



What is Financial Management?

Financial management is about ensuring funds are available when needed and that they are obtained and used in the most efficient and effective way to the benefit of an organisation. Used appropriately, financial management tools can help an organisation to deliver its mission better and to ensure the best and most beneficial use of resources.

Integrating financial with organisational planning

At its most effective, financial management is a core element of an organisation's wider strategic planning.

Time and again financial management ends up being divorced from wider organisational planning and management. This can lead to less effective use of resources. Worse still, failure to link financial management into wider organisational plans can lead to funding problems that, had they been planned for an effectively managed, could have been foreseen and avoided. This can often be the case in smaller or less well-resourced organisations where the finances are managed by a single, frequently part-time, staff member or volunteer. Pressures of time together with an organisational view of the finance worker as "someone who comes in to do the books" can limit the potential effectiveness of an organisation's finance function to monitoring historical information rather than planning for the future.

For example, imagine that a VCO (Voluntary and Community Organisation) has been asked to expand an advice service to young people. The Local Authority agrees to fund the expanded service with a contract covering all the increased costs of £40,000. However, the contract says that payment will be quarterly in arrears and subject to a quarterly usage report.

Question— What are the implications for the organisation of this contract?

Answer— although all costs are to be met, in reality there are very serious consequences implied in the condition of payment of arrears. In essence it is likely that the organisation will not receive payment until the end of each quarter. Worse still, it is most likely, given a report has to be completed, sent in, approved and then a payment order generated in the Local Authority, that it will be more like five months before the organisation is paid any money. This means that nearly half the costs (£20,000) will have been incurred by the organisation before it receives payment.

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Has the organisation sufficient funds in its bank account to cover these costs before receiving the funds? If not how will it cover these costs—with a bank overdraft? But this will mean interest and bank charges. Has the Local Authority agreed to pay these costs?

Even assuming there is sufficient cash in the bank account, this money may have been earning interest that will now be lost. This is a cost in itself. If the organisation is also a registered charity there are also potential implications relating to whether restricted funds meant for another purpose may now be being illegally used to fund the advice service until payment is received.

The final issue raised from this example is the report. Has the VCO the systems in place to capture this information? There will also be a cost to recording and supplying this information—have these costs been covered?

The consequences of bad financial management are therefore very serious. Good financial management requires sound organisational planning and the set-up and implementation of workable systems, policies and procedures which can respond to, accommodate and overcome the financial challenges a VCO may face.

Planning can be defined as the establishment of objectives and the formulation, evaluation and selection of the policies, strategies, tactics and action required to achieve these objectives.

Developing a financial strategy

A financial strategy is a plan that sets out how an organisation will finance its development, identifies what funds are required, and from where they will be sourced.

Even for smaller groups, considering future financial need is beneficial.

These benefits include;

- ◆ Monitoring the viability of the organisation
- ◆ Ensuring resource needs are correctly identified
- ◆ Enabling the organisation to make informal decisions on new initiatives and opportunities
- ◆ Being able to identify potential risks
- ◆ Helping identify contingency requirements
- ◆ Allowing organisations to approach funders, purchasers or banks with confidence.

Knowing what funds are needed can help an organisation consider what may be the best ways of funding its work.

A financial strategy will also highlight the need to develop new, or expand current financial systems to accommodate future work or organisational growth.

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Establishing financial policies, procedures and systems

Financial systems are the series of tasks and procedures by which a VCO's monetary transactions are processed and their financial records are created.

The important thing is to establish workable financial systems as early as possible. These can evolve or change, but a system of some sort should be in place so that everyone can understand how the organisation's finances should be managed and what their responsibilities are. Systems enable VCOs to see where issues may be arising and take action to mitigate any problems. They facilitate reporting to funders and transparent accountability to beneficiaries and wider stakeholders.

Summary—What is financial management?

- ◆ Ensuring that funds are made available at the right time, for the right length of time, at the lowest cost and used in the most efficient and economical manner.
- ◆ Financial planning should be integrated with the core organisational planning
- ◆ A financial strategy helps an organisation consider how future work will be funded and plan for development

Tool—Developing a financial strategy

Essentially the document should contain information on :

- ◆ **Where the VCO is now**—current financial commitments and objectives
- ◆ **What the VCO plans for the future**
- ◆ **How much it will cost**—how will the organisation finance its plans?
- ◆ **How the VCO will manage the process and minimise risks.**
- ◆ **Integration of financial strategy with other organisational strategies**—Has the VCO been objective in the planning process? Are current strategies working?

Use these headings to map out a financial strategy.