

FACT SHEET

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Businesses often fail because of poor financial management or a lack of planning. Social enterprises are no exception and are sometimes vulnerable to pressures such as grant funding expiring or late payment on contracts. Often the business plan that was used to help raise finance is put on a shelf to gather dust.

When it comes to your business' success therefore, developing and implementing sound financial and management systems (or paying someone to do it for you) is vital. Updating your original business plan is a good place to start.

There are a variety of ways to ensure that you are on top of your finances. The initial starting point is to have a solid and realistic business plan in place. This will provide you with a starting point of predicted expenditure (including any borrowing), projected income, cost of sales and profit and loss forecasts. The next step is to set budgets for particular projects and for the organisation in general.

Budgeting

You are basically looking at what your income and expenditure is going to be over a fixed period of time. A successful budget will help you to plan the activities of your enterprise, allocate resources effectively and ensure that you are aware of any changes to your predicted cashflow.

Look at the projected sales/income for the budget period and don't overestimate, as this will cause you problems in the future.

What are the direct costs of sales, i.e. costs of materials, components or subcontractors to make the product or supply the service? Remember that these will vary if you sell more.

What are the fixed costs or overheads?

You should break down the fixed costs and overheads by type:

- cost of premises - eg rent, rates, service charge,
- staff costs - eg wages, benefits, National Insurance,
- utilities - eg heating, lighting, telephone,
- printing, postage and stationery,
- vehicle expenses,
- equipment costs,

- advertising and promotion,
- travel and subsistence expenses,
- legal and professional costs, including insurance,
- your salary as owner or director,
- tax.

These are just some examples and your enterprise may have different types of expenditure so it is important to think carefully as you don't want any surprises.

Your business plan should help in establishing projected sales, cost of sales, fixed costs and overheads, so it would be worthwhile preparing this first.

Once you've got figures for income and expenditure, you can work out how much money you're making. You can look at costs and work out ways to reduce them. You can see if you are likely to have cashflow problems, giving yourself time to do something about them.

When you've set a budget, you should stick to it as far as possible, but review and revise it as needed. Successful businesses often have a rolling budget, so that they are continually budgeting, e.g. for a year in advance.

Key things to remember with budgets

- Be as realistic as possible in setting budgets. Use information from your business plan and last year's budgets to get an indication of income and expenditure.
- Look at the relation between increasing your sales or services and your variable costs. You might need to adjust your pricing structure accordingly.
- Involve the right people; your finance manager, project leaders. You'll then get a greater commitment to sticking to the budget.
- Review on a regular basis – compare your actual income and expenditure figures with your budgeted ones.

Review your financial position

The level and frequency of financial reviews will depend on the nature and complexity of the business. For a typical small business, bank reconciliations should be completed weekly, while other analyses may be more appropriately performed monthly. The quarterly preparation of a VAT

return can provide an excellent overall check on the accuracy of book keeping procedures.

When reviewing your finances, you might want to consider the following:

- **Cashflow** - this is the balance of all of the money flowing in and out of your business. Make sure that your forecast is regularly reviewed and updated.
- **Working capital** – your current assets minus your current liabilities. Do you have enough capital to pay any debts and operational expenditure? If necessary, take steps to source additional capital.
- **Cost base** - keep your costs under constant review. Make sure that your costs are covered in your sale price - but don't expect your customers to pay for any business inefficiencies.
- **Borrowing** - what is the position of any overdrafts or loans? Are there more appropriate or cheaper forms of finance you could use?
- **Growth** - do you have plans in place to adapt your financing to accommodate your business' changing needs and growth? For social enterprises this could have implications on the type of legal structure you adopt.

Tools for financial management

There are a variety of tools that can be used to manage your finances. It is important to keep financial records in order to be able to analyse your business and make decisions.

Although the level of record keeping required may vary from business to business, it should include:

- all receipts and expenditure
- all goods purchased or sold

There are no rules about the format you must use to record your figures - those kept on paper are just as valid as those stored on computer. What's important is that you keep accurate, relevant financial records and update them on a regular basis. You may have to pay a penalty if you're unable to back up the statements made in your VAT and income tax returns.

Management accounts

Management accounts are invaluable in helping you to make timely and meaningful management decisions about your business. They serve a different purpose to Financial Accounts that are prepared for scrutiny by investors and Companies House. Management Accounts are there for you to analyse your financial performance.

Different businesses will have different management accounting needs, depending on the business areas that are important to them. These can include:

- the sales process - including pricing, distribution and debtors
- the purchasing process - including stock records and creditors
- a fixed asset register
- employee records

To run a business effectively, most companies produce management accounts regularly - eg monthly or quarterly. Management accounts analyse recent historical performance and usually include forward-looking elements such as sales, cashflow and profit forecasts.

The analysis is usually performed against forecasts and budgets that have been produced at the start of the year. Management accounts will help you to compare your accounts with original budgets, keep track of your resources and highlight variations in your income or spending which may require attention. They should be used for record keeping, financial control and to make decisions about issues such as pricing, marketing and to evaluate the effect of any previous strategies or plans.

For further information on managing your finances, please see the BusinessLink website:

<http://www.businesslink.gov.uk/bdotg/action/layer?r.l1=1073858790&topicId=1073858944&r.s=tl>