

Budgets in Not-for -Profits

Where are my dice?

A Budget

- A formal written statement of management's plans for a specified future time period, expressed in financial terms
 - The most common is 1 year
 - Continuous budgets add a future period as each period ends
 - Length depends upon the decision and the ability to provide reliable estimates of future performance
- Primary means of communicating agreed upon objectives to all parts of the Organization
- Promotes efficiency
- Control device
 - Important basis for performance evaluation

Benefits of a Budget

Planning dimensions

- Forces managers to plan and formalize goals
- Improves communication and coordination between the parts of an organization
- Results in greater management awareness of the entity's overall operations and the impact of external factors

Benefits of a Budget (continued)

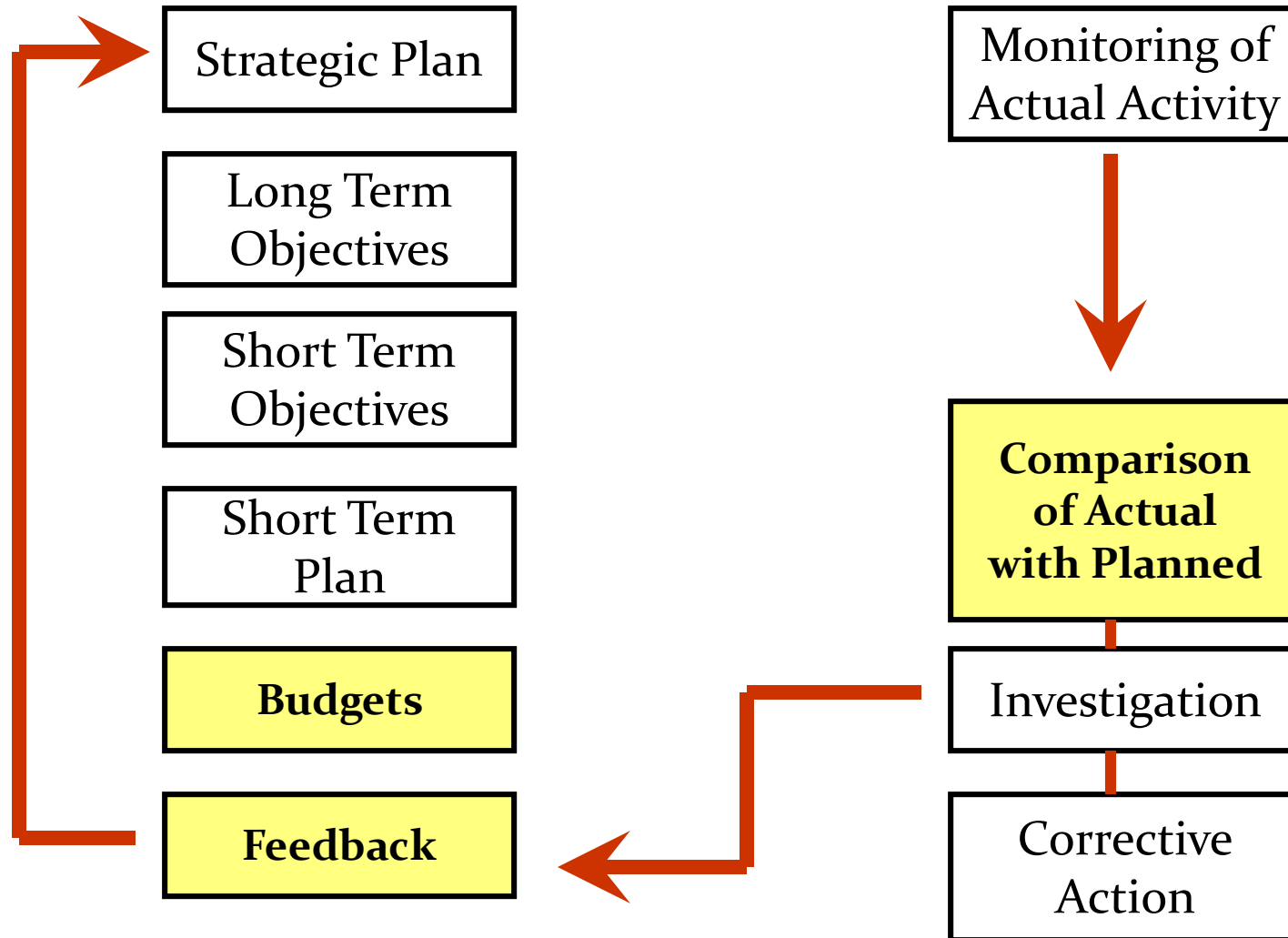
Control dimensions

- Provides definite objectives for evaluating performance at each level of responsibility
 - Improves the use of resources and employees by setting benchmarks
- Creates an early warning system for potential problems
- Motivates personnel throughout organization to meet planned objectives

Two Aspects of Control

- Influence manager's decisions through performance evaluation and responsibility accounting
- Identify cause of a difference and take corrective actions when appropriate

Planning, Control and Effective Budgets



Who is responsible for a budget?

- Planning and control are management activities
- Budgets are the responsibility of management
- Boards Participate in budget development usually at the strategic level
- Variances and changes monitored by boards as part of their fiduciary responsibility

The Reporting System

- Has to provide information to management decision makers
 - Many ways how this is accomplished but primarily through financial statements and schedules
 - Management reports so not as subject to accounting principles

Types of Budgets

Budgets tend to be in three broad general categories.

- Operating – day to day operations
- Capital – Purchase/sale/retirement of long-term assets
- Cash – planning for cash flow fluctuations

Typical Operating Budget

Budgeted (Pro-Forma) Income Statement supported by the following detailed schedules

- Revenue budget that may include sales if you sell things
 - Developed from the revenue (or sales) forecast
- Program budgets
 - Developed in part from the revenue budget
- Yields the following:
 - Program materials budget
 - Labour budget
 - Overhead budget (including Depreciation and occupancy)
 - May include Cost of Goods Sold if you have sales
 - Administrative expense budget

Typical Capital Budget

Budgeted (Pro-Forma) Balance Sheet Items

- Any long-term physical asset
- Developed from a forecast of needs
- May include financing but that is usually in the cash budget

Typical Cash Budget

Cash budget is about timing

- Cash receipts
- Cash disbursements
- Financing (if receipts and disbursements do not coincide or long-term assets are purchased)

Making a Budget

- Budgets tend to be developed at a high level of detail. This is usually each functional line in each program.
- Basically, if you have a schedule in the financial statements, it will have a budget line for every line in it.
- Generally, you will look at a couple of prior years data, a forecast of the current year and then try to determine the next year
- You build in any changes that you know about and document them
- Boards tend to want more summarized material at a program level, but may require the schedule back-up.

Accounts

- An individual accounting record of increases and decreases in a specific asset, liability, or equity item
- All accounts in the organization known as the Chart of Accounts
- Account level information is the starting point for budgets and statements

Chart of Accounts

- Has to be designed to support the type of statements you want
- For the Statement of Financial Position there will be one (or more) account(s) for each line in the statement
- For the Income Statement it will be for each level of detail. For example, if you want to do a Program based Statement with Schedules it will be at the line-item level of the schedules.
- In all cases it has to be at the level of most detail

Cash Budget

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Operating Budget Example

Operating Budget Program 1					
Revenues		2019	2020	2021	2022
Direct Donations		1,000	1,125	1,055	1,100
Grants		45,000	45,000	45,000	42,000
Other		350	344	570	375
Total Program Revenue		46,350	46,469		43,475
Expenses					
Program supplies		750	777	785	790
Salaries		44,000	44,850	45,750	46,650
Benefits		4,400	4,934	4,120	4,665
Rent		7,500	7,500	7,600	7,600
Utilities		850	888	890	900
Depreciation		1,200	1,200	1,200	1,200
Total Program Expenses		58,700	60,149	60,345	61,805
Surplus (deficit)		-12,350	-13,680	-60,345	-18,330

Operating Budget Example

Operating Budget Program 2					
Revenues		2019	2020	2021	2022
Direct Donations		3,600	4,050	3,800	3,960
Grants		192,000	192,000	192,000	195,200
Other		1,260	1,238	2,040	1,350
Total Program Revenue		196,860	197,288	197,840	200,510
Expenses					
Program supplies		2,700	2,797	2,825	2,844
Salaries		158,400	161,460	164,700	167,940
Benefits		15,840	17,761	14,825	16,794
Rent		27,000	27,000	27,360	27,360
Utilities		3,060	3,197	3,205	3,240
Depreciation		4,320	4,320	4,320	4,320
Total Program Expenses		211,320	216,535	217,235	222,498
Surplus (Deficit)		-14,460	-19,246	-19,395	-21,988

Operating Budget Example

Operating Budget Admin and General						
Revenues			2019	2020	2021	2022
General Donations			145,600	125,665	155,000	165,000
Grants			25,000	25,000	19,000	30,000
Other			7,688	7,723	6,635	7,000
Total Program Revenue			178,288	158,388	180,635	202,000
Expenses						
Office Supplies			1,926	1,995	2,015	2,029
Salaries			112,987	115,170	117,480	119,792
Benefits			11,299	12,669	10,575	11,979
Rent			19,259	19,259	19,515	19,516
Utilities			2,183	2,280	2,285	2,311
Depreciation			3,081	3,081	3,080	3,081
Total Program Expenses			150,735	154,454	154,950	158,708
Surplus (Deficit)			27,553	3,934	25,685	43,292

Operating Budget Example

Operating Budget Total						
Revenues			2019	2020	2021	2022
General Donations			150,200	130,840	159,855	170,060
Grants			262,000	262,000	256,000	267,200
Other			9,298	9,305	9,245	8,725
Total Program Revenue			421,498	402,145	425,100	445,985
Expenses						
Office Supplies			5,376	5,569	5,625	5,663
Salaries			315,387	321,480	327,930	334,382
Benefits			31,539	35,363	29,520	33,438
Rent			53,759	53,759	54,475	54,476
Utilities			6,093	6,365	6,380	6,451
Depreciation			8,601	8,601	8,600	8,601
Total Program Expenses			420,755	431,137	432,530	443,011
Surplus (Deficit)			743	-28,992	-7,430	2,974

Capital Budget Example

Sample Capital Budget						
Program 1						
Capital Item 1					Notes	
Funding			45,000	Grant from foundation		
Expenses						
Cost of item			42,000	Purchase from XYZ Company		
Freight			2,000			
Duty and Tax			1,000			
			45,000			
Expected useful Life			6 years			
Salvage value at end of life			1,000			
Change to Depreciation			7,333			

Cash Budget Example

Sample Cash Flow Estimates														
	January	February	March	April	May	June	July	August	September	October	November	December	Total	
Cash Inflows														
Donations	30,000	20,000	70,000	30,000	25,000	65,000	25,000	20,000	30,000	75,000	45,000	125,000	560,000	
Grants	125,000	125,000	145,000	125,000	175,000	145,000	125,000	125,000	145,000	125,000	125,000	145,000	1,630,000	
Other	4,500	4,000	3,700	5,500	2,200	4,000	1,500	1,800	2,000	3,000	4,500	6,000	42,700	
Total	159,500	149,000	218,700	160,500	202,200	214,000	151,500	146,800	177,000	203,000	174,500	276,000	2,232,700	
Cash Outflows														
Supplies	6,000	5,000	5,500	4,500	4,000	3,500	3,000	3,000	3,500	4,000	4,500	5,000	51,500	
Salaries and Benefits	144,000	144,000	144,000	144,000	144,000	144,000	144,000	144,000	144,000	144,000	144,000	144,000	1,728,000	
Capital Items	0	0	0	50,000	0	0	0	0	0	0	0	0	50,000	
Other	35,000	34,000	34,000	32,000	30,000	29,000	34,000	35,000	32,000	33,000	35,000	40,000	403,000	
Total	185,000	183,000	183,500	230,500	178,000	176,500	181,000	182,000	179,500	181,000	183,500	189,000	2,232,500	
Net Cash	-25,500	-34,000	35,200	-70,000	24,200	37,500	-29,500	-35,200	-2,500	22,000	-9,000	87,000	200	
Line of Credit Balance	-25,500	-59,500	-24,300	-94,300	-70,100	-32,600	-62,100	-97,300	-99,800	-77,800	-86,800	0	0	
Do not include depreciation.														

After Approval

- Budgets tend to be set near the end of one year for the next year and things can change
- Industry uses a concept called flexible budgeting that looks at unit sales prices and unit costs as the budget and adjusts up or down for volume changes.
- Although it can be, that is usually not applicable in many not-for-profit so what can you do?

After Approval

- You likely must live within your means, but it does not mean that you can't shift resources from one program to another. (revenues or expenses) Make sure the board is onside with that concept.
- Interim budget revisions can be done and presented/approved by the board.
- If a deficit is looming, make sure the board is aware of it and a plan to fund the deficit in subsequent years or from reserve funds is in place and approved.

Back to Control – Evaluating Performance Using Variances

	Actual Results	Budget Results	Budget-Actual Variances
Revenues	\$217,000	\$279,000	\$62,000 U
Variable costs	<u>152,600</u>	<u>196,200</u>	<u>43,600 F</u>
Margin	\$ 64,400	\$ 82,800	\$18,400 U
Fixed costs	<u>70,000</u>	<u>70,000</u>	<u>–</u>
Operating income	\$ (5,600)	\$ 12,800	\$18,400 U

Evaluating Performance Using Variances

- The difference between actual and budgeted
- **Unfavourable** variances
 - Actual amount paid or used is greater than budgeted
 - Impact on bottom line is negative
- **Favourable** variances
 - Actual amount paid or used is less than budgeted
 - Impact on bottom line is positive

Evaluating Performance Using Variances

Actual
Costs
&
Revenues



Expected
Costs
&
Revenues

How should they be compared?

Interpretation & Use of Variances

- Why might actual performance differ from expected performance?
- What triggers a decision to investigate?
- When is a variance significant?
- What are the consequences of not meeting the budget?

Interpretation & Use of Variances

- Management by Exception
 - Materiality
 - Cost vs. benefit
 - Impact on bottom line
 - Often rules of thumb such as “investigate all variances exceeding \$5,000 or 25% of expected cost whichever is lower”
- Controllability

Interpretation & Use of Variances

- Responsibility Accounting
 - Identify responsibility
 - Controllable versus non-controllable
 - Cause
 - Appropriate corrective action
 - Feedback for future planning

Questions

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