

Pathways to Management and Leadership

**Level 5: Management and
Leadership**

Unit 520

Managing Finance

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Unit 520: Managing Finance

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Managing Finance

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About this workbook

The unit

The main purpose of this workbook is to support you as you study for the Chartered Management Institute Level 5 qualification — Management and Leadership, so it specifically focuses on the content of the syllabus for Unit 520 Managing Finance. This is about how you understand financial management within your organisation and how you create and manage budgets.

This workbook provides underpinning knowledge and develops understanding to improve your skills as well as to prepare for future assessment. If you are studying towards Level 5 in Management and Leadership, then you will be assessed by your approved centre on 'your knowledge and understanding of the following learning outcomes:

1. Understand finance within organisations
2. Know how to set and manage budgets.

The aims of the workbook

This workbook aims to help you learn how to:

- Work with the finance function supporting the operation or enterprise, whilst managing departmental financial performance
- Create and manage budgets effectively
- Analyse financial information in order to evaluate budgetary performance to plan, including cost control
- Implement corrective actions against budget variances ensuring compliance with operating procedures.

This workbook is about how you can develop your knowledge to effectively forecast financial organisational performance and manage the operation/enterprise in alignment with an agreed financial budget.

Syllabus coverage

The table below shows which sections of the workbook address the assessment criteria of the qualification syllabus.

Unit 520: Managing Finance Syllabus coverage		Addressed within section
1.1	Analyse the relationship between the financial function and other functional areas within organisations	1
1.2	Examine the impact of financial objectives on decision making within organisations	1
1.3	Differentiate between management accounting and financial accounting	1
1.4	Analyse the impact of organisational and regulatory frameworks on an organisation's approach to financial management	1
1.5	Analyse the challenges organisations face accessing finance	1
2.1	Differentiate between budget setting and financial forecasting	2
2.2	Evaluate budget setting approaches used by organisations	2
2.3	Formulate and justify a budget for an area of management responsibility	2
2.4	Analyse the factors that impact on budget management	2
2.5	Specify corrective actions to be taken in response to budgetary variance	2
2.6	Discuss reporting procedures for authorising corrective actions to a budget	2

Getting started

Financial management skills are essential for all managers regardless of whether there is a dedicated finance team within an organisation. Financial acumen enhances decision making skills, which in turn supports management of projects, tasks and functional areas. This unit has been designed to enable learners to understand how financial systems within organisations operate. Learners will evaluate the sources of finance for organisations, and understand the principles for setting and managing budgets in line with regulatory and organisational guidelines. This unit has been designed to enhance the learner's confidence and credibility in financial management, which will translate into improved management skills.

How to use the workbook

The workbooks provide ideas from writers and thinkers in the management and leadership field. They offer opportunities for you to investigate and apply these ideas within your working environment and job-role.

Structure

Each workbook is divided into sections that together cover the knowledge and understanding required for that unit of Level 5 Management and Leadership. Each section starts with a clear set of objectives to identify the background knowledge to be covered and the management skills in the workplace that enable you to demonstrate this knowledge. You do not have to complete the sections in the order that they appear in the workbook, but you should try to cover them all to make sure that your work on the unit is complete. There are self-assessment questions at the end of each section that allow you to check your progress. You may want to discuss your answers to the self-assessment questions with your line manager or a colleague.

Activities

Throughout the workbooks there are activities for you to complete. These activities are designed to help you to develop yourself as a manager. Space is provided within the activities for you to enter your own thoughts or findings. Feedback is then provided to confirm your input or to offer more ideas for you to consider.

To get the best from the workbooks, you should try to complete each activity fully before moving on. However, if the answer is obvious to you because the issue is one you have encountered previously, then you might just note some bullet points that you can then compare quickly against the feedback. You may sometimes find it difficult to write your complete response to an activity in the space provided. Don't worry about this — just keep a separate notebook handy, which you can use and refer to as needed.

Try not to look at the feedback section before completing an activity. You might like to try covering up the feedback with a

postcard or piece of paper while you are working through an activity.

Timings

Timings are suggested for each section and activity, although it is important that **you** decide how much time to spend on an activity. Some activities may occupy only a few moments' thought, while others may be of particular interest and so you might decide to spend half an hour or more exploring the issues. This is fine — the purpose of the activities is to help you reflect on what you are doing, and to help you identify ways of enhancing your effectiveness. It is always worth writing something though, even if it's brief — the act of writing will reinforce your learning much more effectively than just referring to the feedback.

Scenarios

There are scenarios and examples throughout each workbook to illustrate key points in real workplace settings. The scenarios cover a wide range of employment sectors. As you work through, you might like to think of your own examples from your own experience.

Planning your work

The reading and reflection scenarios and activities in each section of the workbook are designed to take around two hours to complete (although some may take longer). This is a useful indicator of the minimum length of time that you should aim to set aside for a study session. Try to find a quiet place where you will not be interrupted and where you can keep your workbooks, notes and papers reasonably tidy. You may also like to think about the time of day when you work best — are you a 'morning person' who likes to get things done at the start of the day, or do you work better in the evening when there may be fewer disturbances?

Preparing for assessment

Further information on assessment is available in the Qualification Support section of ManagementDirect, CMI's online resource portal. If you have any further questions about assessment procedures, it is important that you resolve these with your tutor or centre co-ordinator as soon as possible.

Further reading

Suggestions for further reading and links to management information are available via ManagementDirect. You will also find titles for further reading in the Further Resources at the end of this workbook.

Section 1 Understand finance within organisations

Learning outcomes and assessment criteria (about 2 hours)

By the end of this and the next section you will understand finance within organisations and know how to set and manage budgets effectively:

1.1	Analyse the relationship between the financial function and other functional areas within organisations
1.2	Examine the impact of financial objectives on decision making within organisations
1.3	Differentiate between management accounting and financial accounting
1.4	Analyse the impact of organisational and regulatory frameworks on an organisation's approach to financial management
1.5	Analyse the challenges organisations face accessing finance

The finance function

The finance function within an organisation exists to support the organisational objectives in alignment with the management functions. In general terms, the management functions can be segmented into:

- Strategic management
- Operational management
- Risk management.

These management functions are not standalone and do not operate in isolation. There is significant overlap in the management disciplines and this should be reflected in how the organisation operates.

Similarly, the finance function operates in alignment with the other organisational disciplines and it is important that a collaborative working relationship is established and maintained across the organisational functions.

The finance function should support more than back office transactional record keeping by adding additional value through delivering real time valuable insights to help deliver a competitive advantage (ManagementDirect Transforming Finance: From transactional to value added).

There are multiple aspects of the finance function including:

- Operating expenditure - financial planning
- Capital expenditure - investment projects
- Financial control - decision making
- Management accounting
- Financial accounting.

Operating expenditure

Normally created bottom-up for accuracy and buy-in across the organisation, at a functional/departmental level, each department creates an operating budget forecasting the costs required to operate the department function. This budget comprises fixed costs - core cost such as full-time salaries, medical insurance, pensions and fixed operating costs that exist within the department.

Fixed costs can be defined as those costs which the organisation cannot change, or cannot easily change, and are independent of the scale of the operational activity.

Variable costs should also be forecast, typically comprising costs which the departmental manager has influence over and therefore these can increase or decrease as a consequence of managerial decisions. Typical variable costs shall include part-time salaries and associated costs, overtime, sub-contracting costs, maintenance, staff development costs, project development costs, travel, consistency marketing budget etc. These illustrated lists are not exhaustive.

Variable costs can be defined as those costs which increase or decrease in proportion with the business activity; orders and manufacturing etc.

From the fixed and variable cost forecasts a functional/department budget is created. Consolidating each departmental budget along with the senior management team budget; an administration budget and the executive team budget creates a holistic organisational budget. This becomes the operating budget.

Capital expenditure

At a senior management team / executive team level, the capital expenditure shall be forecast. This shall comprise investment decisions, perhaps the purchase of new equipment, infrastructure, IT systems, a new building for expansion etc.

The combination of the operating budget (expenditure) and the capital budget (expenditure) then becomes the organisational budget.

The finance function then takes ownership of the organisational budget in terms of cashflow management; accounts receivable and accounts payable - therefore overall financial management.

The finance function is accountable to the senior team in the organisation. Dialogue should flow two-way to share information and report financial performance - performance to the planned budget (performance to plan) and reporting any variances (deviations from the plan - positive or negative).

Activity

1.1 Costs

(about 20 minutes)

Consider your own organisation and identify fixed costs, variable costs and capital costs:

Feedback

Examples of fixed costs

Fixed costs relate to costs that are incurred by the organisation regardless of the scale of activity. Typical examples include office costs - rent, accommodation costs and salary costs for permanent employees.

Examples of variable costs

Variable costs relate to costs which increase or decrease with the scale of the business. Typical examples are materials in a manufacturing line - as volume increases the quantity of materials increase; overtime costs to support increasing demand; the cost of temporary staff; expansion costs e.g. new office space.

Examples of capital costs

Capital costs relate to the purchase of assets that are required for the organisation. These are often high value assets that will be purchased and depreciated over a number of years.

Typical examples are office rent/lease costs, buildings, equipment required to perform the organisation's core business e.g. manufacturing equipment; computer systems; software systems.

Financial control

The finance function under the leadership of the finance manager (Chief Financial Officer - CFO) has the accountability to manage the budgets and cashflow in co-operation with the management team.

Firstly, it is helpful to highlight the difference between cash and profit as financial managers are required to control both.

Cash can be defined as money in the physical form of currency (banknotes and coins) and current realisable assets that can be accessed immediately.

Profit can be defined as the difference between the sales price and the costs of sales; where the cost of sales captures all of the tangible costs associated with the sale - cost of materials, salaries, operating costs, personal and corporate taxation, travel etc. Alternatively, profit can be defined as the difference between total income minus total costs.

The budgets managed by the finance manager comprise invoicing customers, paying supplier invoices, payroll, managing all cashflow and managing investments.

The finance function has a responsibility to communicate performance to the management relative to performance to the sales plan (business plan); control of the cost base; any impact of exchange rates on international markets; any impact of interest rates and borrowing; reporting the cash position of the organisation; short-term and long-term liabilities.

As noted earlier, the functional departments are required to work together across the organisation, sharing information that allows an accurate illustration of organisational and financial performance to be formulated.

Variances to the plan, particularly reductions in income and/or increases to the cost base will result in the senior management team making decisions which will impact the organisation's objectives. Similarly, positive variances can be realised where the organisation outperforms the plan, realising income and profit in excess of the business plan.

Management accounting

Management accounting is concerned with using financial information to assist in the internal management of an organisation.

Management accounting is a practice that provides the management of a business with the information they need to make decisions. It encompasses performance management, strategic management and risk management.

Management accounting will also evaluate cost-benefit-analysis of new projects or services, analysing a project/investment justification in relation to its costs, its outcomes, and the impact to the organisation, the revenue/growth it creates and the return-on-

investment to the organisation. These cost-benefit-analyses will be used by the senior management team to decide whether to progress with the proposed project or services and will be used to track the performance of those that are approved and implemented. These are tangible tools to justify projects and track their performance.

Management accounting seeks to address the three business areas of performance management; strategic management; and risk management. - CMI Checklist 253 Management Accounting.

Financial accounting

Financial accounting supports the creation and reporting of the balance sheet (Statement of Financial Position) and the profit & loss account (Statement of Profit and Loss).

The balance sheet provides a thorough and detailed understanding of a company's financial position at a given time, as at the last day of the company's financial year.

The financial, or fiscal year, may differ from the calendar year. For example, Her Majesty's Revenue and Customs (HMRC) operates a fiscal tax year from the 01 April in one year (e.g. 2017) to the 31 March the next year (e.g. 2018). It is important to note the appropriate fiscal time period, which informs 3-month quarterly reporting periods.

Be aware that a balance sheet is a snapshot on one particular day and therefore it is always out of date by the time it is communicated. Whilst this may appear odd, it is established financial practice and reflects the fact that the valuation of assets will/can differ over time, so the snapshot time period is an important point to note in asset valuation.

Remember that the assets are documented as 'book values' and may differ from the value that can be realised in the event of a sale. Book values can be defined as the monetary value of assets as documented in the balance sheet.

Alternatively, under IFRS companies may choose to document assets at fair value (market value). Therefore, the senior management team are required to choose the valuation of assets and then be consistent.

The balance sheet illustrates liabilities and assets.

Every balance sheet includes the balance of every account in the accounting system. Accounts are grouped to illustrate one overall figure for each category. The balance of account is then carried forward to the next accounting period.

A balance sheet must be formally approved by the directors and signed by one of them. It must be submitted to Companies House (<https://www.gov.uk/government/organisations/companies-house>) within nine months of the end of the accounting period; an extra three months is permissible if there are export or overseas interests. Balance sheets can be obtained from Companies House.- CMI Checklist 130: Reading a balance sheet.