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## 7. Revolving fund administration

### **ANNUAL WORKPLAN AND LENDING PROGRAMME BUDGET**

Once sufficient experience has been acquired through operation of the loan programme, future plans should be adjusted to reflect loan demand and repayment performance of borrowers. If initial demand for credit has been lower than projected, a reduction in lending in the following year's budget would be normal. If demand for loans is higher than expected, upward revisions should be sought for the budget which will take two to three months. Requests will be based on projections rather than end-of-year figures; this is another reason for maintaining project accounts up to date and at the project site so that management can always use the most recent information.

Loan recovery is an important resource for revolving funds. Shortfalls can only be dealt with by reducing the lending programme, seeking additional funds or reallocating funds from other budget items. Loan recovery begins immediately after the first loans are made. At all stages of the lending programme, but particularly when it starts, loan recovery must be monitored closely. Appropriate action must take place as soon as any undesirable trends are observed. These adjustments should be reflected in the workplan for future years and in budgets for supervisory staff, collection staff or agencies and for legal services.

Adjustments to the workplan which reflect increased efforts in advertising the loan programme and credit education campaigns for prospective borrowers should be made.

## **ACCOUNTING: PROCEDURES FOR MAKING EFFECTIVE USE OF LOAN LEDGERS, INVOICES, VOUCHERS**

In revolving loan funds run as part of a fisheries project, a separate bank account must be set up for the revolving fund. It must not be operated from the project imprest account. The fund account should only be used for loans, including funds for equipment supplied to borrowers in kind, and for loan repayments. General administrative procedures for running the fund account and the procurement of equipment to be supplied in kind are the same as those for administration of FAO project income accounts and the procurement of project equipment. All disbursements from the account must be made by cheque signed by two officers. The project manager should decide with the counterpart agencies the signatories to the account, after consulting the FAO Representative and the operating unit at FAO headquarters. Deposits should be possible for any project staff. Deposits in cash can be accepted, and should be accompanied by a list of amounts paid against individual loans, the total and the block-printed name and the signature of the depositor.

The accounting system for the revolving fund should fulfil a number of functions:

- Maintain an accurate and up-to-date record of the status of individual loans
- Provide data for use by management in programme operations and planning.
- Provide data for the monitoring and evaluation system which allows programme assessment.
- Provide an effective audit base which meets the needs of both internal and external audits.
- Provide the financial and audit reports required by donor agencies and national banking legislation.
- Provide a basis for determining credit costs and risks.
- Keep records required by the courts to ensure legal enforcement of loan agreements, including the ability to produce legible photocopies of appropriate records which are acceptable in court.

**Manual systems.** Accounts should be kept at branch or project level and kept continuously up to date. Disbursements and payments should be posted the day that they are made, so that the bank always has a clear record of what is due on an individual loan. All items delivered in kind should be costed at the time that they are supplied to the borrower. The borrower should be informed by the time of delivery of the cost of the item and the bank's copy of the receipt accepting delivery should constitute a legally binding contract to pay the amount stipulated on the receipt; this amount should be entered immediately into the individual loan accounts. All project inputs supplied in kind should be costed immediately so that the borrower always knows its cost. Ledgers should be of a size which photocopies easily. All entries should be in black ink, to ensure a durable record and to facilitate photocopying. Ledgers should be balanced monthly. A double entry accounting system should be used. Generally accepted accounting principles should be followed; any national rules which deviate from these principles should be reported in the periodic audits.

**Computerized accounting systems.** Many banks in developing countries have already computerized their accounting at main branches. There are software packages (e.g. FAO-developed "Microbanker") which run on microcomputers and handle most of the loan and savings operations; similar systems are being developed by banks in certain developing countries. Microbanker is soon to be released and will be supported by FAO for development banks and other financial institutions providing services to rural people in developing countries. Computerized systems have the advantage that many of the more time-consuming and error-prone tasks are done automatically; built-in checks reduce the possibility of errors. Accounts are always kept up to date since transactions are registered automatically; likewise, management can obtain accurate information on each individual account as well as summaries useful for monitoring principal financial variables of the programme, almost immediately. If microcomputers are located in local branches the primary accounting functions are kept exactly where they belong: as close to the borrower as possible.

Annex 4 shows sample formats of all necessary forms and ledgers to be maintained: a borrower's name file, a loan ledger account, a loan ledger transaction sheet and a monthly statement of loan recovery.

### **AUDITING: NEED FOR ANNUAL AUDITS**

Many financial institutions with which revolving funds are associated have their own rules which require at least internal and occasionally external audits.

The accounting system set up should supply information required by both internal and external audits. Initial audits should comment on the adequacy of the accounting system for this and other purposes.

Audits should focus on the overall soundness of the loan programme and particularly on overdue accounts. Copies of audit reports on revolving fund loans should be provided to collaborating financial institutions, donors and international organizations. All major deficiencies found by the auditors should be discussed by project management and national counterpart agencies and appropriate remedial action taken.

Outside auditors should be from the best nationally or internationally recognized auditing firms. They should be required to confirm that funds are correctly applied, that the accounting system provides the required information as soon as it is needed, that overdue accounts are being handled according to the rules established and that administrative costs are reasonable when compared with those of similar programmes.

### **TREATMENT OF BAD AND DOUBTFUL DEBTS**

Banks tend to keep bad and doubtful debts on their books, which accrue interest and raise the asset side of the portfolio. Strong and prompt action should be taken to collect loans as soon as it becomes apparent that delays in payments are not a temporary phenomenon. Loans should be placed on a non-accrual basis as soon as there is uncertainty as to their full payment; action should be taken no later than four months after the first monthly payment is missed or if the second quarterly payment or one annual payment is missed.

The number of loans in arrears should be reported as well as the amount of arrears. High repayment rates are often based on prepayment of a small number of large loans, which masks the fact that a high percentage of loans and perhaps a high percentage of the value due is unpaid. Management should ensure that loans unpaid are listed in descending order of amount. Older unpaid loans should be highlighted, since the longer a loan goes unpaid, the harder it is to collect.

### **MONITORING COST OF LENDING AND ADJUSTMENTS TO INTEREST RATES AND FEES**

Loan interest rates and fees should be reviewed at least annually. They should be adjusted if they do not cover average costs of operation. To adjust charges appropriately, the bank/revolving loan fund must keep records of staff time, material costs and other costs of the activities in which it is involved. The accounting system should provide an adequate record of what the bank earns from its lending and savings activities. If rates have been set too low to cover costs or if inflation is higher than expected, appropriate changes should be made based on observed costs and new estimates of inflation rates.

In some countries, interest charges are either not permitted for religious reasons or cannot be set at a high enough rate to cover bad debts, costs and inflation due to usury laws. In these cases a combination of loan fees, commissions and perhaps insurance premiums can be developed which at appropriate levels can cover lending programme costs.

### **OTHER BANKING SERVICES REQUIRED BY FISHERFOLK AND AREA RESIDENTS**

#### **Savings accounts**

Facilities for savings should be seen as a service provided if required and if their provision does not interfere with providing credit. They should be provided if the needs assessment survey done at the beginning of the programme shows that the lack of a savings facility is a concern of the community. The same survey should establish how people save, and

whether their methods constitute an acceptable substitute for a nearby savings facility.

If there is a demonstrable need for a savings facility, project managers should be aware that the requirements for setting up and operating such a facility cost money and that adding them to the loan facilities will require more resources and a considerable dedication of management time. They require additional staff, offices, equipment and supplies.

### **Current accounts**

Current accounts are not required by most of the fisherfolk revolving funds are designed to serve. If a financial institution associated with the revolving fund is to expand its presence in coastal areas, it may find that a “full-service” approach makes best use of its small branches. By offering savings facilities and current accounts, local business people may be encouraged to use local branches of the financial institution rather than commercial banks located some distance away. Their large accounts can be used to subsidize losses on small savings accounts held by fisherfolk. If savings mobilization is a goal of the financial institution, the provision of current accounts is a good way to attract larger accounts. Some countries protect the interests of commercial banks by prohibiting agricultural development banks from providing current accounts.

### **Overdrafts**

Any person running a business and using a current account will want overdraft privileges, which protect the account holder against accidentally overdrawing. Most banks do not provide overdraft facilities to all holders of current accounts but only to those who have demonstrated the responsible operation of current accounts without overdraft facilities. Limits are initially set at low levels and are based on past experience of borrowers’ repayment of credit. Since most current account holders in need of overdraft privileges are unlikely to be members of the target groups for fisheries revolving funds, loans and overdrafts to them should be from the bank or financial institutions own funds not from those supplied by the revolving fund.

Most artisanal fishermen do not want current accounts but would like to have unsupervised credit of some sort to meet their most pressing obligations. If it is thought desirable to provide small amounts of unsupervised credit, a pilot programme should be instituted amongst borrowers who have excellent records of repayment of past supervised loans. Each borrower should be set a credit limit and repayment performance should be reviewed frequently. If one payment is missed, the line of credit should be cut off until the borrower is current on all obligations to the bank. Lines of credit can be extended to borrowers who do not have current accounts. A promissory note should be signed upon authorization of the line of credit for its maximum amount. Staff should be trained in the operation of lines of credit, particularly in staying within the limit and in collection procedures for repayment. If borrowers have both the line of credit and supervised loans, supervisory officers should be made aware of this additional financial obligation.

### **Money transfer**

Telegraphic transfers may be most useful to the revolving fund programme since they allow funds collected to be sent to regional and central offices. Money transfers are particularly useful if mechanisms have been developed for the exchange of local currency repayments and surplus funds into foreign currency to provide the foreign currency needs of the project, and as a hedge against devaluation and inflation. Local fisherfolk cooperatives, fishdealers and others engaged in business may find these services useful. If the cooperating financial institution offers these services to clients other than those targeted as beneficiaries of the revolving fund programme, they should be charged the full costs associated with such transfers. Fisherfolk targeted as beneficiaries of the revolving fund should also be charged full cost of these services.

## CHECKLIST

### 1. Annual work plan and lending programme budget

- Is there a mechanism in place for annual adjustments of the lending programme budget according to disbursement and recovery achievements of the previous year?
- Is the project management aware that the adjustment of the lending programme budget might require in some cases - depending on the source of funding of the project - a revision of the project budget, which has to be initiated in time?
- Is there an awareness that when adjusting lending programme budgets, costs associated with loan supervision and collection, borrower education and advertising of the loan programme should also be reflected, if not covered, under other budget lines?

### 2. Accounting

- Has a separate bank account been set up which is exclusively used for operating the revolving fund?
- Are the FAO administrative procedures relating to the operation of income accounts also applied to the operation of the revolving fund account?
- In case of in kind disbursement of loans and the project's involvement in procurement of fishery inputs to be supplied to fisherfolk on credit, are the general FAO administrative procedures and rules also applied to procurement from the revolving fund account?
- Does the accounting system for the revolving fund maintain an accurate and timely record of the status of the individual loans? Which of the following are being used: loan ledger, loan ledger account, name file, repayment file, monthly balance listing?



### **3. Auditing**

- What are the arrangements for internal and external auditing of the revolving fund accounts?

### **4. Treatment of bad and doubtful debts**

- Does the accounting system provide for loans to be placed on a non-accrual basis as soon as any major doubt arises as to their full payment?
- Does the accounting system provide for regular reporting of the number of loans in arrears as well as of the amount of arrears?

### **5. Monitoring cost of lending and adjustments to interest rates and fees**

- Is the cost of lending monitored on a regular basis?
- Are interest and other fees charged on loans from the revolving fund/ fisheries credit programme regularly adjusted according to changing costs of lending?

### **6. Other banking services required by fisherfolk and area residents**

- If a financial institution is involved in operating the revolving fund, which banking services other than credit, such as savings facilities, current accounts with overdraft facilities, could be provided for fisherfolk?
- Which role could the project play in facilitating the access of fisherfolk to these services?

