Finance for Non-Finance Managers

Presented by Genny Jones

Introduction and Objectives

I hope you will get:

- A good understanding of some key finance-based concepts
- Why they apply to you and your role
- And thus how you can make a difference in your organisation's financial management

dsc
directory of social change

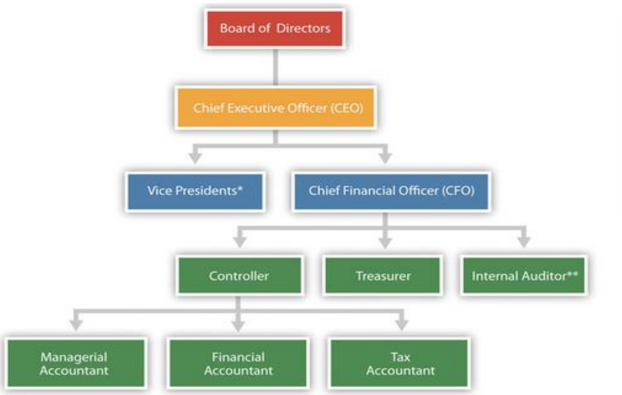
Contents

- **Key finance concepts**
- **The difference between cash and profits**
- **Costs and costings**
- **Budgets and cash flows: why and how**
- **Management and financial information**

dsc
directory of social change

The why of finance

- Statutory obligations (Charity law, Company Law etc)
- Managers need to report to stakeholders (owners)
- enabling external stakeholders to understand and compare results
- Produce reports that can be used for internal decision making



directory of social change

The why of finance

Statutory Duties

- Maintain accounting records
- Prepare and submit statutory accounts
- Audit responsibilities
- Maintain statutory registers
- File returns and reports
- Meetings and other administrative matters

dsc
directory of social change

Financial Reporting

- The law requires summary of finances to be produced
- so that stakeholders can understand the organisation's financial position
- Organisations can be compared
- Managers can be called to account
- Relevant decisions can be made going forward

dsc
directory of social change

Financial Reporting

Receipts and Payments vs Accruals Accounting

. On 1st March invoiced raised for £10,000 grant due to the organization. On the 31st of March we need to prepare accounts

Cash basis – Income will be recorded as 0 in March as I have not yet received the money in the bank.

Accruals basis – Income will be recorded as £10,000 as this was earned during that month even though we have not yet received it. The balance sheet will also have the £10,000 showed as a debtor..

Financial Accounts

Receipts & Payments

- Cash Basis – money in and out of bank/cash accounts

- Receipts & Payments
- List of Assets and Liabilities
- Trustees Annual Report

Accruals

- Cash Basis – money in and out of bank/cash accounts

- + Accounting Adjustments
- State of Financial Activities - by Fuds
- Balance Sheet
- Notes to Accounts
- Trustees/Director's Annual Report

directory of social change

Financial Reporting

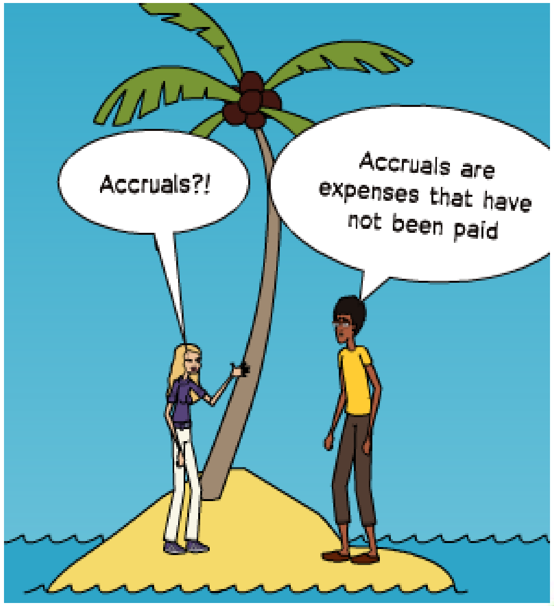
The Trustees (Directors) Report

- Explains financial performance
- Puts into context activities /achievements against plans and objectives set
- Outlines plans for the future

directory of social change

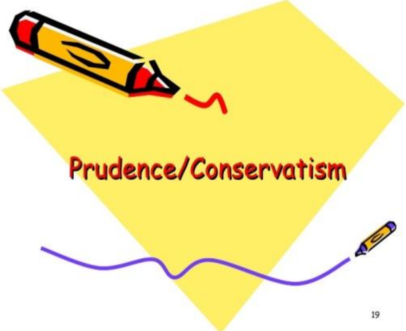
Basic Terminology

*The **Accruals concept** which subject to prudence, brings the relevant transactions into the same period of account, without regard to the actual dates of receipt and payment;*



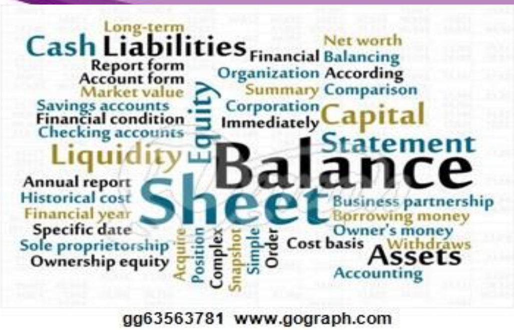
Basic Terminology

- *The "**consistency**" concept of treating like items alike within the accounts and from one year to the next; and*
- *the "**prudence**" concept of making provision for all actual and probable liabilities, but only including assets as incoming resources when they are definitely realisable.*



directory of social change

Balance Sheet



- **Fixed assets**
  - Intangible assets
  - Tangible assets
  - Investments
- **Current assets**
  - Stock and WIP
  - Debtors
  - Investments
  - Cash/bank

- **Liabilities**
  - Creditors within one year
  - Creditors after more than one year
- **Funds/owners equity**
  - Retained profits/reserves or
  - Restricted and unrestricted funds

Balance Sheet

- Fixed Vs current assets
- Depreciation of tangible assets
- Valuation of current assets- stock write offs, bad debts
- Importance of debtors and creditors
- Accrued Income – Income due but not yet invoiced
- Accrued Expense – incurred but invoice not received
- Prepayments – payments made in advance
- Deferred income – income received
the following

Accounting policies

- **Basis of preparation** of accounts
- **Treatment of incoming resources-** accounted for only when received or definitely receivable (gross of related expenditure)
- **Resources expended**- reported when incurred (gross of related income)
- **Capitalisation of fixed assets** e.g only where purchase price is greater than £X (Based on your organisation's Fixed Asset Policy)
- **Investments**- stated at market price at balance sheet date

directory of social change

Financial Reporting

Information will come from the Accounting books and records or the computerised system made up of:-

- **Nominal ledger**
  - Cash records
  - Records of all sales and income receivable
  - Records of all purchases and expenses
  - Details of capital expenditure
- **Sales ledger** (accounts receivable)
- **Purchase ledger** (accounts payable)

Audit/Independent Examinatio

CHARITY COMMISSION

CC63-Independent Examination of Charity Accounts:

"Charities' Act embodies the concept that some form of independent scrutiny is required for the accounts of all but the smallest charities, but ….(may not be) a full requirement for an audit"

acie

association of charity independent examiners

dsc

directory of social change

Audit/Independent Examination

- An audit will be needed if total assets (before liabilities) exceed £3.26 million, and the charity's gross income is more than £250,00

- An independent examination is needed if gross income is between £25,000 and £1 million
- ***Except***
- If governing document stipulates audit
- Other statutory requirement (e.g. Company Law) stipulates audit
- Audit is a requirement of donor etc

Difference between an independent examination and an audit.

Independent Examination is checking that the accounts look correct and agree with the records. This assumes that the underlying records are correct.

Audit would require verifying that the underlying records are correct. ... For these reasons, not all charities are required to have an audit

directory of social change

Audit/Independent Examination

CC63:independent examination

- Review of the accounting records kept by the charity
- A comparison of the accounts presented with those records
- Review of the accounts
- Consideration of any unusual items or disclosures identified
- *No true and fair view opinion needed*

dsc
directory of social change

acie
association of charity independent examiners

Basic Terminology

GOING CONCERN

The importance of

- **Liquidity**- assets in cash or near cash form
- **Solvency**- enough assets to cover liabilities, to continue to be a
- **Going concern-** able to meet debts as they fall due

Budgets and budget management enables this to be done effectively!

Basic Terminology

Going concern

- *“concept used for valuing assets and liabilities on the basis that activities will continue uncurtailed for the foreseeable future ~(in particular, the following year) and that there is therefore no need to use liquidation valuation principles”*

Basic Terminology

A true and fair view of:

- **Incoming resources** for the financial year;
- **Application of resources** in the financial year; and
- **State of affairs or financial position at the end of the financial year**

Complete Task

directory of social change

Costs and costings

Costing (Full cost recovery) is what charities need to charge to break-even and recover all costs, including overheads. It is the real cost of doing business.

Pricing is how much charities are willing to charge for services especially if they are bidding for contracts. It includes an element of profit and any contingency they may want to include.

directory of social change

Costs and costings

Variable costs

- These are costs that change with activity, so that each time something is done there is a cost associated with it

Fixed costs

- These are costs that are incurred even where there is no activity

directory of social change

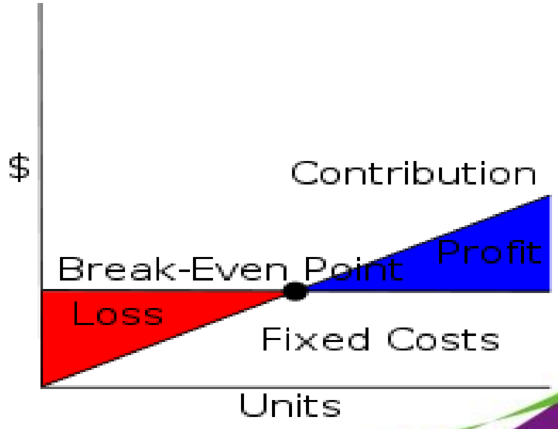
Costs and costings

Breakeven

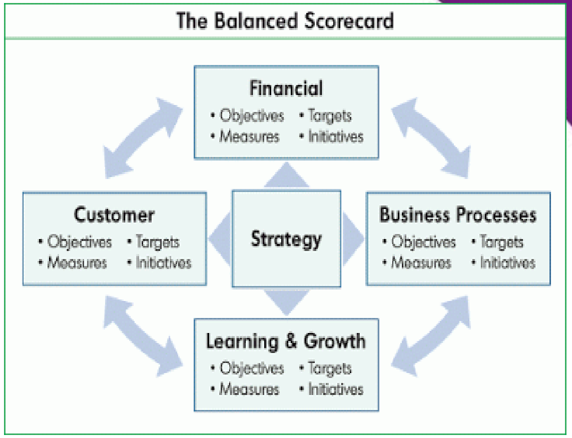
The point (level of activity) at which fixed costs are covered exactly

*** Break Even Point = fixed costs/Contribution**

•Contribution = selling price – variable costs



Costs and costings



The break point

- The point at which the service reaches capacity (viable)
- Given the resources the organisation has currently
- Beyond which the service is past capacity and
- Will simply be responding or crisis managing
- Unless extra resources are provided

directory of social change

Complete Task

directory of social change

Cost Recovery: How

dsc
directory of social change

Cost Recovery: How

Full Cost Recovery

Overheads can be broken down into:

- Premises and office costs
- Central function costs
- Governance and strategic development costs
- General fundraising costs

Cost Recovery: How

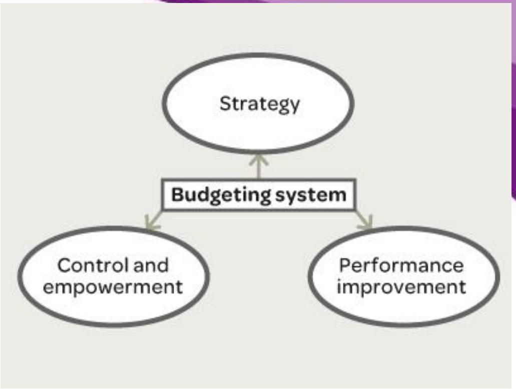
Full Cost Recovery

Cost allocation basis (Cost drivers):

- Premises and office costs- **headcount, desk space or floor space**
- Central function costs-**time**
- Governance and strategic development costs-**expenditure**
- General fundraising costs- **income or income shortfall**

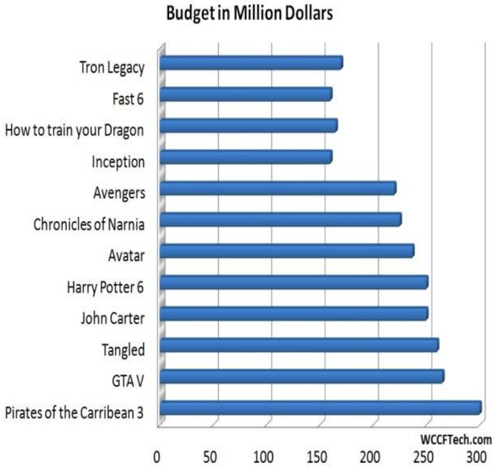
dsc
directory of social change

Budgets- as a Tool



Establish a mission or strategy

- Budgeting used to:
    - Allocate/ maximise resources
    - Implementing plan
    - Identify financial/ resource prob
    - Indicator for employee performance
    - Actions required to fulfil goals



directory of social change

Budgetary Control:

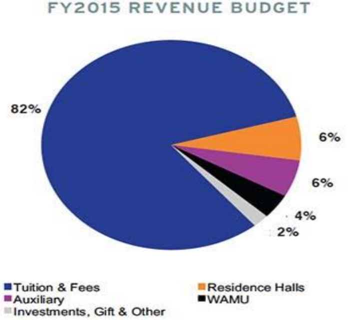
- *Helps to maintain and monitor finance*
- *Budgets should be prepared in in advance of an accounting period, ideally for 3 years and should be reviewed,*
- *Budgets are compared with actual performance to establish any variances.*
- *Managers should be made responsible for the controllable activities within their budgets.*
- *The budget should be approved, signed and dated*

Approach to budgeting

- **Zero based –** start with a clean sheet

- **Incremental** – take history and change, either your own or someone else's

dsc
directory of social change



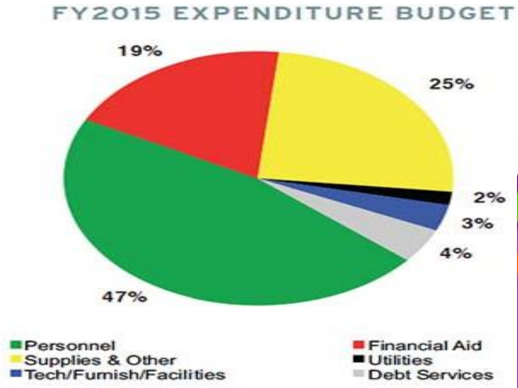
Budgeting: Revenue/Income

- Grant aid from statutory bodies
- Service agreements and contracts
- Grants from trusts and companies
- Public fundraising
- Sponsorships
- Legacies
- Subscriptions and donations from members
- Profit from trading operations
- Earned income from the sale of services
- Hire of resources
- Investment income
- Management fees
- Consultancy fees
- Income from users(e.g rent)

directory of social change

Budget assumptions and contingency planning

- **Start up costs**,such as moving in, recruitment of staff-often underestimated
- **Slow start costs** - services slower than planned
- **Marketing costs**
- **Working capital -** used to develop new projects and to experiment
- **Research and development** costs e.g user consultation
- **Cash flow costs** - funding periods of cash shortages
- **Management and administrative costs** e.g payroll, volunteer management
- Replacement and repair costs
- **Contingency costs** e.g maternity, sickness cover
- **Close down costs**



directory of social change

Young Pioneers Project Budget		
Details	Basis/Assumptions	Amount
Recruitment of project Manager	One off fee to advertise post (Third Sector half page advert)	2,325
Project manager's salary	£34k per annum prorate for 3 days of the week (i.e 3/5)	20,400
Employer's cost of PM's salary	Salary of £20,400 x 18.8% as on-costs	3,835
Total Project Manager salary		26,560
Cost of Facilitators	2 Facilitators for 24 days x £80 per Facilitator per day	3,840
Cost of Guides	4 Guides for 24 days x £40 per Guide per day	3,840
Cost of Volunteers	2 Volunteers per day for 24 days x £10 per Volunteer per day	480
Additional staffing costs		8,160
Premises costs	£85 per day cost of the project/training room, for 24 days	2,040
Course materials	Estimated cost of £10 per beneficiary x 40 youth	400
Other direct costs		2,440
Total direct costs		37,160
Share of organisational overhead	On the basis of expected income. Young Pioneers Project expected to raise (45K/565K) 8% of total income, so would "absorb" 8% of overheads. I.e. 8% x £98k	7,840
Total project costs		45,000

Cash-flow forecasts: what

Cash-flow forecasts provide estimates about:

- Income when realistically expected
- Expenditure: when payment would be made
- And the impact of these timings on the overall cash position

directory of social change

The purpose of a cash flow forecast

- Identify cash critical points
- Based on cash receipt dates
- And cash payments outflows
- Plan accordingly

dsc
directory of social change

Cash-flow forecasts: What

Expenditure shown when due to be paid

- In accordance with credit terms negotiated with suppliers
- And applied appropriately to enable a good relationship to be maintained
- Taking account of regular (monthly) items which cannot ordinarily be delayed e.g wages.

dsc
directory of social change

Cash-flow forecasts: why

The budget will show whether there is enough overall income to cover overall expenditure

The “when” when are expecting income and when we are making payments becomes more critical in the short to medium term especially in an adverse financial climate.

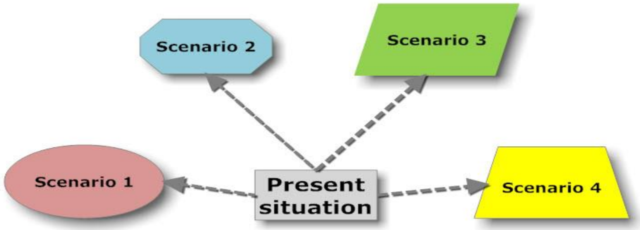
dsc
directory of social change

Using cash-flow forecasts

- Having established income and expenditure on a monthly basis,
- Work out any surplus or deficit of income over expenditure in that month
- Determine how to “finance” any deficit
- Decide what to do with surplus

dsc
directory of social change

Using cash-flow forecasts



- Having determined likely surplus/deficit, could look at different scenarios:
  - What if income was higher/lower?
  - What if (less) income came in earlier or more came in later?
  - What if expenditure was more or less?
  - could expenditure be paid earlier (less amount), or (more) later?

Cash Flow Forecast Example

Details	June	July	August	Total
	£	£	£	£
Inflows				
Grants	47000	47000	25000	119000
Other income	275	500	9	784
Total Inflows	47,275	47,500	25,009	119,784
Outflows				
Salary	15,000	15,000	15,000	45,000
Employer salary costs	2700	2700	2700	8,100
General overheads	23,000	22,000	19,000	64,000
Total Outflows	40,700	39,700	36,700	117,100
Cash Surplus/deficit	6,575	7,800	-11,691	2,684
Brought forward	0	6,575	14,375	0
Carried forward	6,575	14,375	2,684	2,684

directory of social change

Complete Task

directory of social change

Management Accounts

Financial accounts

- Statutory compliance
- Charity Law
- Companies Act

Management accounts

- internal decision-making
- forms the basis of financial accounts.

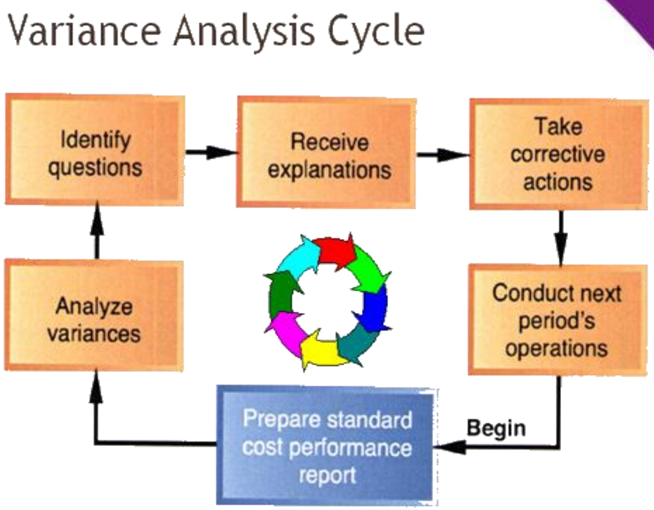
dsc
directory of social change

Management Accounts- Format

- No prescribed format
- There will be many different types of information
- Depends on audience
- What they need to know

dsc
directory of social change

Management Accounts- Variance Analysis



Budget-Actual= variance

Variances:

•highlight areas where assumptions are incorrect and

•areas where there is potential for improvement

Management Accounts

Operating Statements for board reporting

- Analysing (key) variances
- Favourable variances:
  - – Actual (sales) income exceeds budget
  - – Actual expenditure is less than budget
- Adverse variances:
  - – Actual (sales) income is less than budget
  - – Actual expenditure exceeds budget

Management Accounts- Variance Analysis

- Good budgetary control ensures
- That significant variances are explained
- Questions answered about impact on budget
- That year-to-date information is made available to get the overall picture
- Budgets are revised/reforecast to enable more realistic future estimates to be made

dsc
directory of social change

Management Accounts

Operating Statements for board reporting

- (Re) forecasting
- Actual turnover/income
- and expenditure against budget
- Actual against forecast
- Update on sales and income
- Summary of year-to-date position

dsc
directory of social change

Further readings

- Further reading:
  - A practical guide to financial management for charities and voluntary organisations: Kate Sayer (DSC)
  - A practical guide to charity accounting: Kate Sayer (DSC)
- Reference points: www.charity-commission.gov.uk
  - CC3: the essential trustee, what you need to know
  - CC15a - Charity Reporting and Accounting: The essentials
  - CC8- Internal financial controls for charities
  - Accounting and Reporting by Charities: Statement of Recommended Practice- (revised 2005)

directory of social change