a project manager. On a recurring basis, EFM conducts internal audits of the records to ensure that good accounting practices are in effect and are reported to the corporation administrators.

EFM also has a moral responsibility to the private donors who support the organization to ensure that accounting procedures throughout the organization are strong and accurate. Recent years have seen increased media attention to non-profit organizations that maintain obscene overhead costs or cannot account for funds received. As donors become savvier, non-profits have begun to provide more information to donors in an effort to increase levels of accountability and transparency. To this end, EFM ensures that complete information regarding any donation can be provided to an individual upon request.

Finally, the strongest reason to devote scarce resources to the preparation of sound financial statements derives from the legal and regulatory obligations of the corporation to government. In the case of EFM, the fact that the organization is incorporated in Florida and is funded through private individuals across the U.S. necessitates that EFM file an annual US Tax Return with the Internal Revenue Service. Because EFM conducts business activities internationally, there are also regulatory requirements that must be met in Zambia. The Zambian institution charged with collecting taxes and auditing the financial statements of individuals and corporations is the Zambian Revenue Authority (ZRA). The basic requirements imposed by the ZRA are as follows. A corporation is subject to a turnover tax that is divided into two levels. For a "small" corporation with less than \$40,000 in turnover the tax rate is 3% of net revenue. For a "large" corporation with more than \$40,000 in turnover the tax rate is 15% in the agricultural sector and 35% for everything else. The only caveat is that large corporations are permitted to deduct VAT (value added tax) where small corporations are not.

Reporting requirements also differ on the size of the corporation. For a small corporation you are required to prepare monthly financial statements to be filed with an accountant. The main purpose of this law is to ensure that businesses are paying into pension programs for employees. Large corporations are required to file quarterly financial statements and tax payments based upon annual projections. The ZRA requires that each corporation be audited annually by an external accountant who serves as the liaison between the business and the ZRA. All financial records (receipt books, payroll records, etc.) are required to be stored

at an external accountant's office. Only after the ZRA conducts an audit with the business accountant is the ZRA legally allowed to proceed to the business site to conduct a field audit.

PROBLEMS

As with any international non-profit organization, Enright Flight Ministries (EFM) has faced a significant number of challenges in maintaining adequate accounting systems that meet the needs of project managers, donors, and governments. We choose to look at these problems in two groups: external and internal challenges.

External Challenges

One of the biggest challenges to EFM has been in understanding the often incomprehensible regulatory requirements imposed by the ZRA. As a former British colony, the ZRA has inherited a legacy of bureaucracy that makes it difficult to navigate the filing of annual paperwork without incurring major fines. Even with the services of external accountants there is a serious problem of information transfer between the ZRA and the businesses and accountants who follow their guidelines. In one such instance the accountants who conducted the audit felt that there was no need to file a quarterly report since there was no profit on which to pay taxes. During the ZRA audit the accountant's mistake resulted in a hefty fine, further emphasizing the steep learning curve.

EFM must also cope with the monetary uncertainty of conducting business in sub-Saharan Africa. Zambia operates primarily as a cash-based economy, especially in the small scale agricultural sales of EFM business activities. The largest bill presently in circulation is a 50,000 kwacha note which is valued at roughly \$10 USD. Such small denominations mean that EFM is forced to account for massive amounts of cash that leave a large amount of room for accounting errors. Recent reports in Zambian periodicals also suggest that a major revaluation of the currency will occur in mid 2012 to cut 3 zeroes from each bill. This means that the 50,000 kwacha note will become a 50 kwacha note, and in the process make it very difficult to maintain accurate accounting during the change.

Historical underdevelopment also contributes to the difficulty in maintaining strong accounting practices because high volumes of business are a relatively new phenomenon. In the past two decades, huge investment in Zambia's mining sector from Asian and European markets have helped to spur a national growth rate in excess of 6%. Rising incomes and an emerging middle class have boosted sales across all sectors of the economy, and both businesses and their accountants are dealing with significantly larger operations than in the past. EFM has found that historically smaller businesses have made it difficult to find qualified accounting talent to handle larger volume corporations. As noted before, mistakes on the part of the accountant can result in fines and penalties that are imposed with the ZRA. This combination has resulted in significant search costs for EFM in securing a permanent accountant.

Zambia's historically "thin" markets for goods and services have produced an underdeveloped banking sector that is struggling to cope with new volumes of financial transactions. In the past year, several of the EFM businesses were required to open new corporate accounts at local financial institutions to facilitate new grants and expanded business activities. From these new accounts, fastest time to completion was 6 weeks and the slowest was over 5 months due to a labyrinthine bureaucracy. There is also a significant challenge to EFM accounting records in the transfer of funds from U.S. banking institutions to Zambia. Fees are imposed in the U.S. when funds are sent and in Zambia when funds are collected, representing a significant cost in the management of multiple separate accounts.

Internal Challenges

EFM faces the constant obstacle of balancing the goals of a humanitarian organization with those of a business venture. Managers must constantly evaluate their business decisions to ensure that ventures are economically viable, but that they are also contributing to the overall well-being of the community. These forces are best demonstrated in the wood-shop venture. Manufacturing high-end custom doors, tables, and chairs for sale to private individuals and businesses in northern Zambia is the main goal of the venture and brings in a healthy profit for the business. What happens when another aid activity, say a women's sewing class, needs a table to work on? Should the manager provide a quote that includes a normal markup or should the product be produced for the mission at cost? Under which business is this transaction accounted for? These situations are common in the daily activities of EFM ventures.

Accounting is also made more difficult for EFM due to the limitations of human capital. Because of EFM operations in rural Zambia, agricultural laborers often have very little formal schooling or training in math which can result in significant difficulties in regards to selling, pricing, and inventories. One recent example is in the averaging of weights for the chicken business. The selling price is based on the average weight of a random sample of 10 chickens that are taken from each batch of 500. Every day this sampling procedure is repeated and results are reported to managers. In February 2012, the average weight reported was consistently greater than the weight of any individual chicken. When investigated, it was revealed that the workers conducting the sampling were not aware of how to conduct an average, even after two years of agricultural college.

Besides worker skills, employee character has been a constant problem for EFM operations in Zambia. Managers must be vigilant in maintaining accounting checks in inventory and sales because theft has been a huge problem. In the banana venture this year, there was widespread incidence of theft among the employees charged with sorting the bananas into quality grades of "A", "B", "C", and "no grade". What the graders were doing was assigning high-quality "A" grade bananas into "no grade" crates. Because the low-quality "no grade" bananas are unfit for sale, managers often give them to the employees at the end of the day. In this manner, the employees were smuggling high-quality bananas home which they were then able to sell for a profit in local produce markets. Other instances of theft have included employees forging receipts, stealing inventory outright, lying about cash advances, and the shorting of change to customers. It requires a significant amount of time and resources for the organization to monitor financial records to both find and correct for these discrepancies. Employee compensation also presents a challenge for EFM for several reasons. First, Zambian law through the ZRA only allows for the payment of employees on a monthly basis. This requires maintaining huge amounts of cash on hand at the end of each month, and can often delay project activities due to a cash shortage. Second, the businesses struggle with meeting employee needs. This goes back to the idea of balancing for-profit business strategies with the realities of working for a non-profit humanitarian mission. Situations arise among the employees of each business (emergencies, illness, school fees, etc.) where a cash advance is needed. Unfortunately, in sub-Saharan Africa these issues arise on an almost weekly basis creating a nightmare of accounting records because most employee pay is generally already advanced before the end of the month. Finally, because EFM deals almost exclusively in agricultural products, many workers ask to receive a portion of their pay in the product produced. This practice also produces additional paperwork that convolutes the accounting records.

EFM has also had difficulty maintaining field managers over a longer period. This has created significant continuity issues with internal accounting procedures whenever there is the departure by a major staff member. Because each venture is compartmentalized in operations, there has been no back-up solution or succession plan in place for lower level managers. The case in point for EFM has been the wood-shop which has gone through a series of 4 managers in under 10 years. Each shift has left the finances in disarray and caused EFM to bear greater costs when preparing the venture for a replacement manager.

SOLUTIONS

For Enright Flight Ministries (EFM), there are no simple solutions to the external challenges to maintaining adequate accounting records in sub-Saharan Africa but there are some significant steps that can be taken to mitigate external risk and correct the internal problems. One major step is to use the services of two independent accountants in Zambia. An internal accountant who conducts audits and prepares reports for project managers has now been hired by EFM. This internal accountant is the first barrier against the often incomprehensible laws and accounting mistakes that can result in significant fines. When the internal accountant runs up against an issue that is not fully understood, it provides EFM with advance warning to determine the appropriate actions and paperwork needed to rectify a problem before it reaches the ZRA. This is where the services of the second accountant come into play. The second accountant for EFM works in an external office, and the project managers use reports from the internal audits in their meetings here. The external accountant serves as an important second opinion and is the liaison between EFM and the ZRA. Having two separate accountants, the internal and external accountant, helps to minimize the risk of misunderstandings and fines and is necessary to create a central record and institutional memory of good accounting practices that can be maintained even with the departure of key EFM staff members or even an accountant. Having these two individuals working for EFM will also help to develop the accounting skills necessary to handle the ever increasing quantities of business transactions.

Until Zambia improves the state of banking and finance, large amounts of cash and the fees associated with cash transfers from the U.S. will remain an operating reality for EFM activities. This is why a significant second step for EFM has been maintaining the services of an accounting firm in the U.S. as a means to adequately account for all funds received from U.S. donors and to prepare the annual U.S. Tax Return for EFM. Having a U.S. based accountant is imperative to provide financial information to interested donors and to facilitate the cash transfers to Zambia in the lowest cost manner. EFM attempts to send money in the fewest number of transactions possible to minimize the fees incurred at the bank and maximize the funds available for project implementation. At the same time, holding most of EFM resources in U.S. dollars is a sound strategy that allows the non-profit administrators to mitigate some of the risks and uncertainty associated with the Zambian kwacha. EFM has moved the responsibility for cash accounting onto the managers of each separate venture. At the close of each business day, each manager must reconcile inventory, sales, and cash receipts for review by the internal accountant the next morning. When a discrepancy arises, the internal accountant notifies the relevant manager, who now has the ability to investigate the problem on the next business day. In addition to managing the large amounts of currency on hand, this process helps to safeguard against the problem of employee theft.

In regards to employee skills, EFM has instituted numerous training programs to help boost the language and business abilities of employees to prevent accounting or business errors that arise from miscommunication and human error. One of the most popular efforts has been the formation of English classes for beginners and advanced speakers. These classes are open to employees of all EFM ventures and occur twice each week. Additional training classes are conducted weekly by managers of the individual ventures. Every employee of that venture is required to attend, and they spend time teaching each worker how every aspect of the business operates. These sessions are useful for teaching the skills required for each employee position (mathematical, technical, accounting, etc.) and serve as an important mechanism for building a relationship of trust and accountability between the managers and the employees. EFM feels that training sessions are the best vehicle to combat failings in the character of the employees and lower the incidence of theft. If the organization is transparent and makes an effort to supply full information to the employees they will be less likely to try to steal because they feel like an integral part of the business activities. Fostering ideas of community ownership, teamwork, and

camaraderie are central to this effort and supplemented by external activities such as employee dinners, picnics, and celebrations.

EFM has also come up with a novel means to address the accounting issue of the single pay period per month. For several of the businesses, every employee now receives a portion of their pay, about 30%, in the form of a cash advance during the second week of each month. This allows the ventures to meet the needs of employee requests for advances while also reducing the amount of cash that must be on hand for payroll at the end of the month. This practice falls entirely in line with Zambian law for employee compensation and has been a large success among workers. It has also streamlined the accounting process because there is not an individual cash advance for each employee, but a standard amount across the board. Also streamlining the process of paying employees in agricultural products has been a new EFM policy where employees are allowed to receive a fixed amount of their salary in the form of finished product. This practice only extends to employees of the relevant venture. For example, a worker in the chicken business can receive part of a salary in the form of 3 chickens but cannot receive part of the salary in the form of fish. This has cut down on confusion (and discord) that arises between the separate ventures, and has gone a long way to improving the clarity of EFM accounting records.

CONCLUSION

Maintaining adequate accounting records requires the significant investment of time and resources for any organization. For Enright Flight Ministries, Inc. (EFM) this responsibility is especially important in an effort to be transparent for private donors, meet the legal obligations of the various countries where operations take place, and to ensure that program funds are used to meet the humanitarian goals of the organization. EFM faces a myriad of challenges to maintaining strong accounting records. Cash based economies, currency uncertainty, and historical under-development, are the biggest external problems. Internal problems include balancing business goals with humanitarian goals, limited employee abilities, and payroll management. EFM manages external challenges through the use of a two accountant system in Zambia and the services of a U.S. based accountant to mitigate the risks associated with international operations and foreign currencies. Internally, the compartmentalization of business ventures under the leadership of project managers has led to a more horizontal business structure that allows for greater monitoring and accountability within the business. Additionally, significant investment in employee training and knowledge sharing are used to combat the prevalence of poor character and low education among workers.

From this case we believe the most significant lessons for small-scale NGO's can be derived from the implementation of a system of checks and balances that include accountants in each country of operations. Too often, the managers of non-profit NGO's are so involved in the implementation of projects or other humanitarian efforts that they are not equipped with the time or knowledge to fully understand the nuances of accounting law applicable in the region. Having accountants in both the U.S. and Zambia allow EFM to satisfy responsibilities to donors and governments in a professional and timely manner, with minimal waste of scarce aid dollars. This system extends into the system of checks permitted by the close interactions of project managers with an internal accountant who works in the field. This system has provided EFM managers with extremely reliable financial reports that have been invaluable in the preparation of annual budgets and sales projections to solicit new donors. Additionally, it prevents accounting errors in one business venture from permeating through the entire organization because the internal accountant has the opportunity to correct bad practices at an early stage. The key to maintaining adequate accounting records in sub-Saharan Africa is to design an accounting system that is able to efficiently adapt to the harsh realities of operating in the developing world.

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