



**AFRICAN MEDICAL RESEARCH FOUNDATION TRAINING
MANUAL ON THE UNIT STANDARD: *Manage finances of a
new venture*: ID No: 114586: Credits: 5**

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Manage finances of a new venture

Outcomes	Notional Hours
1. Open and operate a banking account for own business	8
2. Explain the financial aspects involved in running a business	8
3. Establish accounting systems	8
4. Analyse the elements of an income and expenditure statement	8
5. Analyse a balance sheet	8
6. Use the evidence in financial statements to make a financial decision	10
Total Notional Hours	50 Hours

Specific Outcome 1: Open and operate a banking account for own business

Mode of delivery	Assessment	Assessment instrument
Classroom presentation	Oral and written questioning	Written assignments/Tests

In terms of the Non Profit Organizations Act 71 of 1997 all non-profit organization registered in terms of section 13 Act are required to meet government’s requirements for registration. One of these requirements is that the organization’s financial transactions must be conducted by means of a banking account. Every registered non-profit organization is by law required to adhere to the standards of generally accepted accounting practices i.e.

- It must keep accounting records of its income, expenditure, assets and liabilities
- It must within 6 months after the end of its financial year draw up its financial statements (i.e. A statement of income and expenditure for the financial year ending and a balance sheet showing its assets and liabilities

Without operating a bank account any non-profit organization would not be registered as it would not meet legal requirements of registration. Without a bank, it is also very difficult to keep track of the financial transactions of the organization. Banks offer non-profit organizations a variety of accounts from which they can chose. The decision of which type of account the organization uses is an important choice to make. There are different types of accounts to be used, each one of them with its own advantages and disadvantages

Savings Account

It is an ordinary savings account at a bank/building society with a credit balance, which means that you have money available to use. Interest is paid to a credit balance and the account may not be overdrawn (debit balance).

Advantages

- Income can be deposited directly into the savings account.
- Fairly inexpensive account - minimum costs involved with withdrawal.
- Interest is paid to credit balance.
- Teller cards linked to account are obtained.
- Debit order and stop order facilities are available.

Disadvantages

- Has no overdraft facilities; may not "borrow" money against the account.

Current Account

This is a current account linked to a cheque book. This account has many advantages but is expensive. The screening in order to obtain a cheque account is strict and income, expenditure are checked before the cheque account is approved.

Advantages

- Easy way to pay something for the cheque serves as proof of payment and cash is not used.
- Overdraft facilities are available and money may be "borrowed" against the account.
- Debit order and stop order facilities are available.

Disadvantages

- The expenses incurred by using cheques are recoverable which makes this type of account very expensive.

Learners are expected at this stage to have collected flyers in commercial banks which explain what the different accounts entail and details the requirements of each account. The facilitator will provide the learners with a sample of bank statement.

Interest rates

Interest rates are the rate of compensation agreed between borrowers and lenders of money. Commercial banks act as intermediaries between savers (depositors) and borrowers. Commercial banks cannot however lend out all their available funds because they are required by law to keep some of their funds in cash to meet the demands for payment by depositors. The percentage of cash to be held (i.e. also called the reserve requirement) is determined by the central bank. The central bank attempts to control the money supply by means of a monetary policy. The central bank does not only enforce a certain reserve requirement, it also:

- Acts as a lender of the last resort to the banking sector and influences interest rates by raising or lowering the rate at which it lends money to commercial banks (this is known as the repo rate/minimum lending rate)
- Reduces the level of money supply in the economy by issuing treasury bills which absorb some of the money in circulation
- Rediscounts bills and other short term instruments on behalf of commercial banks
- Acts as the government's banker by managing the country's gold and foreign reserves

Any financial manager must establish whether interest rates are expected to increase or decrease during the period under consideration and if so what will be the impact on the economy. Lower interest rates result in improved consumers' disposable income because the rate at which consumers pay off debt is reduced thus increasing disposable income. Organizations that have borrowed money will pay less interest when interest rates are down and thus will lower their financial risk.

Suggested tasks for the learner to attain competence against this specific outcome

1. Explain the necessity of banking for non-profit organizations
2. Identify and explain types of accounts that may be used by non-profit organizations
3. Explain how the reserve bank controls interest rates

Evidence that the learner has achieved competence against this specific outcome

1. The reasons why non profit organizations need to have banking accounts are explained
2. Types of accounts that may be used by non profit organization are identified and explained
3. How the reserve bank controls interest rates is explained

Specific Outcome 2: Explain the financial aspects involved in running a business

Mode of delivery	Assessment	Assessment instrument
Classroom presentation	Oral and written questioning	Written assignments/Tests

The medium to long term goal of running any organization is to increase the value of the organization by keeping the organization's cost of capital as low as possible. The management of any organization must at all times see to it that the organization is solvent (i.e. the organization's assets exceed its liabilities). Whilst the accountant who handles the organization's funds develops and provides data for measuring the organization's performance and assessing the organization's financial position, the management evaluates the accountant's statements, processes additional data and makes decisions based on subsequent analyses.

Financial statements provide a fair presentation of the organization's financial performance and financial position. The financial statements of an organization consist of the income statement, the balance sheet, and the cash flow statement.

Financial statements are used to assess the financial performance and condition of an organization. The measurement and evaluation of information presented in the financial statements is known as analysis and interpretation and is the link between the financial statement and decision making. The purpose of financial analysis is to determine the strengths and weaknesses of an organization. To do this it is necessary to get some benchmark based on historic performance or how other similar enterprises operate. Financial analysis is diagnostic as it highlights symptoms and indicates problem areas. It is on the basis of financial analysis that the management prepares a financial plan.

Planning

Planning can be categorized into two broad categories, namely long term planning and short term planning.

Long term planning

Long term planning is known as strategic planning. It involves what the organization wants to achieve in the long term (i.e. beyond one calendar year) and how the organization intends to achieve this. Long term planning involves 4 basic steps:

- Step 1- Identify organizational objectives
- Step 2- Consider alternative courses of action-this involves the organization assessing its strengths and weaknesses and a review of its threats and opportunities
- Step 3-Information gathering-Having narrowed down the alternatives detailed research is needed to acquire all available data on the ability to achieve the desired objectives

- Step 4-Prepare long term financial plan-Areas of activity with the best long run potential should be chosen as the basis for putting together a long term financial plan

Short term planning

To put a long term plan into effect requires the completion of a sequence of short term plans. The most common example of a short term plan is an annual budget, which wholly or partly includes major activity areas of the long term budget. The budget is therefore instrumental in helping achieve the organizational long term objectives

Financial planning allows management to anticipate events before they occur, particularly the need to raise funds externally. It begins with the construction of projected financial statements which indicate how much the organization anticipates it will make. Once the projections are made, the challenge is to operate within the parameters projected by containing expenses within the constraints of cost budgets and generating income to achieve revenue targets. The facilitator will show learners a specimen of a projected financial statements explaining importance of these projections

Start up capital and working capital

For the any business to operate it need to have the money that is used to start up the business. This money is meant to be a long term source of finance not to be withdrawn from the business within a short period of time. It is an interest free source of capital as the business will not pay any interest on it. In order for an enterprise to function on a sound financial footing, it needs sufficient money available on a permanent basis preferably at no cost.

Working capital on the other hand refers to the net total of all short term current assets and current liabilities which are in cash or will be turned into cash within the a year. Working capital is also referred to as trading capital as it the amount of money that is earned in the short term from debtors minus the money that it needs to pay its creditors and overheads Examples of short term assets are accounts receivable, cash on hand or in the bank whereas short term liabilities can be exemplified by accounts payable within 12 months, tax payable, a bank overdraft.

Management of cash

It has been mentioned that cash is the oil that lubricates the wheels of a firm. Without oil, machines will grind to a halt and a firm with inadequate cash will do likewise. The management of cash flow is a vital activity in any organization and does not only involve the financial manager but all other managers or decision makers in the main functional areas of the organization. Proper integration of all business activities and cash activities is important to the survival of any organization. This implies both profitability and liquidity. An enterprise must be profitable in that it must yield a return on the capital employed yet it must also be liquid in that it must be able to have adequate cash to meet its obligations timeously.

Short term finance and long term debt finance

Any organization's financing requirements can be split into permanent and seasonal needs. Short term finance is money used to meet the seasonal or temporary needs of the organization which are attributed to the existence of certain temporary current assets that vary throughout the year. Short term finance takes the form of spontaneous financing that arises from the organization's normal operating cycle. The two key sources of short term financing are accounts payable and accruals. Accounts payable refer to trade credit that is not associated with any financial institution. The purchaser is simply debited for the purchase price in the books of the seller and payment follows at a later stage. Trade credit is granted on an informal basis and is largely determined by the industry. Accruals are delayed payments for wages/salaries or tax. Because there is no interest cost on these accruals they constitute a cheap form of financing that may be used by an organization in the short term. Bank loans can also act as short term financing but these need to be negotiated and applied for and interest is payable on these.

Long term debt finance relates to financing needs for fixed assets together with the permanent portions of the organization's assets. Long term debt financing can be broadly classified into debt financing and equity financing. Debt financing entails procuring borrowed funds from financial institutions or individual investors. Interest is charged on the sum advanced which must be paid back to the lender. Equity financing is provided by the owners of the enterprise. In companies this is represented by the ordinary shares that have been issued and sold to investors at a value

Suggested tasks for the learner to attain competence against this specific outcome

1. Explain the purpose of financial management
2. List and explain the different types of financial statements
3. Explain the importance of financial statements to the running of an organization
4. Explain the importance of financial planning for an organization

Evidence that the learner has achieved competence against this specific outcome

1. The purpose of financial management is explained
2. Different types of financial statements are listed and explained
3. The importance of financial statements to the running of an organization is explained
4. The importance of financial planning for an organization is explained

Specific Outcome 3: Establish accounting systems

Mode of delivery	Assessment	Assessment instrument
Classroom presentation	Oral and written questioning	Written assignments/Tests

The responsibility of establishing an accounting system rests with a trained accountant. Non-accountants will not be directly involved in the implementation and operation of a cost accounting system. Non-accountants however will certainly be required to help the accountants by giving them guidance over technical matters and to provide them with information they want. The accountant will be responsible for calculating detailed service costs and estimates of stock valuations. A summary of the results relating to each department or responsibility area will be passed to staff. In order for staff to rely on the information they are presented with, it is vital that staff know how the accountant views the enterprise.

Responsibility accounting

Accounting embraces more than the mere reporting of financial data. One aspect of particular importance is measuring performance. In a large organization it is impossible for central management to control the whole organization, some degree of decentralization is necessary. This is done by the creation of responsibility centres. A responsibility centre is a unit of the organization where an individual manager is held responsible for that unit's performance. Responsibility accounting therefore rests on the premise that managers are held accountable for their areas of responsibility. It requires that the organization be divided into separate identifiable divisions where performance can be controlled and evaluated effectively. There are four types of responsibility centres:

- Cost centre- A cost centre is a division where a manager is held responsible for the costs under his control but not for any revenue
- Revenue centre- A revenue centre is a division that has responsibility to generate income. This division does not control the costs that affect net income.
- Profit centre- A profit centre is a division that is responsible for both costs and revenue
- Investment centre- An investment centre is a division that is responsible for investment of funds

Each responsibility centre is clearly demarcated from another and a manager is put in charge of each operating his/her division as independently as possible. By establishing boundaries between the different divisions, it is possible to identify clearly their respective costs and revenues.

Classification of costs

Each cost item should be identified with a responsibility centre. Costs that are easily identifiable with a particular division are known as direct costs. Some costs however are so general and basic that no one division has control over them. Such costs are called indirect costs.

Costs can be classified into 4 categories namely:

- Manufacturing costs- these are also classified into direct and indirect costs- Direct manufacturing costs are materials, the wages and all other expenses related to the manufacture of a particular product or service. The total of all direct manufacturing costs is known as prime costs Indirect manufacturing costs are those materials that cannot be easily identified with a production unit, remuneration paid to employees that do not work directly on a product and other production costs that cannot be identified with the particular product or service like telephones, electricity etc. The total of all indirect manufacturing costs is known as secondary costs.
- Administration costs- These are expenses incurred in the general running of the enterprise. Examples of these are salaries of office staff, office equipment, stationery etc.
- Research and development costs- Research expenditure involves the costs of working on new products or processes. Development expenditure includes costs associated with trying to improve existing products or processes
- Marketing costs- These are costs incurred for the acquisition of orders

Learner should at this point be presented with the costs of incurred by their organization and be asked to classify each cost item

Suggested tasks for the learner to attain competence against this specific outcome

1. Explain responsibility accounting with reference to your own organization
2. Name and explain the 4 types of responsibility centers with reference to your own organization
3. Name and explain the 4 categories of costs

Evidence that the learner has achieved competence against this specific outcome

1. Responsibility accounting is explained in relation to own organization
2. The 4 types of responsibility centers are named and explained in relation to own organization
3. The 4 categories of costs are named and explained

Specific Outcome 4: Analyse the elements of an income and expenditure statement

Mode of delivery	Assessment	Assessment instrument
Classroom presentation	Oral and written questioning	Written assignments/Tests

The income statement measures the financial performance of an organization during a certain period. It records whether a profit or loss was made. The purpose of an income statement is to evaluate profitability by matching the revenue earned during a given period with the expenses incurred in the process of obtaining that revenue. If revenue exceeds expenses, the organization is ensuring its survival. It is crucial to know that income statements cover an accounting period that may be a month, a quarter of a year, half of the year or a year. Every business concern prepares a yearly income statement but management of a business concern needs to know from month to month whether revenue is rising or falling, whether expenses are being held at the anticipated level and how net income compares with that of the preceding month

Since the operation of a business entity entails a stream of continuing transactions, many transactions begin in one accounting period but affect several succeeding periods. Not all transactions can be precisely divided by accounting periods. The purchase of for example an alarm system provides benefits to the organization over all the years it is in use. No one can determine in advance how many months or years of service will be benefited from such an asset. Nevertheless, in measuring the net income of an organization the accountant must estimate what portion of long lived assets must be applicable to the current year. This is reflected by non-cash charges which are expenses on the income statement that do not involve an actual cash outflow. A typical example of this is depreciation. Depreciation is the systematic changing of a portion of the costs of fixed assets against annual revenue over time. The accountant will decide on the time period over which an asset will be depreciated and will assign a depreciation life to the asset

The facilitator will show learners a specimen of an income statement. Learners must be able to identify assets and liabilities and determine whether the organization is on a sound financial footing

Suggested tasks for the learner to attain competence against this specific outcome

1. The purpose of an income statement is explained
2. Determine assets and liabilities in your own organization
3. Identify sources of income and expenditure in your own organization
4. Identify assets and liabilities in a given income statement
5. Based on the given income statement determine the financial position of the organization. Give reasons for your assumptions

Evidence that the learner has achieved competence against this specific outcome

1. The purpose of an income statement is explained
2. Assets and liabilities of own organization are determined
3. Sources of income and expenditure in own organization are identified
4. Assets and liabilities are identified in a given income statement
5. The financial position of an organization is determined based on a given income statement

Specific Outcome 5: Analyse a balance sheet

Mode of delivery	Assessment	Assessment instrument
Classroom presentation	Oral and written questioning	Written assignments/Tests

The balance sheet indicates the financial position of the organization at a particular date. (What the firm is worth in book value). Assets are economic resources which are owned by the organization and are expected to benefit the organization in its future operations. A distinction is made between fixed and current assets.

Fixed assets refer to assets that will be retained for longer than the accounting period of the organization. They include land, buildings, equipment and motor vehicles. Fixed assets are used or get worn out over time therefore their original costs are reduced in order to reflect the usage and resultant loss in value. (This loss in value is known as depreciation.) The financial manager must keep track of all fixed assets of the organization by maintaining an asset register.

Current assets are short term assets which are expected to be converted into cash during the next accounting period. Current assets include inventory, accounts receivable and cash deposited or on hand

It is important to bear in mind that the rand amounts listed do not show the real value at which the assets could be sold thus the balance sheet does not show the real value of the organization at all times.

Liabilities on the other hand are debts. All business concerns have liabilities. Liabilities can be generalized into two categories namely long term debt and current liabilities. Long term debts are loans with a maturity exceeding one year whilst current liabilities are debts with a maturity of less than a year. Examples of current liabilities are accounts payable, tax payable and wages and salaries payable. These result from the normal operations of the organization.

The facilitator will show learners a specimen of a balance sheet with emphasis on the assets and liabilities of the organization.

Suggested tasks for the learner to attain competence against this specific outcome

1. Explain the purpose of a balance sheet
2. Explain what an asset is and classify assets in terms of fixed and current assets
3. Explain what a liability is and classify liabilities in terms of long term and current liabilities
4. Based on the given balance sheet determine the financial worth of the organization

Evidence that the learner has achieved competence against this specific outcome

1. The purpose of a balance sheet is explained
2. The concept asset is explained and assets are classified in terms of fixed and current assets
3. The concept of a liability is explained and liabilities are classified in terms of long term and current liabilities
4. The financial worth of an organization is determined based on a given balance sheet

Specific Outcome 6: Use the evidence in financial statements to make a financial decision

Mode of delivery	Assessment	Assessment instrument
Classroom presentation	Oral and written questioning	Written assignments/Tests

Having studied the income statement and balance sheet of an organization in the same accounting period learners should be able to determine whether an organization is financially sound or not. Learners who are part of the organization should be able to identify the strengths and weaknesses of the organization and make suggestions as to how income can be improved and costs reduced.

Financial statement are use to assess the financial performance and condition of an organization. The measurement and evaluation of information presented in the financial statements is known as analysis and interpretation or ratio analysis. The inputs in ratio analysis are the organization's income statement and the balance sheet for the period under scrutiny. The data provided by these statements can be used to calculate ratios that permit the evaluation of certain aspects of financial performance and condition. The usefulness of ratios is wholly dependent on their skillful application and interpretation. Ratios need to be compared to a standard if they are to be effectively interpreted. Two such standards are comparing the organization's ratio with the ratios of different firms at the same point in time (i.e. industry ratio) and comparing historic ratios of the organization over time to determine whether it is progressing as planned (i.e. time series analyses)

Ratios can be grouped within the broad categories of business performance that they are attempting to examine. These categories of business performance that are: Liquidity; Asset management; Debt management; Profitability and Investment.

- Liquid ratios- An organization that has a good proportion of liquid assets will be more able to meet its bills as they become due than one with fewer liquid assets.
- Asset management ratios-These ratios measure how effectively management is using the organization's assets to generate income. If two organizations have the same level of sales but one has a lower investment in inventories, the one with lower inventories is regarded as more efficient with respect to inventory investment.
- Debt management ratios- Debt management plays an important role in financial management and the extent of the organization's financial leverage has a number of implications. The greater the organization's financial leverage, the greater its financial risk. The debt management ratios assess the impact of financial leverage on risk

- Profitability ratios- The profitability ratios show the combined effect of liquidity, asset management and debt management on operating results.
- Investor ratios- Investors are primarily concerned with the rate of return earned by their investment in a company. These ratios determine what the investment is likely to earn in future

Suggested tasks for the learner to attain competence against this specific outcome

1. List the different financial ratios and explain the purpose of ratio category
2. Identify the strengths and weaknesses of your organization and make suggestions as to how income can be improved and costs reduced

Evidence that the learner has achieved competence against this specific outcome

1. Different financial ratios are listed and the purpose each ratio category is explained
2. Strengths and weaknesses of own organization are identified and suggestions on how income can be improved and costs minimized are made