

# Simple is Beautiful:

Small Charity Accounts as if Trustees Mattered



## Budgets & Cash Flows

*One of a Series of Guidance Leaflets for Small Charities*

### The Scope of These Guidance Leaflets

The title of this series of leaflet has been inspired by the 1960s (but even more relevant today) iconic book, *Small is Beautiful: Economics as if People Mattered*, by E.E.Schumacher.

This leaflet is one of a series which give a quick overview of the various things that you will need to consider in managing the money of a small charity.

They are NOT a full and comprehensive guide to Charity Law and all the associated regulations. They are just an overview, in simple everyday language (rather than legalistic/accountancy jargon) of the main points for those who want to run their small charity efficiently and effectively for the benefit of their local community, or to help trustees who have encountered a common difficulty.

So, if you are expecting your charity's annual income to be more than £150,000/yr, or to own property, or to employ more than the equivalent of 3 full-time staff then you will probably need to seek professional guidance elsewhere.

The topics covered in this series are:

**What Accounts ALL Small Charities MUST Keep**

**The Role of the Charity Treasurer (and assistants)**

**Recording & Managing Your Charity's Funds**

**Budgets & Cash Flows** *{This Leaflet}*

**Financial Controls CheckList**

**Preparing the Annual Report & Accounts – Unincorp.Associations**

**Preparing the Annual Report & Accounts – CIOs**

Receipts & Payments vs Accruals Accounting *{Not yet available}*

**A Bank Account**

Other guidance leaflets for small charities (or people looking to set up a new small charity) available elsewhere on the Small Charity Support website ([www.smallcharitysupport.uk](http://www.smallcharitysupport.uk)) include:

Outputs & Outcomes

Governing Documents

The "Minute Book"

Business Planning & Risk Management

Registering with the Charity Commission

Charitable Purposes/Objects

Trustees & Officers

Policies & Procedures

Gift Aid Registration with HMRC

Your comments and suggestions (to [comments@smallcharitysupport.uk](mailto:comments@smallcharitysupport.uk)) as to how these leaflets could be improved to make them simpler and clearer would be much appreciated.

**Last Updated: 03-Jul-18**

# Budgets & Cash Flows

## (Reviewing the Charity's Financial Performance)

### 1. Introduction

As noted in some of the other leaflets in this series:

- ☛ **Charity officers (including the Treasurer) don't automatically have any extra powers or legal duties than their co-trustees.**
- ☛ **All trustees share responsibility for finances (not just the treasurer)**

In the event that a charity's finances "find themselves in troubled waters" its Trustees will NOT get away with excusing themselves of personal responsibility for the consequences by simply saying: "Oh, it's not our fault – we leave all the financial matters up to the Treasurer".

One valuable way of keeping the responsibility for financial matters firmly in front of the Trustees is for a review of the charity's finances to be on the Agenda automatically for EVERY Trustees' meeting.

**It DOESN'T have to be long !**

Hopefully in most cases it will simply be a case of presenting the budget and financial performance figures to date to reassure the Trustees that "all is going to plan".

How budget reports are produced and what they display will vary from system to system. But a format for the regular budget and financial report which is close to (if not exactly) the format which will appear in the final end-of-year accounts is useful. That enables the Trustees to see how the accounts are building up throughout the year, thereby avoiding any end-of-year unwelcome surprises.

The illustration shows the Budget Report produced by the Small Charity Support Simple Accounts Spreadsheet. The

| Better Living Charity Budget Report: 31-Dec-16 |                  |                |                     |                     |              |
|--|------------------|----------------|---------------------|---------------------|--------------|
| RECEIPTS                                       | Prev Yr Out-turn | This Yr Budget | Budget to 31-Dec-16 | Actual To 31-Dec-16 | Variance     |
| <b>R1-VOLUNTARY INCOME</b>                     |                  |                |                     |                     |              |
| R1-Membership                                  | 1,230            | 2,500          | 2,500               | 2,550               | 50           |
| R1-Donations                                   | 1,904            | 3,000          | 3,000               | 2,864               | -136         |
| R1-GiftAid                                     | 0                | 800            | 800                 | 0                   | -800         |
|  | <b>3,134</b>     | <b>6,300</b>   | <b>6,300</b>        | <b>5,414</b>        | <b>-886</b>  |
| <b>R2-INCOME GENERATION</b>                    |                  |                |                     |                     |              |
| R2-Fundraising                                 | 0                | 240            | 240                 | 0                   | -240         |
|  | <b>0</b>         | <b>240</b>     | <b>240</b>          | <b>0</b>            | <b>-240</b>  |
| <b>R3-INVESTMENT INCOME</b>                    |                  |                |                     |                     |              |
| R3-Interest-Bank Accounts                      | 0                | 12             | 12                  | 0                   | -12          |
|  | <b>0</b>         | <b>12</b>      | <b>12</b>           | <b>0</b>            | <b>-12</b>   |
| <b>R4-CHARITABLE INCOME</b>                    |                  |                |                     |                     |              |
| <b>R4G-GENERAL FUNDS</b>                       |                  |                |                     |                     |              |
| R4G-ConfRegistrations                          | 0                | 0              | 0                   | 1,350               | 1,350        |
| R4G-Miscellaneous                              | 0                | 0              | 0                   | 0                   | 0            |
|  | <b>0</b>         | <b>0</b>       | <b>0</b>            | <b>1,350</b>        | <b>1,350</b> |
| <b>R4R-RESTRICTED FUNDS</b>                    |                  |                |                     |                     |              |

layout of the categories of Receipts and Payments replicates the layout used in the Annual Financial Statements. That way each presentation of the Budget Report shows the Trustees how the financial performance is progressing to what will actually appear in the final Annual Report.

The columns in the report show the information which will help the Trustees to understand better the implications of the various numbers for each category of receipts or payments.

**B – Prev Yr Out-turn:** shows the final figure for the previous year for comparison purpose;

**D – This Yr Budget:** shows the budget for the whole year;

**E – Budget to {date}:** shows the budget to the date of the report {as selected at the top-right of the screen};

**G – Actual to {date}:** show actual receipts/payments to the date of the report;

**I – Variance:** shows the difference between the budget and actual at the date of the report.

Columns C, F & H are blank to improve the readability of the screen.

On those occasions when there is a significant variance between the budget and the actual performance to date the Budget-Holder for that category, or the Treasurer, can provide an explanation of the reason for that and what is being done to address it. That is key to reassuring the Trustees that the matter has been picked up promptly and is being dealt with before it becomes a crisis.

**And the regular financial review SHOULD NOT be the last agenda item so that by the time that item is reached the only thing that the Trustees are interested in is "switching off the lights and going home".**

## 2. Financial Performance – Setting the Budget

### 2.1. The Role of the Treasurer

It is axiomatic that, in order to review its financial performance (*ie*: make sure that its resources, particularly money, are being used wisely and effectively) the charity should have realistic and carefully planned & approved budget for the financial year.

And it is equally axiomatic that the budget should be central to the Trustee's review of the charity's financial performance at each Trustees' meeting.

It is NOT the role of the Treasurer to set the budget – *ie*: decide what figures should go where. That is the role/responsibility of the Trustees as they approve the budget.

Having said that, it **IS** the role of the Treasurer is to take the lead in collecting and collating the budget proposals from those taking the lead responsibilities for the different aspects of the charity's activities. And that includes helping and supporting those who are putting the proposals together.

The range of activities involved will, of course, vary considerably from charity to charity. But "activities leads" will typically include:

- ✓ the person(s) looking after fundraising, donation, subscriptions, grants, *etc.* for what receipts they expect the charity to be getting in the current year;
- ✓ the person(s) looking after activities for beneficiaries, administration, maintenance, publicity, *etc.* for what payments they expect the charity to be making in the coming year;

It is important when seeking budget proposals that high-profile activities – the latest project or big fundraising campaign – don't overshadow the more mundane aspects of the charity's activities – the cost of postage or the income from a donations box – so that they get overlooked.

Getting those figures for the Treasurer to collate depends on the charity (the Trustees, not the Treasurer) having first put together a Business Plan outlining what it wants to achieve in the coming year. Business Planning is NOT a specific role/responsibility of the Treasurer (though the Treasurer will usually be highly involved). So Business Planning is dealt with in separate guidance notes (see: <http://www.smallcharity.support/BusPlan.html>)

The Treasurer then "puts all those numbers together" to see what they add up to in terms of the charity being in surplus<sup>1</sup> or deficit at the end of the year. The initial draft budget can then be looked at "in the round" to check whether what is being proposed – both in money terms and activity terms – is consistent with both the charity's objects and its priorities in addressing those objects.

It will, of course, happen that the first draft figures "don't add up".

There might be rather more income proposed than expenditure, creating an unjustifiable surplus.

Or, perhaps more likely, more expenditure proposed than income, creating a deficit (which may or may not be acceptable). But whatever the initial proposal figures add up to, it is likely that several revisions of the proposals will be needed to achieve an acceptably balanced budget.

### 2.2. The Role of Budget Holders

The notion that "*those taking lead responsibilities...*" for the various activities of the charity are also responsible for identifying and putting forward for approval the amount of money that they expect to raise from, or spend on, the activities for which they are responsible effectively makes them the "Budget Holder(s)" for their activities. So the budget-setting process – allocating money-raising targets or spending limits based on what was proposed, effectively allocates "Budget Holder" responsibility for ensuring that those targets/limits are adhered to those who proposed them.

This is a good way of building into the culture of the charity the shared responsibility of Trustees for its effective financial management.

It is not uncommon in small charities for the Treasurer to be asked for "permission" to spend money on a particular item or activity. And sometimes that is appropriate, particularly when there is a temporary cash-flow issue (*eg*: an unexpected delay in incoming funds). But in many cases that question should

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<sup>1</sup> Charities, being "Not-for-Profit", don't make profits – despite the number of times that charity guidance refers to charities' "profits". Instead they only make surpluses.

properly be asked not of the Treasurer but of the relevant Budget Holder. Provided that the regular financial report to the Trustees is showing that the charity's finances are generally running to budget, the approval of the budget was the Trustees' authorisation for the charity's money to be spent in the way which had been proposed. If "asking permission" to spend money really means that permission is being sought to spend money outside of what was authorised in the budget the question should really come back to the Trustees for consideration and further approval, particularly if the amount is significant.

### 2.3. Setting the Budget

**Budget setting is NOT an exact science.**

**Some figures may be defined and predictable.**

**But much of budget setting is often seen as a "Black Art" of opinion, guesses and approximations.**

Setting a budget will therefore generally require several attempts, particularly if there are any inconsistencies or conflicts of priorities which need to be resolved before a final budget can be approved by the Trustees.

**So, leaving "budget setting" to the week before the end of the financial year is NOT a good idea!**



It is often assumed that a budget which shows a significant deficit is always a bad thing while one which shows a significant surplus is always a good thing.

**BOTH THOSE ASSUMPTIONS ARE WRONG.**

A large deficit budget is a GOOD thing if, for example, it is due to the charity planning to spend some of the money it had been building up in its designated funds to pay for a major investment in its resources (eg: setting up a new project or activities, or re-furbishing its dilapidating accommodation).

A large surplus budget is a BAD thing if, for example, it is due to the charity making charges for its charitable services which are inappropriately high thereby excluding those beneficiaries who need those services most, or it is making over-optimistic claims to donors about what the charity is achieving (or will be achieving) – effectively fundraising under false pretences.

Of course, if a surplus budget has been set specifically to raise money to go into a designated fund to provide the resources for a major development in the future, that is a different matter – provided, of course, that that is properly and clearly explained in the charity's annual financial review.

But whether the final outcome is agreed to be a surplus or deficit, the budget should always include provision for a margin of error – a realistic allowance for "contingencies" – receipts being a bit lower or payments a bit higher than expected.

This should be part of the charity's policy on maintaining uncommitted reserves carried forward from year to year, as described in its financial review in the Annual Report.

## 3. Financial Performance – Setting the Cash Flow

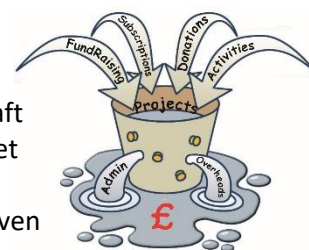
It is often assumed that budgeting and cash-flow are different things – in larger organisations being (apparently) dealt with by different sections of the "finance team".

**WRONG !**

An annual budget is simply a tool for forecasting and monitoring cash-flow based on the premise that a charity's money comes in yearly chunks.

Returning to the example (earlier, in section 3) of bank manager's attitudes. We all know that if a cheque is written for £30 when there is only £20 in the bank there is the risk of the cheque "bouncing" or of us being charged overdraft fees, even if a week later our wages/salary, sufficient to clear any overdraft, get paid into account.

So we all know about "cash flow" and the necessity to manage it effectively, even if we don't know that's what accountants and "bean counters" call it.



And we all know that looking at our annual income and expenditure just on a yearly basis is insufficient. It can be very "disappointing" to have booked, and be looking forward to, a nice holiday if it then has to

be cancelled because the day on which the final balance has to be paid comes before the day that we receive the salary that will pay for it.

People on monthly salaries know they have to manage their “cash flow” on a monthly basis to keep in financial balance – people on weekly wages perhaps weekly.

CHARITIES ARE NO DIFFERENT – and neither are the principles and practices of cash-flow management that charities, rather than individuals, need to follow (*ie*: we don’t need accountants and financial wizards to tell us how to do it).

Budgets are just CashFlows on a yearly basis

CashFlows are just Budgets on a monthly (or shorter) basis.

### 3.1. Creating a Monthly Cash Flow/Budget

Some charity receipts and payments come in or go out on a regular monthly basis. *eg*: subscriptions or payments for activities; utility bills; staff salaries. For those, setting and managing the monthly cash-flow (*ie*: the monthly “budget”) is easy – it is just the annual budget (cash-flow) figure divided by 12.

At the other end of the scale, some receipts and payment also come in or go out on a “regular”, but yearly or quarterly, basis. *eg*: major grants, insurance, MOT on vehicles.

Those, too, are “easy” in that the amount and date are known in advance.

But they still have to be dovetailed with all the other receipts and payments to ensure that the money needed to pay those bills will have come in before they need to be paid.

In the middle are those receipts and payments which are less well defined: *eg*: the amount of money expected to be raised by a fundraising event. and the costs of the event, may be rather speculative. In addition, the dates on which money will received in and paid out may also be “loosely defined” and spread over several months, perhaps with some of the costs going out before the money comes in if participants in the event want payment in advance. In such cases even the most carefully considered cash-flow predictions will be subject to significant margins of error.

And that why it is important for charities to manage their reserves carefully, too. A charity’s reserves are not just for “the doomsday scenario” – ensuring that the charity can close down successfully if its funding unexpectedly dried up. Reserves are also necessary to provide the safety-net which ensures that the charity is not put into financial difficulty when some of its cash-flow projections don’t turn out as expected -*ie*: expenses arrive earlier than expected or receipts arrive later than expected.

In essence – such differences as there are between a “budget” and “cash flow” are simply due to differences of time-scale. Aggregated over the year the sums of the monthly (“cash flow”) figures for receipts and payments are the same as the yearly (“budget”).

For example: a charity is proposing to hold a fundraising event half way through its financial year.

Looked at on a yearly (*ie*: “budget”) time-scale the event is expected to have more receipts than payments (*ie*: to make a net surplus) and all seems well. But, when looked at on a monthly (*ie*: “cash-flow”) time-scale it can be seen that the event will create a period of significant deficit in the month or two before the event as advance deposits have to be made and materials bought. A charity which only budgeted on a yearly basis would therefore have found itself in a serious financial crisis as it was unable to pay bills in the run-up to its fundraising event – while a charity which budgeted on a monthly (*ie*: cash-flow) basis would have seen the problem coming and taken steps to avoid it.

It therefore makes good sense for charities, small as well as large, to “budget” on a monthly (“cash flow”) basis as a matter of routine – rather than having “cash flow” as a separate exercise.

And why not, given that it very simple to do – rather than an “esoteric accountancy skill”.

The Small Charity Support “Simple Accounts Spreadsheet” illustrates just how easy it is.

The “Categories” worksheet (illustrated on the next page), where the amounts of the transactions relating to the individual categories are added up, includes not just a column (D) where the full year’s budget/cash-flow for each category can be entered but also columns (H-S) for entering the monthly cash-flow/budgets.

| Monthly Budget - FYE: 31-Dec-16 |                     |                  |                     |          |          |          |          |        |          |        |          |        |        |        |        |                      |
|---------------------------------|---------------------|------------------|---------------------|----------|----------|----------|----------|--------|----------|--------|----------|--------|--------|--------|--------|----------------------|
|                                 | Actual To 31-Dec-16 | Full Year Budget | Budget to 31-Dec-16 | Jan-16   | Feb-16   | Mar-16   | Apr-16   | May-16 | Jun-16   | Jul-16 | Aug-16   | Sep-16 | Oct-16 | Nov-16 | Dec-16 | SumCheck: Year Total |
| <b>RECEIPTS</b>                 |                     |                  |                     |          |          |          |          |        |          |        |          |        |        |        |        |                      |
| <b>R1-VOLUNTARY INCOME</b>      |                     |                  |                     |          |          |          |          |        |          |        |          |        |        |        |        |                      |
| R1-Membership                   | 2,550.00            | 2,500.00         | 2,500.00            | 1,500.00 | 750.00   | 250.00   | 0.00     | 0.00   | 0.00     | 0.00   | 0.00     | 0.00   | 0.00   | 0.00   | 0.00   | OK                   |
| R1-Donations                    | 2,863.70            | 3,000.00         | 3,000.00            | 250.00   | 250.00   | 250.00   | 250.00   | 250.00 | 250.00   | 250.00 | 250.00   | 250.00 | 250.00 | 250.00 | 250.00 | OK                   |
| R1-GiftAid                      | 0.00                | 800.00           | 800.00              | 0.00     | 0.00     | 0.00     | 0.00     | 800.00 | 0.00     | 0.00   | 0.00     | 0.00   | 0.00   | 200.00 | 0.00   | OK                   |
| <b>R2-INCOME GENERATION</b>     |                     |                  |                     |          |          |          |          |        |          |        |          |        |        |        |        |                      |
| R2-Fundraising                  | 0.00                | 240.00           | 240.00              | 20.00    | 20.00    | 20.00    | 20.00    | 20.00  | 20.00    | 20.00  | 20.00    | 20.00  | 20.00  | 20.00  | 20.00  | OK                   |
| <b>R3-INVESTMENT INCOME</b>     |                     |                  |                     |          |          |          |          |        |          |        |          |        |        |        |        |                      |
| R3-Interest-Bank Accounts       | 0.00                | 12.00            | 12.00               | 1.00     | 1.00     | 1.00     | 1.00     | 1.00   | 1.00     | 1.00   | 1.00     | 1.00   | 1.00   | 1.00   | 1.00   | OK                   |
| <b>R4-CHARITABLE INCOME</b>     |                     |                  |                     |          |          |          |          |        |          |        |          |        |        |        |        |                      |
| <b>R4G-GENERAL FUNDS</b>        |                     |                  |                     |          |          |          |          |        |          |        |          |        |        |        |        |                      |
| R4G-ConfRegistrations           | 1,350.00            | 0.00             | 0.00                | 0.00     | 0.00     | 0.00     | 0.00     | 0.00   | 0.00     | 0.00   | 0.00     | 0.00   | 0.00   | 0.00   | 0.00   | OK                   |
| R4G-Miscellaneous               | 0.00                | 0.00             | 0.00                | 0.00     | 0.00     | 0.00     | 0.00     | 0.00   | 0.00     | 0.00   | 0.00     | 0.00   | 0.00   | 0.00   | 0.00   | OK                   |
| <b>R4R-RESTRICTED FUNDS</b>     |                     |                  |                     |          |          |          |          |        |          |        |          |        |        |        |        |                      |
| R4R-SafeAtHome                  | 11,832.46           | 11,250.00        | 11,250.00           | 0.00     | 7,500.00 | 0.00     | 0.00     | 0.00   | 0.00     | 0.00   | 3,750.00 | 0.00   | 0.00   | 0.00   | 0.00   | OK                   |
| R4R-BetterEating                | 12,500.00           | 12,500.00        | 12,500.00           | 4,500.00 | 0.00     | 0.00     | 4,000.00 | 0.00   | 0.00     | 0.00   | 4,000.00 | 0.00   | 0.00   | 0.00   | 0.00   | OK                   |
| R4R-HealthMatters               | 3,905.39            | 4,000.00         | 4,000.00            | 0.00     | 0.00     | 2,500.00 | 0.00     | 0.00   | 1,500.00 | 0.00   | 0.00     | 0.00   | 0.00   | 0.00   | 0.00   | OK                   |

For categories (eg: Donations, row-3, in the example) where the receipts/payments are expected to be regular throughout the year, the monthly amount is just 1/12<sup>th</sup> of the annual amount and, by default, is calculated/entered by formulae.

For categories (eg: Membership, row-2 in the example) where the receipts/payments are dependent on the time of year, the expected amounts in each month (including zero) are entered by hand (overtyping the default formulae).

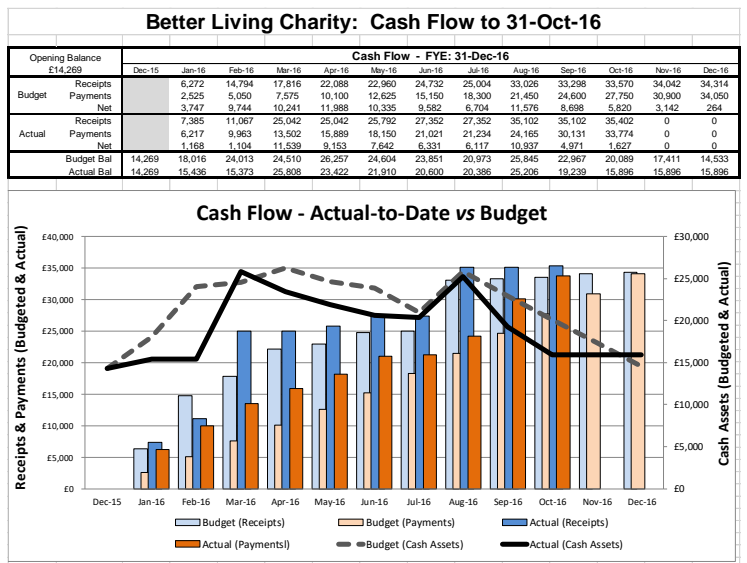
The "OK" in the right hand column is just a sum-check to ensure that the "cash flow" amounts entered for each month do actually add up to the "budget" amount entered for the year.

That's it. That's all that is necessary.

Once the monthly CashFlow/Budget figures have been set up (usually just once, prior to the start of the financial year) all that is required is that the transactions records are kept up-to-date. The figures for actual receipts and payments to date for the CashFlow/Budget reports are updated automatically "in real time" as the transaction records are being entered. And the corresponding figures for the expected receipts and payments to date are calculated from the relevant columns in H-S of the Categories worksheet – the relevant columns being determined by the Budget Report Date selected at the top of the Budget worksheet.

And the Cash Flow worksheet shows the same figures aggregated into a summary table and displayed in a graphic form.

The vertical bars show how the total receipts and payments are progressing as the year progresses. The lighter coloured bars represent the cash-flow/budget and the darker-coloured bars the actuals. The broken line represents how much money the charity was expected to have month-by-month (including its reserve brought forward from the previous year) and the solid line represents how much money the charity actually has.



The illustration shows that the charity had set itself a balanced budget – over the year it was expecting total income to match total payment, leaving the charity at the end of the year with roughly the same amount of reserves as it started with (the broken line). But much of its receipts come in the early part of the year, creating an early rise in reserves which then gets used up as the year progresses. In the event, receipt of one of the early grants was delayed, causing the actual reserves (the solid line) to fall significantly below the predicted until the following month. Thereafter, although the charity's receipts were slightly higher than expected, so too was its payment, leaving its actual reserves lower than expected. This improved a bit around the middle of the year – helped by the receipt, as expected, of another tranche of grant. But as the year progressed the deficit widened again. The illustration is just an interim report (as at the end of October, with another 2 month of the year remaining), so the actual figures for November & December are not known. But what the cash-flow/budget report shows is that, with no more significant receipts

expected at the end of the year but, with significant payments still to be made, the financial year looks like ending with a net deficit, *ie.* with less money in reserves than it started with.

The “good news” is that, having started the year with more than sufficient reserves, the charity is not going to end the year in financial difficulty. But, when setting the budget/cash-flow for next year, the Trustees will certainly be wanting to look carefully at why they had under-estimated the charity’s expenditure for the current year.

## **4. Simple is Beautiful ?**

Budgeting and, particularly CashFlow, ISN’T “rocket science” – as it’s sometimes made to appear.

It’s simple and straightforward – something that we all do naturally in the normal course of our lives.

It can become rather tedious and time-consuming when a charity has decided that it wants its receipts and payments broken down into a rather large number of categories.

And it is true that designing a spreadsheet or other accountancy software to do all the calculations automatically requires more than “typical amateur” programming skills.

But, as the Small Charity Support “Simple Accounts System” illustrates, that does NOT mean that any special expertise – particularly external expertise – is required to create and manage cashflows on a day-to-day basis once the appropriate software has been set up.