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Contents

Glossary

Australian Accounting Standards – the Australian Accounting Standards Board's principles that assist the definition and treatment of financial reporting.

accrual accounting – is an accounting method whereby revenue and expenses are recorded in the periods in which they are incurred.

balance sheet (or statement of financial position) – a financial report which represents a snap shot of the assets, liabilities and members' funds as at a certain date.

business activity statement (BAS) – the activity statement that your organisation sends to the Australian Tax Office showing GST information.

cash accounting – an accounting basis that brings items into the accounts when money is physically received or spent.

cash flow statement – a financial statement that shows the amount of cash and cash equivalents entering and leaving a company during the reporting period.

constitution – the name given to the memorandum and rules of an organisation.

current assets – an asset which, in the normal course of business, can be turned into cash within twelve months.

depreciation – a decrease in the original value of an asset because of wear and tear, obsolescence, and deterioration.

director – a person formally elected and/or appointed under law to a Board, in accordance with the organisation's constitution. Note: Some organisations refer to the members of their governing body as management committee members. The term 'director' is used in this manual to refer to both directors and board members and includes management committee members.

disposable – an item not meant for use on multiple occasions.

fiduciary duty – The legal duty to act honestly, in good faith and in the best interests of the organisation.

fixed asset – an asset which, in the normal course of operations, is not expected to be converted into cash in the next twelve months.

fixed costs – costs that do not increase as the volume/activity of your service increases, e.g. rent.

goods and services tax (GST) – a broad-based tax of 10% on most goods, services or anything else for consumption in Australia.

liability – the value of obligations and commitments made to third parties.

current liability – the value of obligations and commitments made to third parties that are due for discharge within twelve months.

insolvency – when an organisation cannot pay its debts as and when they fall due.

net profit – the profit or surplus remaining after expenses.

non-current assets – items that are not expected to be converted into cash within twelve months.

operating profit/surplus – the profit/surplus arising from the organisation's ordinary operations.

pay as you go (PAYG) – a single integrated system for the reporting and paying of:

- amounts withheld from payments to employees and others (PAYG withholding), and
- tax on business and investment income (PAYG installments).

pecuniary – relating to money; financial.

profit and loss – financial report that shows the income and expenditure of the organisation and the resulting Profit (Surplus) or Loss (Deficit) for specified certain period. It is also referred to as the Income and Expenditure report.

ratios – comparison of one item with another, such as current assets/current liabilities, to asses/compare performance

solvent – the organisation has sufficient assets to meet its obligations and commitments as they arise.

standard chart of accounts –a common and consistent way to capture/ record accounting information of items of non-government organisations. The Standard Chart of accounts was designed by Queensland Institute of Technology.

unit costing – a calculation of costs (direct and indirect) associated with the delivery of a unit. (eg. Cost/session, cost/service hour)

variable costs – costs that vary (increase/decrease) when the volume and/or activity of your organisation changes, e.g. fuel costs for a motor vehicle.

variance – the difference between planned and actual of activity / item, e.g. hours, trips, income or expenditure.

written down value (or carrying value) – the value of a fixed asset after depreciation.

About this chapter

As a director you are required to be aware of your obligations and responsibilities in regard to financial management.

This chapter provides you with a practical approach to understanding financial reports and questions that should be asked in order to fulfil your fiduciary duty.

Directors need to receive and understand financial information to support decision making about their organisation. The information in this chapter is based on the Australian Accounting Standards.

Resources and policy checklists are included at the end of this chapter. They can be copied and worked through by your board on an annual basis, or as required.

4.1 Director responsibilities

4.1.1 Introduction

The board is responsible for ensuring that the organisation remains solvent, complies with financial obligations and standards and are financially healthy.

To meet these responsibilities, directors need to:

- be able to read financial reports, be aware of taxation and regulatory requirements and understand compliance requirements
- set financial directions for the organisation
- ensure the organisation complies with financial requirements & Accounting Standards
- monitor and review the finances of the organisation.

As a director of a non-government organisation, you have legal duties in relation to the finances of the organisation. You also have statutory obligations related to your organisation's form of incorporation. There are two main forms of incorporation – Associations and Companies.

4.1.2 Associations Incorporation Act 2009 (NSW)

The legal obligations in relation to the financial responsibilities of directors of incorporated associations under the *Associations Incorporation Act 2009* (NSW) (Associations Act) are:

- ensuring the rules of the Association address how the finances will be managed in accordance with the Act
- ensuring that proper financial records and accounts are kept
- providing an annual financial report to members of the Association
- lodging an annual return with the Registry Service of NSW Fair Trading.

Financial matters to be provided for in the rules

The Associations Act outlines financial matters which are to be included in the rules of an incorporated association. These include:

- fees and subscriptions
- members' liabilities
- the permitted sources of funds (for example, some organisation's rules prohibit receiving funds from alcohol related organisations; other rules describe where funds can be borrowed or invested)
- funds management
- custody of books, documents and securities of the incorporated association
- inspection of books
- the association's financial year.

Tier 1 and 2 associations

Under the Associations Act, associations are grouped into two tiers, Tier 1 Associations and Tier 2 Associations.

Tier 1 associations

Tier 1 associations are associations whose total revenue as recorded in the income and expenditure statement for a financial year exceeds $250,000 (excludes GST) or current assets (defined as assets other than real property and capable of depreciation) exceed $500,000.

Tier 1 associations must prepare financial statements in accordance with Australian Accounting Standards.

The organisation must keep financial accounts that record all financial transactions (receipts and payments), keep track of assets and liabilities and explain the financial position of the organisation.

Tier 1 associations must ensure the financial statements for the association, and any trust for which the association acts as a trustee, are prepared and audited after the association's financial year, for submission to the AGM.

The financial statements must also include details of any mortgages, charges and other securities affecting any property owned by the association.

Tier 1 associations must lodge financial statements within one month after the annual general meeting (AGM).

The association must ensure that the relevant documents are lodged within NSW Fair Trading one month after the AGM which must be held within six months of the end of the financial year unless approval has been granted for an extension of time to hold the AGM.

Tier 1 associations must lodge:

- an annual summary of financial affairs for the financial year
- the financial statements for the financial year as presented at the AGM and the auditor's report
- a copy of any resolution passed at the AGM, concerning the financial statements and the auditor's report.
- a fee prescribed by NSW Fair Trading.

Tier 2 associations

Tier 2 associations are associations whose total revenue as recorded in the income and expenditure statement is less than $250,000 (excludes GST) and current assets (defined as assets other than real property and capable of depreciation) are less than $500,000.

The association must keep financial accounts that record all financial transactions (receipts and payments), keep track of assets and liabilities and explain the financial position of the organisation.

For Tier 2 associations, the statements must give a true and fair view of the association's affairs and must include:

- an income and expenditure statement that sets out detailed income and expenses
- a balance sheet that sets out assets and liabilities
- details of any mortgages, charges and other securities affecting any property owned by the association
- a separate income and expenditure statement and balance sheet for each trust for which the association is the trustee.

For Tier 2 associations, it is not mandatory that these accounts comply with Australian Accounting Standards. However, these Standards provide a guide to good practice in the keeping of financial records.

Tier 2 associations must lodge financial statements within one month after the annual general meeting (AGM).

Tier 2 associations must ensure that an annual summary of financial affairs for the financial year is lodged within NSW Fair Trading one month after. The AGM must be held within six months of the end of the financial year unless approval has been granted for an extension of time to hold the AGM.

The prescribed fee must be paid at the time of lodgment of the documentation.

Trading by an incorporated association

An incorporated association cannot trade or secure monetary gains for its members. However, associations are allowed to undertake certain types of activities without these being considered as trading or securing pecuniary gain for members, such as charging admission fees or client contributions.

Breach of the prohibition of trading or securing pecuniary gain attracts possible prosecution and penalty and cancellation of incorporation.

4.1.3 Corporations Act 2001 (Cth)

Under a company structure, charitable and not-for-profit organisations will generally be registered as public companies that are limited by guarantee.

This means the liability of the company's members is limited to the amount the members undertake to contribute to the property of the company if it is wound up. Organisations limited by guarantee are incorporated under the *Corporations Act 2001* (Cth), administered by the Australian Securities and Investment Commission (ASIC).

If your organisation is a charity it should also be registered with the Australian Charities and Not-for-profits Commission (ACNC).

Overview of financial obligations

Under the *Corporations Act 2001* (Cth) (the Act) companies are required to meet Australian Accounting Standards developed by the Australian Accounting Standards Board (AASB).

If your organisation is a charity registered with the ACNC, your reporting obligations (except for changes to corporate status or changes to auditors) will be to the ACNC instead of to ASIC (refer to section 4.1.4).

Not for profits that are public companies, but are not charities registered with the ACNC, must:

- prepare a financial report including financial statements, directors' declaration and directors' report
- have the financial report audited and obtain an auditor's report
- send the financial report, directors' report and auditor's report to members at least 21 days prior to the AGM or four months after the end of the financial year
- present the financial report, directors' report and auditor's report to the AGM
- lodge the financial report, directors' report and auditor's report with ASIC.

Lodging Reports with ASIC – failure to comply.

A director is guilty of an offence and liable to a penalty, if in regard to documents required by, or for the purposes of the Act, they:

- make or authorise the making of a statement that to the person's knowledge is false or misleading
- leave out, or authorise to leave out, any matter or thing without which the document is to the person's knowledge misleading in any material respect.

4.1.4 Australian Charities and Not for Profits Commission Act 2012 (Cth)

Organisations who are charities, are required to be registered with the Australian Charities and Not-for-profits Commission (ACNC) in order to gain or retain charity tax concessions.

In order to maintain registration, a charity has ongoing obligations to the ACNC including:

- notify the ACNC of certain changes
- report each year by submitting an annual information statement (AIS) – (excluding small charities, see www.acnc.gov.au for a definition of charity size)
- comply with governance standards (except basic religious charities, see www.acnc.gov.au for a definition of basic religious charity)

For some charities, their obligations to the ACNC replace their obligations to other government regulators (for example, charitable companies no longer need to report to ASIC). However, other charities will continue to have obligations to other Commonwealth, state, territory or local government agencies (for example, incorporated associations will continue to have obligations to NSW Fair Trading under the *Incorporated Associations Act 2009* (NSW)).

4.1.5 Accounting standards

Australian Accounting Standards

The Australian Accounting Standards Board develops and issues the Australian Accounting Standards. The accounting standards referred to in this chapter are the Australian Accounting Standards.

National Standard Chart of Accounts (NSCOA)

The Queensland Institute of Commerce and Technology and the Queensland University of Technology (Australian Centre of Philanthropy and Nonprofit Studies and the School of Accountancy) have developed a Standard Chart of Accounts and accompanying data dictionary for use by non-government organisations that receive government funding.

The Australian Charities and Not-for-profits Commission has taken responsibility for management of the NSCOA. Resources are available on their website.

The NSCOA provides a common approach to the capture of accounting information by non-government organisations and aims to make financial data consistent across non-government organisations and across multiple jurisdictions. For this reason the use of the NSCOA is beneficial for organisations who are increasingly operating across multiple jurisdictions.

The NSCOA is an agreed convention for grouping like financial transactions together in reports.

Funding agency financial reporting requirements

Where an organisation receives government funding, a funding agreement will detail the type of financial reporting required by the funding body. The board is responsible for approving and signing this agreement, and must ensure that financial reporting requirements are met.

As a director you should understand the implications of receiving, spending and being financially accountable to the funder for any grants.

4.2 Reading and understanding financial statements

4.2.1 Introduction

Directors are expected to be able to examine and understand the key financial statements and reports of their organisation. A full set of financial statements should be regularly reviewed by the board.

It is important for directors to understand financial statements and to be able to use them to make informed enquiries and decisions about the organisation's business.

4.2.2 Cash and accrual accounting

Financial accounts and statements can be produced on either a 'cash' or an 'accrual' basis.

A 'cash' approach deals with the cash transactions that have occurred within the reported period – that is the actual money has been spent and received in that period. This would include, for example, the money spent: wages and other bills, and money banked: fees and other.

An 'accrual' approach deals with accounting for items as 'earned' or 'incurred' in the reporting period, but for which the cash transactions may or may not have taken place in that period.

For example:

- staff are paid their wages, but they also 'accrue' their entitlements (such as long service leave or holiday leave loading). At the end of any one period, the organisation will owe an amount for these entitlements that staff have 'earned'.
- a service user may have had a service delivered in one period, but under the organisation's payments terms may only be required to pay the invoice in another period. In this instance, under accrual accounting, the organisation has earned revenue in the period the service was delivered.
- similarly, a funding grant, whether this comes from a State or Commonwealth department or from a philanthropic source, may be received, that applies to a future period as well as to the current period. Accrual accounting would show only a part of the grant as income for the current period, the balance would appear in the organisation's balance sheet as a liability (grant in advance).
- under accrual accounting, income received for a future event, say a conference, would be shown as income in the period the event takes place, rather than when the cash is received.

Accrual accounting can provide a fuller, more complete picture of the organisation's financial performance, show a complete financial position of the organisation and help decision makers make more informed decisions.

Cash accounting can be more intuitive and easier for non-accountants to use and understand. However, it may not always provide a full and accurate view of the organisation's performance and can show an incomplete picture of the financial position of the organisation. This may make it harder to understand whether the organisation is solvent.

4.2.3 Profit and loss statements

Profit and loss statements are also known as 'income and expenditure' statements.

These contain information about income and expenses. Examples of items of income could include client fees and charges, fundraising and government grants. Examples of items of expenditure could include salaries, rent and other service delivery and administration costs.

The 'Statement of Comprehensive Income' is a summarised profit and loss statement found in the annual financial statements with more detail provided in the notes to the accounts.

4.2.4 Cash flow statements

A cash flow statement is a summary of information about the movement of actual money – where it came from and where it went.

Cash flow statements include broad items such as:

- income
- payments to staff
- purchase of equipment or vehicles
- petty cash

A cash flow budget or forecast is used to predict how much actual money is available to the organisation to make payments.

4.2.5 Balance sheets

A balance sheet is a snapshot at a point in time of what the organisation owns (assets) and what it owes (liabilities) and includes items such as cash at bank, trade creditors, loans and grants in advance.

Usually the categories are divided into current (can be turned into cash (asset), or obliged to repay (liability) in the next twelve months) and non-current (ability to realise the value (asset), or obligation to repay (liability) is likely to last for longer than twelve months).

Very often, current assets are those where the value is relatively accurately known, while fixed assets tend to be calculated. The value of fixed assets are usually calculated as the purchase cost of the item less depreciation. Land does not depreciate, and land and buildings are usually valued according to market values.

The difference between what an organisation owns and what it owes is called 'equity'. In the accounts equity may also be called 'retained profits' or 'net assets'. Therefore:

equity = assets *minus* liabilities.

Depreciation

Depreciation is the loss in value of a fixed asset over time. Depreciation rates vary depending on the class of asset – the ATO provides guidance on this, see *www.ato.gov.au/Individuals/Tax-return/2016/In-detail/Publications/Guide-to-depreciating-assets-2016/*.

Depreciation accrues across the 'useful life' of an asset – the expense recognised each year adds to the accumulated depreciation (balance sheet account) and decreases the overall value of the fixed assets.

Written down or carrying value = cost of assets *minus* depreciation.

4.2.6 Maintaining accounting records

A manual accounting system may be sufficient for very small organisations, however if there is a large volume of transactions, it will become fairly time consuming to both maintain and prepare reports.

Computer-based systems can automate some aspects of accounting entries and produce a wide range of reports simply.

Organisations should choose an accounting system that meets their individual needs and provides timely, accurate reporting.

> **TIP:** There are many accounting systems available on the market and some have the capacity to integrate with client management systems as well as other reporting and analysis programs. It would be beneficial for your organisation to perform an audit of your internal and external data and reporting needs to explore ways to integrate and streamline the systems your organisation uses.

4.3 Taxation issues

4.3.1 Taxation concessions and exemptions

Not-for-profit organisations are eligible for various taxation exemptions or concessions, depending on the purpose of the organisation and type of activity conducted.

Charities must register with the ACNC to apply for charity tax benefits administered by the Australian Taxation Office (ATO) including:

- income tax exemption and refunds on franking credits
- goods and services tax concession
- fringe benefits tax rebate or exemption
- public benevolent institution or health promotion charity status
- deductible gift recipient status

Note that not for profit organisations that are not a charity (and not registered with the ACNC) are still eligible to apply to the ATO for tax concessions.

Not for profit organisations may also be eligible for exemptions from State government taxes, such as stamp duty (eg. on vehicle purchases, insurance), payroll tax and land tax, as well as local government concessions on rates. For information visit, *www.ato.gov.au*

4.3.2 Goods and Services Tax (GST)

The GST is a 10% tax on most goods and services sold in Australia. It is collected by registered businesses at each step in the supply chain. GST collected, less GST paid, is remitted to the ATO on a quarterly or monthly basis on submission of a Business Activity Statement (BAS).

Non-government organisations with an annual turnover of $150,000 or more must register with the ATO for GST within twenty-one days of the turnover meeting or exceeding the registration turnover threshold.

Organisations with a turnover of less than $150,000 per year may still register for GST. This enables organisations to claim back GST paid for business expenses (e.g. accounting fees) but it will create additional administrative effort – smaller organisations should understand the cost/benefit of ongoing compliance.

All receipts/invoices issued must include the organisation's Australian Business Number (ABN) and state the amount of GST.

In order to claim back the GST paid on business expenses, organisations must hold a valid tax invoice, unless the item equals or is less than $75 (ex GST). A normal receipt is sufficient for these items.

4.3.3 Pay as you go (PAYG) income tax

Organisations must collect and pay tax on wages paid to employees and on payments made to businesses that have not quoted their ABN. PAYG is a system for the reporting and paying of amounts withheld from payments to employees and others (PAYG withholding).

PAYG withholding amounts are reported on the Installment Activity Statement (IAS) and Business Activity Statement (BAS) and withheld amounts are paid to the ATO.

4.3.4 Fringe Benefits Tax (FBT)

Fringe benefits tax (FBT) is a tax payable by employers who provide fringe benefits to their employees or to associates of their employees. FBT regulations are quite strict, and a non-government organisation should obtain advice from an accountant or from the ATO about eligibility for exemption or rebates of FBT.

What is a fringe benefit?

Fringe benefits include rights, privileges or services. The most common fringe benefits are:

- expense payments
- cars
- meals/entertainment
- loans
- housing.

Common exempt benefits

Some benefits exempt from FBT are:

- laptop computers (one per FBT year, 1 April to 31 March, per employee)
- mobile phones primarily used in employment
- in-house health care facilities
- most minor benefits valued at less than $300 where it would be unreasonable to treat the benefit as a fringe benefit.

4.3.5 Cash and accrual reporting

Most charities endorsed by the ATO have the option of reporting their GST on a cash, or an accrual basis.

Under the cash basis, at the end of each BAS period, organisations include in their accounts the amounts they have actually paid or received.

Under the accruals basis, organisations include all income and expenses relating to the period, whether or not they have actually been received or paid.

4.4 Costs and cost behaviour

4.4.1 Introduction

In reviewing the organisation's planning processes for the coming year, Directors must be able to predict the expenses/costs that proposed activities will generate. Directors must therefore have some understanding of different types of costs and the relationship between them.

An understanding of the organisation's costs are a useful management tool:

- for planning services
- for operational efficiency
- to maximise the level of appropriate services to clients
- to identify trends
- for setting prices when operating in a fee-for service environment
- for ongoing viability and sustainability of services
- for informed negotiation.

TIP: Your organisation should ensure that you have a robust, systematic and consistent process to determine and analyse your unit costs and profitability across all activities. The capacity to monitor costs will be particularly important for those organisations registering to provide services under the National Disability Insurance Scheme.

4.4.2 Fixed costs/variable costs

Fixed costs are generally constant costs of operating an organisation e.g office rent/building, insurance.

Variable costs are the costs of the activities or services provided by an organisation which usually vary in proportion to the volume of activity e.g salaries/wages for care workers, support workers, therapists, transport costs to and from client visits.

4.4.3 Calculating total cost

It is important that organisations ensure that costs are covered, especially as the disability service sector transitions from block funding to an individualised funding model under the NDIS (where service users can exercise choice and control over who delivers the services they require).

Directors can calculate the total cost of activities using the following formula:

Total cost = fixed costs + variable costs

Where variable cost = number of people x variable cost per person.

Example:
An organisation that offers transport assistance services has eight regular weekly clients. The average round trip for each client is 20km. The volunteer driver undertakes quarterly training which costs $130 per session. The driver is reimbursed mileage at 25c/km plus $3 for a drink each trip. What should the organisation charge each client given the costs incurred to run the service?

Total cost per week:

Fixed cost (training)	$10	(assuming 13 weeks in a quarter – $130 per quarter)
Variable costs		
20km x 0.25 x 8 trips	$40	
$3 Drink x 8 trips	$24	
Total cost per week	$74	

Cost per client = $74 divided by 8 = $9.25 (remember: organisation has 8 clients per week)

The organisation will have to charge each client a fee of at least $9.25 to break even. If there are other costs (such as administration costs) that need to be covered by activity fees, they will have to charge more.

4.4.4 Allocating costs to activities

Unit based costing is a means of calculating and understanding all the costs associated with the delivery of particular activities and services.

The unit cost formula
At a very basic level, unit cost is the average cost of producing one unit of output. It is calculated by dividing the total cost of a service by the total number of units of output delivered.

For example, an organisation which offers meal preparation services delivers 500 meals for a total cost of $3,000 then the cost-per-unit (meal) is $6.

Unit cost = total cost ÷ total output

It becomes more difficult when allocating costs that have the following characteristics:

- the fixed cost relates to a number of activities (e.g. the cost of running the office, paying insurance for volunteers and paying a coordinator’s salary)
- the fixed cost has “excess capacity” – it could be used more than it currently is (such as the on road costs for a vehicle that is used only 50% of the working week)
- the variable cost is hard to trace to a specific activity (e.g. maintenance costs for the vehicle that may have arisen because of dirt road driving to the homes of a few clients)
- the variable cost includes wastage or administration that is not a true cost of the job.

When calculating the unit cost of a service, organisations should first understand the comprehensive cost of that service. This is calculated by including direct labour costs and other direct costs as well as allocated overheads (indirect costs).

Direct costs can be both fixed and variable.

Direct costs: Fixed direct costs, Variable direct costs
Indirect costs: Overheads

Comprehensive cost of service = Fixed direct costs + Variable direct costs + Overheads

Unit cost of service = Comprehensive cost of service ÷ Quantity of service delivered

Example:
A disability service provider provides a development and life skills training program to a group of clients in a community centre once a week, 50 weeks per year. The centre is rented by the service provider.

- direct costs
  - Fixed: Staff, travel costs and rent of the community centre.
  - Variable: Utilities, meals
- indirect costs (overheads)
  - Head office rent, cleaning, utilities (electricity costs) and insurance costs allocated at an appropriate percentage for the service.
- quantity of service delivered: 1 x 50

> **TIP:** Disability service providers should ensure the pricing of services has been set based on a deep knowledge of the NDIS pricing guide (as prices are currently regulated under the NDIS), the cost of delivering services to service users and external drivers (i.e. understanding of clients' needs, competition from other service providers and the choice and control that service users can exercise in choosing which services to access) to ensure longer-term viability.

The principle of unit costing is applicable across the board to any business.

For specific resources developed for disability service providers, organisations could refer to the Unit costing tool and associated resources available through the Industry Development Fund, *www.industrydevelopmentfund.org.au/adhc-unit-costing-tool-resources*

4.5 Setting financial directions

4.5.1 The board's role in financial planning

The board has an important role to play in setting the directions for the organisation generally. This is done through organisational planning. As part of this process the board needs to also make longer term plans for the organisation's financial health.

In terms of its role in financial planning and management, directors need to consider each of the following:

- maintaining the longer term financial viability and health of the organisation
- the cost of implementing the organisational plan
- the annual operating budget.

Directors should review the organisation's financial plan alongside the review of their strategic and business plans (yearly review/evaluation and a more substantial review every three years) or more often if significant external factors come into play.

4.5.2 Operating budgets

An operating budget is a planning instrument that provides a forecast of assumptions of income and expenses. It is the responsibility of the board to approve the budget prior to the beginning of each financial year.

The budget also enables the directors and senior staff to monitor financial performance over the year.

Where an organisation has multiple funded projects or activities, individual budgets may also need to be developed for each discrete project.

4.5.3 Preparing a budget

Preparing a budget allows directors to see the financial consequences of the strategic business plan and determine whether there will be sufficient income to cover expenses.

Budgets should be prepared each year and should include the timing and the amount of income and expenditure forecasts.

4.5.4 Reviewing the budget

Budget setting should be done annually, and the budget reviewed at least once by the board during the year. At each board meeting, directors should see a profit and loss or income and expenditure report that compares the actual results with the budgeted results.

4.5.5 Cash flow budgets (or cash flow forecasts)

A cash flow budget is a document that needs to be prepared on a regular basis throughout the financial year for review by directors. It describes the amount of cash coming into the organisation and when an organisation has financial obligations. Cashflow forecasting becomes particularly important when income is irregular or unpredictable.

As human services transition to more consumer-centric, market-based models, cashflow management becomes increasingly important for service providers. Revenue will flow via the consumer, in arrears, based on services provided, which differs from the traditional block-funding arrangements organisations were used to.

> **TIP:** The effective management of cash flow is particularly important for organisations moving from a block funded model to fees for service with payments in arrears. Your organisation should ensure that you have a systematic and regular process in place to calculate cash flows. Your organisation should ensure acceptable cash flow levels have been clearly defined and are monitored on a regular basis. Your organisation should also develop and implement clear strategies to improve cash flow levels should they drop below a defined level.

4.6 Monitoring financial performance

4.6.1 Monitoring against the budget

The board should receive and review a profit and loss or income and expenditure report showing actual income and expenditure against the budget on a regular basis.

The report should include:

- planned and actual income and expenditure for the period (eg. month or quarter)
- planned and actual income and expenditure for the year to date (YTD)
- variances – the difference between planned and actual figures
- explanatory notes – explaining why a variance has occurred.

4.6.2 Reviewing financial performance

Review and analysis of financial performance information allows the board to:

- identify trends in the organisation's finances
- manage and understand the relationships between revenue, expenses, assets, liabilities and equity
- use past performance information to make decisions about immediate needs and to plan for the future.

Boards should also consider:

- specific measures of financial performance (ratio analysis)
- trends and changes from one year to another (percentage analysis)
- monitoring cashflow and solvency
- assessing the overall health of the organisation from year to year by analysing the balance sheet.

Some services and/or business streams may require more frequent forecasting than others. Organisations should take particular care at identifying areas of their business that are subject to increased variability and establish processes accordingly.

Analysing the balance sheet

The balance sheet shows the total worth of the organisation (equity). An organisation's equity is the balance of assets held after all liabilities have been met.

Assets minus liabilities = equity

The balance sheet is the key report that confirms the organisation's ability to meet its debts when they fall due. This is determined by the ratio of current assets to current liabilities, combined with understanding the cash needs as set out in a cash flow forecast.

Essential to the monitoring of organisational performance, is the implementation of systems and processes that allow the organisation to capture relevant data and regularly analyse that data. Organisations should ensure IT systems, including accounting and financial reporting as well as Customer Relationship Management (CRM) systems are adequate for the current and future needs of the organisation.

4.6.3 Complying with funding agreements

In monitoring financial performance, the board also needs to ensure that the organisation meets its obligations under any contractual and/or funding agreement(s).

Where an organisation has individual service agreements with their customers (service users), it is important for the organisation to monitor its compliance with contractual obligations under those agreements and that it is able to report information to the individual customers (service users).

Typically this involves:

- ensuring the project or activity is viable
- reviewing and signing contracts and/or funding agreements
- ensuring that the accounts are aligned with the reporting requirements
- monitoring financial performance
- providing progress reports to the funding provider(s) or service users as required
- acquittal of the funds as required
- retention and management of records as required.

References

Australian Accounting Standards Board
Phone: 1300 857 602

Fax: (03) 9617 7608

Email: standard@aasb.gov.au

www.aasb.gov.au

Australian Charities and Not-for-profits Commission (ACNC)
Phone: 13 22 62

Email: advice@acnc.gov.au

www.acnc.gov.au

Australian Securities and Investments Commission (ASIC)
Phone: 1300 300 630

Email: info.enquiries@asic.gov.au

www.asic.gov.au

Australian Taxation Office
Phone: 13 72 26

www.ato.gov.au

Relevant Legislation

Note: note that this is not a comprehensive list of legislation.

NSW Fair Trading
www.fairtrading.nsw.gov.au

Associations Incorporation Act 2009 (NSW)

Commonwealth Legislation
www.comlaw.gov.au

Australian Securities and Investments Commission Act 2001 (Cth)

Corporations Act 2001 (Cth)

Australian Charities and Not for Profit Commission Act 2012 (Cth)

A New Tax System (Goods and Services Tax) Act 1999 (Cth)

Resources

Checklist 1: Financial statements	DIRECTOR'S NOTE
Tick 'Yes' or 'No' to indicate the status in your organisation.	**This checklist should be used by the board annually to review their knowledge of financial statements.**

Questions	Yes	No	Considerations
Do you have access to accurate and up to date information on a monthly, quarterly basis or more regularly (as required)?			You should ensure that your accounts are produced regularly enough to provide you with the information you need for decision making.
Do you know the financial reporting requirements of the organisation's internal and external information users?			You need to decide how detailed and in what format you would like your information presented.
Do you recognise the significance of the major items in your organisation's financial reports and can you assess whether these items are realistic and accurate?			You will need this skill in order to provide input into strategic and operational planning.
How is your organisation incorporated? Are you familiar with the financial requirements of your constitution?			Is it incorporated under the appropriate: • Associations Act • Incorporation Act? • Corporations law? • as a Cooperative? • by statute?
Is the organisation registered with the ACNC?			You will need to be familiar with the reporting requirements under the ACNC Act 2012.
Do you have access to the relevant legislation governing your type of organisation?			It is useful to provide directors with a summary of the main requirements and/or links to the full legislation online.

Questions	Yes	No	Considerations
Does your constitution recognise the board or management sub-committees?			As a director you need to be aware of who has authority to make decisions and how decisions are made.
Does your organisation prepare a three to five year strategic/business plan, an annual budget plan (fixed) and a revised annual estimate (actual YTD and forecast)?			Strategic planning and budgeting are important aspects of governance.
Do you monitor performance against the above?			It is a director's responsibility to ensure that reports are provided to the board that enable them to assess the performance of the organisation against both the budget and the strategic plan.
Is your organisation an employer? Does it comply with all statutory requirements – WorkCover, PAYG, superannuation, holiday and sick leave entitlements?			You need to be aware of the legal requirements in respect of employees.
As part of your risk management do you have the appropriate insurances?			Refer to the insurance section of the chapter on risk management.
Does your organisation have an appointed independent auditor?			An independent auditor who can give a professional and impartial assessment of financial position of the organisation is vital.

Use this template to add any further items you wish to monitor in your organisation. List any areas where you have identified that further action is required.

Checklist 2: Financial statement review	DIRECTOR'S NOTE
This checklist will help you to analyse the financial statements in preparation for your board meetings. Included are considerations for directors in responding to the questions. A blank copy of this checklist is included for your use.	**Included below are points that directors should consider when analysing the financial statements for your board meetings.**

Questions	Considerations for Directors
Balance sheet	
Are total assets greater than total liabilities?	If liabilities are greater than assets, the future financial viability is in doubt.
Are there more current assets than current liabilities?	If not, in the next twelve months how will you cover the shortfall?
Have your debtors increased significantly since the last report?	This could indicate a bad debt or a general slowing of payments in the industry. Cash flow availability could be jeopardised.
Have your creditors increased significantly since the last report?	This might indicate less cash is available to pay obligations. Is the organisation taking longer to pay suppliers?
Is the plant and equipment written down to a very low value?	This might indicate it is due for replacement. Note that this is not always the case – some types of asset may remain in use for longer than the "useful life" for depreciation purposes.
Is all of the cash at the bank available for use?	A portion of this cash may be a compensating balance for security against a bank loan.

Questions	Considerations for Directors
Profit and loss	
Does the bottom line match your budget/expectation?	If not, what are the significant differences and does action need to be taken to control costs or improve income?
Has the type of income you are receiving changed significantly?	This may indicate success/failure of an activity in the period (e.g. sponsorship push).
Has there been a significant change in the level of expenses compared to the previous period?	Will this affect the result for the year? Is there sufficient cash to meet increased expenditure?
Have you paid all expenses for employees?	For example, workers compensation, PAYG and superannuation. Are leave entitlements provided for on the balance sheet?
Statement of cash flows	
Are there significant differences from prior year results in the net cash flows from financial activities?	This review will assist with planning for future years, and will indicate if non-core activities are funding core activities, e.g. sale of equipment has provided funds to operate.
Has there been a significant movement in the cash balance to date?	This might indicate a need to review banking arrangements – possibly excess cash should be placed in term deposits or additional banking facilities arranged.

Checklist 3 Financial statement review:	**DIRECTOR'S NOTE**
This checklist will help you to analyse the financial statements in preparation for, or at, your meetings. Develop actions for any items identified for improvement. Tick in appropriate column. Tick 'Yes' or 'No' to indicate the status in your organisation.	**This checklist may be used at each board meeting when reviewing financial statements.**

Questions	Yes	No	Comments
Balance sheet			
Are total assets greater than total liabilities?			
Are there more current assets than current liabilities?			
Have your debtors increased significantly since the last report?			
Have your creditors increased significantly since the last report?			
Is the plant and equipment written down to a very low value?			
Is all of the cash at the bank available for use?			
Profit and loss			
Does the bottom line match your budget/ expectation?			
Has the type of income you are receiving changed significantly?			
Has there been a significant change in the level of expenses compared to the previous period?			
Have you paid all expenses for employees?			
Statement of cash flows			
Are there significant differences from prior year results in the net cash flows from financial activities?			
Has there been a significant movement in the cash balance to date?			

Director checklist: Responsibilities

Points to remember

Use this checklist to review your understanding of the information within the director responsibilities section.	Tick to indicate understanding: Yes	No	Limited
Common law responsibilities of directors:			
• Financial literacy			
• Setting financial directions			
• Ensuring compliance			
• Monitoring and reviewing			
Associations Incorporation Act (NSW) 2009 **(if relevant to your organisation)**			
• Financial matters to be provided for in the Rules			
• Keeping of accounts and records			
• Annual reporting			
• Lodgment of statement regarding accounts			
• Trading by incorporated associations			
Corporations Act 2001 **(Cth) (if relevant to your organisation)**			
• Prepare financial report			
• Prepare Directors' report			
• Have the financial report audited and obtain auditor's report			
• Send the financial report, Directors' report and auditor's report to members			
• Lodge the financial report, Directors' report and auditor's report with ASIC			
• Presentation of financial report, Directors' report and auditor's report to AGM			

	Tick to indicate understanding		
	Yes	No	Limited
***Australian Charities and Not-for-profits Commission Act* 2012 (Cth) (if relevant to your organisation)**			
Submit an Annual Information Statement			
Comply with ACNC governance standards: • work towards the organisation's charitable purpose • be accountable to members • comply with Australian laws • ensure responsible persons are suitable and not disqualified • ensure responsible persons undertake their duties with care and diligence • adhere to the requirements in your Rules or Constitution regarding meetings and provision of information to members			
Financial reporting:			
• Australian Accounting Standards			
• National Standard Chart of Accounts			
• Funder requirements for financial reporting			
• Schedules of the funding agreement			
• Annual acquittal and or financial reporting requirements			

If you have ticked the 'No' box please review that section again.

Director checklist: Reading and understanding financial statements Points to remember			
	Tick to indicate understanding		
Use this checklist to review your understanding of the information within the reading and understanding financial statements section.	Yes	No	Limited
Identify which financial statements are needed			
Cash and accrual accounting			
Review the organisation's results on the profit and loss statement to help plan for future activities			
Review the cash flow statement to determine if additional funding is necessary			
Understand balance sheet			
Understand depreciation			
Frequency of financial reporting			
Maintaining accounting records			
Limitations of financial statements			
Table any issues that arise from your review and any necessary action determined by the board at the next meeting			
Consider non-financial as well as financial indicators in your organisation and the interaction between the two when reviewing the financial statements			

If you have ticked the 'No' box please review that section again.

Director checklist: Taxation Points to remember			
	Tick to indicate understanding		
Use this checklist to review your understanding of the information within the taxation section.	Yes	No	Limited
The organisation's eligibility for tax concessions or exemptions			
The process for applying for tax concessions or exemptions			
Your obligations for collecting, reporting and forwarding Goods and Services Tax (GST) to the Australian Tax Office			
Sufficient record keeping (e.g. are there checks to ensure that you are receiving tax invoices from suppliers?)			
Evaluate and plan for the cash flow impact of GST on your organisation			
Your organisations obligations in respect of Pay As You Go (PAYG) withholding and PAYG instalments.			
If applicable, that accounting systems are within your organisation to register, record, report on and pay Fringe Benefits Tax (FBT) to the Australian Tax Office			
If applicable, your organisation's obligations in respect of Capital Gains Tax			

If you have ticked the 'No' box please review that section again.

Director checklist: Costs Points to remember			
	Tick to indicate understanding		
Use this checklist to review your understand of the information within the costs and cost behaviour section.	Yes	No	Limited
The relationship between fixed and variable costs and using this to plan for the coming year's activities			
Ensure that the organisation's accounting information is collected and processed to allow the board to identify relevant costs			
The accounting system should be reviewed annually to check that the way costs are allocated and presented shows the true cost of activities			
The relationship between the organisation's service unit costs and the funder's requirements for service outputs as specified in the funding agreement			

If you have ticked the 'No' box please review that section again.

Director checklist: Setting financial directions Points to remember			
	Tick to indicate understanding		
Use this checklist to review your understanding of the information within the setting financial directions section.	Yes	No	Limited
Board role in setting financial directions:			
• longer term financial viability and health			
• relationship between financial plan and the strategic business plan			
• annual budget setting			
New or expanding revenue			
Benefits of an operating budget			
Budget preparation			
Budget review			
Cash flow budget			

If you have ticked the 'No' box please review that section again.

Director checklist: Monitoring financial performance Points to remember			
	Tick to indicate understanding		
Use this checklist to review your understanding of the information within the monitoring financial performance section.	Yes	No	Limited
Contents of a financial report for monitoring against the budget			
Understanding variances			
Methods for reviewing financial performance:			
• ratio analysis			
• percentage analysis			
• analysing the balance sheet			
• complying with funding requirements			

If you have ticked the 'No' box please review that section again.

Appendix 1: Sample documents

Sample profit and loss statement

MyAbility Care for the year ended June 30 XXXX	Past yr ($)	Current yr ($)
Income		
Grant	20,866	20,650
Fees	27,434	26,350
Bank interest	200	300
Total income	48,500	47,300
Expenditure		
Electricity	390	780
Insurance	2,500	2,158
Rent	7,500	8,850
Salary	25,236	25,723
Telephone and internet	3,500	2,675
Training	1,200	850
Vehicle expenses	4,500	4,500
Volunteer expenses	350	275
Total expenditure	45,176	45,811
Profit	**3,324**	**1,489**

Sample cash flow statement

MyAbility Care for the year ended June 30 XXXX	Past yr ($)	Current yr ($)
Cash flows from operating activities		
Receipts – Fees	27,434	24,350
Receipts – Grant	20,866	20,650
Payments to suppliers and employees	(44,826)	(28,521)
Net cash provided from operating activities	3,474	16,479
Cash flows from investing activities		
Payments from plant and equipment	(2,011)	0
Payments for plant and equipment	0	975
Net cash used in investing activities	(2,011)	975
Cash flows from financing activities		
Interest from accounts	200	300
Repayment of loans to associated entities	800	0
Loan to associated entities	–	(1,000)
Repayment of loan to bank	0	(3,304)
Net cash provided from financing activities	1,000	(4,004)
Net increase (decrease) in cash held	**2,463**	**11,500**

Sample balance sheet

MyAbility Care for the year ended June 30 XXXX	Note	Past yr ($)	Current yr ($)
Current assets			
Cash	1	57,100	53,600
Receivables	2	900	900
Loans to associated entities	3	1,000	1,000
Inventories	4	155	740
Total current assets		59,155	56,240
Non-current assets			
Plant and equipment	5	6,400	7,100
Loans to associated entities	6	5,000	6,000
Other assets	7	200	300
Total non-current assets		11,600	13,400
Total assets		70,755	69,640
Current liabilities			
Creditors and borrowings	8	1,600	1,700
Income in advance	9	3,400	1,800
Employee leave provisions		2,600	5,200
Total current liabilities		7,600	8,800
Non-current liabilities			
Bank loan		5,500	2,196
Total non-current liabilities		5,500	2,196
Total liabilities		13,100	10,996
Equity (Net assets)		**57,655**	**58,644**

Sample notes to the accounts

The accompanying notes form part of these financial statements

MyAbility Care for the year ended June 30 XXXX	Past yr ($)	Current yr ($)
1. Cash		
Cash on hand	1,100	1,000
Cheque account	56,00	52,600
	57,100	53,600
2. Receivables		
Debtors	156	200
Prepaid expenses	175	680
Accruals	569	20
	900	900
3. Loans to associated entities		
Loan – Aged Care Activity Group	1,000	1,000
	1,000	1,000
4. Inventories		
Disability aid equipment	155	740
	155	740
5. Plant and equipment at cost		
Plant and equipment	6,750	7,725
Less: accumulated depreciation	350	625
	6,400	7,100
6. Loans to associated entities		
Aged Care Activity Group	5,000	6,000
	5,000	6,000
7. Other assets		
Website development	5,000	5,000
Less: accumulated depreciation	4,800	4,700
	200	300
8. Creditors & borrowings		
Sundry creditors	1,600	1,700
	1,600	1,700
9. Income in advance		
Project funding in advance	3,400	1,800
	3,400	1,800

Sample operating budget format

MyAbility Operating Budget from 1st July XXXX to 30th June XXXX ACTUALS				
Account name	Prior year actuals	Budget	Variance ($ or %)	Assumptions/ Notes
	Fees			
	Donations			
	Grants			
	Other			
	GST Collected			
	TOTAL INCOME			
	EXPENSES			
	Accountancy			
	Bank Fees			
	Training			
	Insurance			
	Repairs and Maintenance			
	Printing Postage and Stationery			
	Rent on land and buildings			
	Salaries			
	Asset Purchases			
	Superannuation			
	Telephone			
	Other Expenses			
	GST paid			
	TOTAL EXPENSES			
	SURPLUS (DEFICIT)			

MyAbility Cash Flow Budget from 1st July XXXX to 30th June XXXX												
	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN
Cash Receipts (A)												
Fees												
Donations												
Grants												
Other												
GST Collected												
Cash in	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Cash Payments (B)												
Accountancy and Audit												
Bank Fees												
Training												
Insurance												
Repairs and Maintenance												
Printing Postage and Stationery												
Rent on land and buildings												
Salaries												
Asset Purchases												
Superannuation												
Telephone												
Other Expenses												
GST paid												
Cash out	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Surplus/Deficit **(A less B or A – B)**	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Closing Bank	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0

Sample Monthly Financial Report

Item Income	Actual for month	Budget for month	Variance for month	Actual for year to date	Budget for year to date	Variance for year to date
Fees						
Donations						
Income (including Grants)						
Other						
GST Collected						
Total						
Expenditure						
Accounting & Audit						
Bank Fees						
Training						
Insurance						
Repairs and Maintenance						
Printing Postage and Stationery						
Rent on land and buildings						
Salaries						
Asset Purchases						
Superannuation						
Telephone						
Other Expenses						
GST paid						
Total						
Surplus or (Deficit)						

Appendix 2: Financial analysis tools

Introduction
This section provides information to support knowledge development, analysis and interpretation of the financial performance of your organisation by using financial and non-financial performance indicators.

What are the benefits of reviewing financial performance?
Review and analysis of financial performance allows directors to:

- identify trends
- manage and understand the relationships between revenue, expenses, assets, liabilities and equity
- take action to ensure viability/manage risk and ensure viability
- use past performance information to plan for the future.

Should you review reports other than the financial statements?
Yes – financial information is an important indicator of an organisation's health and compliance, but it is not the only source of information. The board should also have access to reporting against outcomes, outputs or other performance measures, especially those required under contractual obligations.

Ratio analysis
A ratio is the comparison of one item with another. The table on the following page includes examples of ratios that might be used to analyse the financial status of an organisation.

One or two ratios that help to quantify progress in achieving key financial targets for the particular provider can be useful.

Examples of Ratios

Ratio	Calculation	Indication
Accounts receivable days	This is the average number of days that your customers/ clients take to pay accounts/ fees.	This has a direct effect on working capital, i.e. how much money you have available to run the organisation from day to day.
Operating margin	Calculated by dividing the profit by the income.	The lower the margin the greater the risk of going into loss. I.e. should income from subsidies/fees is reduced or costs increase.
Interest cover	Calculated by dividing the earnings before interest and taxes by the annual interest charges.	This ratio provides a measure of the ability of the business to service its interest debt.
Debt to equity	Calculated by dividing the total debt in the business by its equity (assets minus liabilities).	This ratio measures financial gearing or the extent to which external parties own the provider's assets
Current ratio	Calculated by dividing current assets by the current liabilities.	This ratio measures the capacity to meet short term (within twelve months) financial commitments.
Quick/Acid test ratio	Current assets minus inventory divided by current liabilities minus overdraft.	This ratio gives guidance as to the ability of an organisation to use near-cash assets to meet short term/current liabilities.

Examples:

Accounts Receivable Days:

$$\frac{\text{Accounts receivable from activity x 365}}{\text{Annual income from activity}}$$

e.g.

Client Fees are: $9,000

Outstanding Client Debtors are: $1,210

$\frac{1{,}210 \times 365}{9{,}000}$	= 49 days

In other words it takes forty-nine days on average for fees to be physically received by the organisation from clients who have received a service. Note that under the NDIS, payments for electronic claims are made within two days of submission while payments for paper invoices are made within thirty days of submission.

See http://www.ndis.gov.au/

Operating Margin:
This ratio indicates if overheads are being maintained at an acceptable level relative to income.

$$\frac{\text{Total operating expenses – interest expense}}{\text{Income}}$$

Percentage analysis

This analysis simply involves working out the percentage change from one year to the next of income and expenses. It is most efficient to perform this analysis using computer-based templates but the calculations can often be prepared by hand fairly quickly. The percentages used can be tailored to the organisation.

Sample percentage analysis

MyAbility Care			Percentage analysis		
	This yr ($)	%	$ Chg	Last yr ($)	%
Income					
Fees	27,434	56.56%	3,084	24,350	53.75%
Grants	20,866	43.02%	216	20,650	45.58%
Bank interest	200	0.41%	–100	300	0.66%
Gross profit	48,500	100%	3,200	45,300	
Less: expenses					
Electricity	390	0.80%	–1,190	1,580	3.49%
Insurance	2,500	5.15%	342	2,158	4.76%
Volunteer expenses	350	0.72%	75	275	0.61%
Vehicle expenses	4,500	9.28%	300	4,200	9.27%
Rent	7,500	15.46%	650	6,850	15.12%
Training	1,200	2.47%	350	850	1.88%
Telephone	3,500	7.22%	825	2,675	5.91%
Wages and salaries	25,236	52.03%	–487	25,723	56.78%
Total expenses	45,176	93.15%	865	44,311	97.82%

Disability service provider financial ratios

As the National Disability Insurance Scheme (NDIS) rolls out, it will be particularly important for organisations providing disability services to have an understanding of tools for financial analysis. Below are some ratios which may assist with understanding and assessing financial performance when transitioning to the NDIS.

Ratio	Calculation	Indication
Months of Spending Ratio	This is calculated by subtracting Current Liabilities from Current Assets and dividing this figure by Total expenses less Depreciation, then multiplied by twelve. OR (Current Assets – Current Liabilities) / (total expenses – Depreciation) x 12	This ratio provides an assessment of the ability of the organisation to immediately support NDIS transition from payments in advance to payments in arrears. A minimum of three months is highly recommended.
Disability Revenue Concentration Ratio	Divide revenue received from current block funded disability services from Government agencies by Total revenue. OR Disability Revenue / Total Revenue	This indicator will help assess the reliance of the organisation on public disability funding, which will be impacted by the NDIS.
Government Revenue Concentration Ratio	Divide revenue received from Government agencies by Total revenue. OR Government Revenue / Total Revenue	This indicator will help assess the reliance of the organisation on public funding. This ratio could be used to analyse the need to potentially diversify revenue, in order to reduce reliance on government funding.

Non-financial performance indicators

Organisations often have goals and objectives that cannot be measured by assessing financial performance. The achievement of these goals must be measured and often non-financial performance indicators are reported alongside financial performance indicators.

These indicators include:

- growth in client base
- client satisfaction and quality assurance
- activities meeting identified community needs.

Developing a set of key performance indicators (KPIs)

The indicators chosen should be easy to prepare, relevant to the organisation's goals and allow comparison to budgets and/or prior periods. An example of some indicators that might be included in a report is below:

	This year	Last year
Client base growth	12%	4%
Average client age	65	58
Operating margin	41%	45%
Client satisfaction	75%	85%
Debtors days	25	45
Gross profit on services	25%	5%

Appendix 3: Exercises

Exercise 1: Fixed and Variable Costs

Instructions
Categorise the following costs into Fixed and Variable. What reasons did your board have for making this decision? Please tick the appropriate column:

Item	Fixed	Variable	Reasons
Using plant and equipment			
Standard wages			
Board expenses			
Computer software			
Insurance for directors			
Office stationery			
Rent for office			
Using a vehicle			
Client and volunteer social event			
Superannuation			

Note: An alternative exercise might be to review and analyse your organisation's expenditure for the previous year.

Responses to this exercise are located in Appendix 4.

Exercise 2 Balance sheet or profit and loss items?

Instructions

The aim of this exercise is to categorise the following items into balance sheet (asset or liability) or profit and loss (income or expense).

	Balance sheet		Profit and loss		Explanations
	Asset	Liability	Income	Expense	
Insurance					
Superannuation					
Term deposit					
Gardening tools					
Client fees received					
Client fees in advance					
Sales income					
Office furniture					
Postage					
Sponsorship					
Cash at bank					
Depreciation					

Exercise 3: Assessing financial risks

You are a director of an organisation that is considering expanding their service offering in a new location. Management staff have prepared a submission and as a director you have been asked to make comment on it from a financial risk perspective. What are the factors you would consider in making your recommendation?

Suggested responses to this exercise are located in Appendix 4

Appendix 4: Responses to exercises

Exercise 1: Fixed or Variable costs?

Item	Fixed	Variable	Reasons
Using plant and equipment		Y	Varies according to volume of use
Standard wages		Y	Varies according to wage changes and staff changes
Board expenses		Y	Varies according to number of board meetings, volume of board business
Computer software	Y		Capital items
Insurance for directors	Y		Fixed annual amount
Office stationery		Y	Varies according to office need
Rent for office	Y		Fixed contract
Using a vehicle		Y	Varies according to use
Client and volunteer social event		Y	Varies according to number of people involved
Superannuation		Y	Varies according to wages

Exercise 2: Balance sheet or profit and loss items?

Instructions
The aim of this exercise is to categorise the following items into balance sheet (asset or liability) or profit and loss (income or expense).

	Balance sheet		Profit and loss		Explanations
	Asset	Liability	Income	Expense	
Insurance				√	Normally this would be an expense.
Superannuation				√	If you owed super for employees (i.e. you had not sent it to the super fund), super might be in your accounts as a liability.
Term deposit	√				
Gardening tools	√				If these were of low value and essentially disposable, they would be an expense. If they were of greater value and would last a number of years, they would be an asset.
Client fees received			√		
Client fees in advance		√			If fees were non-refundable, the fees would be classed as income. If the fees were refundable they would be classed as a liability.
Sales income			√		
Office furniture	√				
Postage				√	
Sponsorship			√		
Cash at bank	√				
Depreciation				√	
Accumulated depreciation	√				This category sits next to plant and equipment and other fixed assets and could be considered to be a negative asset. It is the total of the depreciation expensed since your organisation purchased the equipment. The accounts show the original cost of the equipment, which is then reduced by the accumulated depreciation to give a final written down value for the equipment.

Exercise 3: Financial risk assessment

Key elements which a director should consider in reviewing a submission to ensure financial viability include:

- Capacity of the organisation
  - Human resource expertise:
    - do you have people with the skills to undertake this service?
    - how do you recruit them?
    - how do you train them?
    - how do you ensure they have/retain the competency to undertake the work?
  - Financial Capacity – does your organisation have the financial resources required to undertake this? Has a cost analysis been done and the unit cost established?
- Is the scope of the organisation's systems, processes, policies and assets sufficient to meet the requirements? If not, has allowance been made in the estimates to provide for the additional cost?
- Does the organisation have the knowledge of the, local area, target groups, and the needs of the particular community so that they are able to deliver an efficient and appropriate service?
- Has consideration been given to special needs groups in that location? Any additional costs this may entail should also be factored into the unit cost.