

Financial guidance for grant holders: budget classification and budget management

Introduction

This document presents financial guidelines for UK Aid Match. It covers the classification system of UK Aid Match budgets, and the methodologies used in calculating the expenditure of grants.

Structure of the budget

Under UK Aid Match, budgets are split into standardised budget headings / subheadings. These are organised in two categories:

1. Project activities: defined as costs which are linked to the achievement of the project outputs. Activities are what the project team do to achieve the aims of the project.
2. Project costs: defined as project running costs and costs that cut across project activities. These costs are not so easily defined or tracked under one activity and contribute to the delivery of the whole project. This covers standard budget headings of staff costs, capital expenditure, other administrative expenditure, monitoring evaluation and lesson learning.

UK Aid Match budget headings

This section covers basic guidance on the classification of expenditure between the standard budget headings.

Capital Expenditure

The grant holder must budget for all items of capital expenditure to be funded under the project. Recognition of capital, including de minimis limits should be in line with the grant holders own finance manual but remain subject to the requirements of reporting an inventory, as set out below. For ease of asset disposal at project end each asset should be wholly funded by either FCDCO or match.

Grant holders must report on capital expenditure in the year in which cash is exchanged. The cost of the transaction should not be spread over the lifetime of the project, i.e. the depreciation of an asset should not be included in reporting.

Management of project assets

Foreign, Commonwealth & Development Office (FCDO) considers any equipment and / or supplies purchased in part or fully from FCDO funds as project assets if they have a useful life of more than one year; and either:

1. the purchase price or development cost of the asset is in excess of £500 or equivalent in local currency; or
2. is a group of lower value items (e.g. pharmaceutical products, food, relief packs, etc) where the combined value is in excess of £500 or equivalent in local currency; or
3. can be considered an attractive item regardless of cost (for example mobile phones, cameras, laptops, tablets, satellite phones)

As per the FCDO Accountable Grant Arrangement, ultimate ownership of the inventory of assets will remain with FCDO and any ownership, transfer, or asset disposal is otherwise agreed in writing by FCDO, normally at the end of the grant. It should not be assumed that assets will remain with the lead grant holder or local implementing partners after project completion, so grant holders should plan for replacement of assets after the end of the grant if this will impact on the continuation of the critical project activities. We encourage large value assets to be purchased from a component of the budget not funded by UK aid and avoid splitting the costs of such items between different funding sources.

Reporting on the inventory is completed once per year.

Project Activities

The Project Activities budget heading is expected to cover all recurrent project delivery expenditure unrelated to administrative costs, staff costs, or monitoring and evaluation.

It would be expected that all project activities included within the project plan and logframe have corresponding costs included within the budget in the period the activity is due to take place.

Staff Costs

Staff costs are recorded in a separate section of the UK Aid Match budget. Staff costs will typically include expenditure incurred for:

- Staff associated with project activities
- Staff associated with administrative costs, unless judged to be inseparable from the overheads

- Payments to consultants as well as staff members
- Employment costs not included in salaries (these may include payroll taxes, pensions, staff bonuses as dictated by contract). These additional costs are expected to be appropriate to the normal practice of the country of implementation.

To allow for verification of amounts in all cases it is required that timesheets will be completed, and formal payslips will be produced.

Budgeting for staff costs is based on percentage FTEs (full-time equivalents), so it is important that the grant holder collects sufficient information to demonstrate compliance against their UK Aid budget.

Grant holders do have the flexibility to adjust pay if it is within their budget or the flexibilities identified in section 5.2 of this guidance. However, where salaries are significantly adjusted upwards, and charged to the UK Aid Match budget, there should always be a clear justification for doing so, and the grant holder should be prepared to demonstrate that the change was necessary to achieve value for money in the context of the project.

Other admin costs

FCDO recognises the need for grant holders to support any project through head office administration. These costs are accumulated under the heading of 'Other Admin Costs'.

'Other admin costs' is intended to cover an appropriate and justifiable apportionment of the grant holder's (and any implementing partner's) administrative costs expended in support of the grant, where these costs are not covered by the other budget classifications.

These costs should be minimised in line with FCDO's approach to value for money. UK Aid Match grant holders should consider where cost savings could be made through sharing administrative costs across projects.

The fund manager is aware that most grant holders will already have their own internal guidance on the calculation of administrative support costs and, as far as is appropriate, are content for this to be used in the calculation of administration costs under UK aid.

For the conveniences of grant holders however this guidance sets out some good practice principles which must be adhered to, and recommended methodologies which are cleared as appropriate to UK Aid Match.

- Expensed costs must be based on the actual expenditure
- Any costs charged must be evidenced by supporting documentation
- Staff time allocation charges should be supportable by time sheets
- The recognition of costs should follow the standard reporting principles of all other types of expense regarding the cash basis of accounting and the timing of reporting
- These principles should apply to both grant holder and any implementing partners.

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Note that the principles above preclude certain methodologies for charging of administrative costs. In particular, it is not acceptable for grant holders to change a fixed rate for administration (e.g. a fixed figure of £100,000) or to charge a flat rate based on the size of the grant (e.g. 10% of the total granted). In some cases, grant holders have spread costs for highly predictable charges across the reporting year (e.g. in the case of audit charges) which is also not accepted.

Recommended and approved methodologies to apply to UK Aid Match grants are as follows:

- Calculation based on the actual observed levels of effort by project
- Calculation based on the total actual administrative costs apportioned across the project portfolio

Monitoring, Evaluation and Lesson Learning

External evaluation is an important aspect of any project and we expect to see a separate budget line for this. There is no specific ceiling for the cost of the evaluation, but the assessor will consider if the allocation is appropriate for the proposed project.

Monitoring and Evaluation (M&E) after project end

By default, the budgeting and claims process for M&E costs follows the same rule as for all other expenses under UK Aid Match.

It is good practice for grant holders to pay consultants after all inputs have been completed and the final product can be approved, but in the case of M&E this timing means that payment will often take place after the project has closed.

Whilst in general expenditure incurred after the project has ended cannot be claimed, there is an exception under M&E for the project specific audit and external evaluation costs. Where an external evaluation is budgeted in the final quarter of the project, a final payment for consultant fees might be payable upon completion of the evaluation, rather than paid for before the assignment is complete and the 'product / evaluation report' is received by the grant holder. Providing the expenditure is incurred before the project end date, if invoices for these particular costs are received after the project end date you can submit a claim as long as it's within 3 months of project end.

Staff and admin costs for conducting MEL activities after the end date of the project are not eligible – whether for routine MEL, the project completion report or supporting with an external evaluation. This also applies for staff time and other costs linked with completion of the project completion report which is due up to three months after the end date of the project. Any costs relating to the PCR must be incurred either before the end date of the project OR with match funds.

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Items which may not be claimed

Principles to follow:

- By default, transactions are expected to be 100% for the purposes of the UK Aid Match grant. In some cases, (especially when related to admin costs) cost sharing is allowed and encouraged, but this should not lead to UK Aid Match paying disproportionately for a shared cost
- Inflation must not be included as a stand-alone cost in a separate budget line
- Large capital expenditures are not envisaged under UK Aid Match.

All items of expenditure must confirm to the principles above and be allowable within the agreed budget. There has previously been some uncertainty in the application of the rules in relation to specific items of expenditure. The following list are types of expenditure NOT allowable within UK Aid Match. This list is non-exhaustive but covers some of the common points of confusion:

- Lobbying UK government, i.e. using grant funds to fund lobbying to influence or attempt to influence Parliament, UK government or political activity; or attempting to influence legislative or regulatory action
- Using grant funds to directly enable one part of UK government to challenge another on topics unrelated to the agreed purpose of the grant
- Using grant funding to petition for additional funding
- Expenses such as for entertaining, specifically aimed at exerting undue influence to change UK government policy
- VAT reclaimable by the grant recipient from HMRC
- Payments for activities of a political or exclusively religious nature
- Gifts
- Statutory fines, criminal fines or penalties
- Payments for works or activities which the grant recipient, or any member of their Partnership has a statutory duty to undertake, or that are fully funded by other sources
- Severance pay, payments for unfair dismissal or other compensation
- Land purchase
- Cars
- Major capital expenditure cannot be supported as the primary focus of the proposed initiative
- Contingency / unforeseen costs arising during the project implementation should not be included as a separate item in the budget
- Depreciation is an accruals accounting concept and should not be included

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- Debt Repayment, bad debts to related parties, or interest payments or service charge payments for finance leases.

In some cases, it may be possible for a budget line including capital expenditure (for example the purchase of a car) to be funded through a project's match-funding rather than by FCDO.

The funding amount is to be used solely for costs included as part of the budget agreed with FCDO for the delivery of the outputs and outcomes set out in this Arrangement. More specifically FCDO funds cannot be used for the above activities

The above list is not exhaustive and not intended as a universal list of what is permissible or otherwise under this arrangement.

Budget Management

Good practice

All grant holders are expected to closely monitor their budget against the project plan and logframe. FCDO allows some degree of flexibility within budgets, but the expectation is that accurate planning and forecasting should occur upfront and that the need for revisions to the budget will be by exception only and will in most cases be anticipated in advance by the grant holder.

As FCDO has its own budgetary restrictions, the quality of forecasting on all grants is paramount and repeated high variance against forecast is seen as a consequence of weak financial management.

UK Aid Match does not attempt to dictate the planning system of each grant holder; however, all organisations should consider the below points of best practice when designing their systems:

- Collaborative. Management of the budget is only effective when it is a collaboration of the finance section and technical delivery sections. Financial forecasts should be activity based and consider the real-world actions taking place, with an awareness of the local context, rather than a simple apportionment of budget across months
- Forward looking. The fund manager should be made aware of the need to adjust budgets as far in advance as possible. If grant holders report budget variances only during annual reviews, then they are at risk of the fund manager and FCDO rejecting the budget adjustment and denying any disbursement of funds not in the agreed budget
- Regularly updated. It is recommended that forecasts and plans are reviewed at least monthly and accurate up to date financial forecasts are reported to the fund manager in every funding claim

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- Realistic. There is an inevitable tendency to over-promise on the delivery of projects. Effective planning should attempt to control this and set a project plan linked to a budget that is ambitious but achievable.

Budget flexibility

In most cases grant holders are expected to operate within the constraints of their project budget, and where adjustments to the agreed budget are required approval must be sought through the fund manager. However, to avoid the need for approval of many small changes there is some flexibility in budgets for adjustments which can be made without approval from the fund manager. This flexibility is set out in the grant arrangements:

During the course of any financial year, up to 10% of the value of a budget subheading (subtotal) can be transferred between the budget lines (within the subheading) without Fund Manager approval. Any proposed virement within the budget subheading amounting to over 10%, or any virement between budget subheadings, must be approved in advance and in writing by the Fund Manager before the budget is changed.

The paragraph above is best read alongside the structure of the budget set out in section 2. The allowed flexibility is to move budgeted funds from one budget line to another within a single budget subheading. This flexibility does not allow movement between the subheadings or allow the creation/deletion of budget lines themselves.

Any variance in expenditure outside the allowed flexibility above will require a formal budget revision in line with the process below.

Budget revision

Where budget variance in a given year is required which is outside of the above flexibility grant holders must formally request Prior Approval and Budget Revision (and if necessary, a revised logframe). This will be the case when any one of the following flexibilities is required:

- Budget lines change by more than 10% of the value of the subheading
- Any reallocation from one sub heading to another
- Budget line going to £0
- New budget line

Grant holders should inform the fund manager as soon as it appears likely that there will be a variance of the budget which requires a budget revision. Grant holders must submit a Budget Revision according to the standard template which will be provided by the fund manager, this template requires the grant holder to state the original budget, revisions, and the revised budget alongside each other. Grant holders are also required to provide an explanation of any budget lines which are being revised and justify the reasons for the change. When the

requested budget changes have an impact on project outputs and activities, you must also submit a revised logframe.

If the fund manager approves the revised budget, then the grant holder will also be issued a revised grant arrangement. Grant holders are responsible for signing and returning the grant arrangement within 30 days of receipt. Until this has been received by the fund manager then grant holders are not permitted to report or claim against the revised budget.

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