

## 8. Managing money

### 8.2 Setting a budget

#### **What is a budget?**

A budget is a plan translated into money-terms for a defined period of time, usually 12 months from April to March or January to December.

#### **What is the budget for?**

Setting budgets is an essential part of strategic planning. The budget is prepared after the organisation has clarified its aims and objectives and produced a variety of action plans to achieve them. The purposes of a budget are:

- To co-ordinate different activities (departments) towards a single plan.
- To communicate and set targets.
- To maximise and allocate resources.
- To identify financial problems.
- To establish a system of control by having a plan against which actual results can be compared.
- To compel planning.

#### **Who is responsible for the budget?**

The voluntary management committee is guided by the Treasurer and the Finance sub-committee (if there is one) and has the responsibility of agreeing the budget for the organisation. The budget must be approved in advance of its implementation.

#### **What are the key decisions to be taken when setting a budget?**

##### **Does the budget have to be balanced?**

- A balanced budget is one that creates no surplus or loss (deficit). A surplus, for example, will help accumulate reserves. Conversely, sufficient reserves might allow a period of temporary deficit.

##### **How will accountability be allocated?**

- Accepted practice is to identify 'budget holders'; individuals responsible for delivering services with subsidiary budgets attached.

## **What will happen if the budget is thrown off course during the year?**

- It is wise to develop a reserve or contingency budget to cover unforeseen costs during the year.

## **What does a management committee need to do to oversee the budget?**

The voluntary management committee should set regular financial review meetings and ask for regular financial reports to ensure activities are staying within budget. It should ask for explanations of significant variations between the original budget and actual performance, with recommendations for action.

## **What is the budgetary process?**

Budgeting in most organisations is a cyclical activity revolving around the financial year with:

- Treasurer or finance officer providing budget holders with a plan and budget worksheets six months before the budget is due to start.
- Budget holders then compile the respective budget for their activity and return to the finance officer responsible.
- Treasurer or finance officer compiles these into a master budget.
- Senior management reviews this then seeks approval from the management committee.

In smaller voluntary organisations this activity is usually informal.

## **What does a budget look like?**

A basic budget is an estimate of income and expenditures for the next year in table form. Each line is an authorisation to spend or a target to achieve. Some columns break this down into shorter time periods, e.g. quarters, and others allow for actual figures to be included at the end of each period.

## **What is involved in preparing and presenting a budget?**

For small organisations a single budget will probably suffice. Larger or more complex organisations may need to develop a master budget from which a series of subsidiary budgets are derived. In addition to a master budget an additional cash flow budget will be required. This identifies expected outflows and inflows and, by comparing this against what actually happens, organisations can anticipate problems and take early action to deal with them.

The budget and specific items within can vary over the year. A fixed budget gives only one estimate of income and expenditure at one level of activity. A flexible budget identifies items around which the level of activity might vary, e.g. units sold or cases handled, and provides alternate figures for each level.

## **What is forecasting?**

Forecasting is a process that requires asking simple but practical questions such as *'it cost this much last year but how much will it cost next year?'* Forecasting can include an analysis of the strengths and weaknesses of income sources. Timing differences between receipt of income and payment of expenditure are also a consideration.

A healthy financial picture overall might disguise cash flow problems at particular times that will require preventative action, e.g. bridging loans or negotiation with funders.

## **How should information from previous budgets be treated?**

When a budget item follows on from a previous year there are two choices:

- Arrive at an updated figure by applying a percentage increase (incremental method).
- Re-calculating the item (zero based method).

While the incremental approach can lead to inaccuracy, applying a zero based approach to all items may be extremely time consuming. An assessment should be made as to the best balance between these approaches.

## **What is necessary for monitoring and reporting on the budget?**

Normally the Treasurer or finance officer will make regular comparison of actual results against the budget. This information is reported to 'budget holders', managers with responsibility for a part of the overall budget. Budget holders can then either take corrective action or be reassured that everything is going according to plan. Finance officers and budget holders should make regular reports to the voluntary management committee.

## Further information

Charity Finance Director's Group

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