



INTRODUCTION TO ACCOUNTING

Financial and Management
Accounting

Week 3

The Finance element of the module .
We will be covering topics including:

Accounting
terminology

Financial and
Management
accounting

The Financial
Statements

The role of
Accounting in
Decision Making

Financial
Forecasting

Yield
Management

Budgets

SOURCES OF FINANCE

Money that is
already in the firm
or can be earned



Financial Accounting



PREPARATION OF
FINANCIAL STATEMENTS
FOR EXTERNAL USE.



SUMMARISES
HISTORICAL DATA

Financial accounting is:



Historic i.e. all figures show what has happened in the past.



Must be produced annually.



Prepared for many different stakeholders.

Differences
between cost
and financial
accounting

**Financial
accounting is:**



Required by law.



Accurate (audited to prove accounts are accurate).



More important to be accurate than timely.



Deals with a whole company/ organisation.



Has to comply with SSAPs (Statement of Statutory Accounting Principles), FRS (Financial Reporting Standard), etc i.e., items must be treated in certain ways.

Management Accounting



produces information about the costs and profitability of products and different parts of the business using internally produced reports



enables managers to take planning and control decisions



produces detailed information about sales, production, finance etc



preparation of budgets, setting price levels and advising on future activities

Key Definitions

Cost Unit

A cost unit is a unit of product or service for which costs can be ascertained.

Direct Cost

Costs which can be directly attributed to a cost unit.

Indirect Cost

Costs which cannot economically be identified with a specific cost unit.

Cost accounting is:

- Can be for periods in the past, present or future.
- Produced when required.
- Prepared for management.

Cost accounting is:

- Cost accounting is an internal reporting system to facilitate decision making by management
- Cost accounting is a form of management accounting that enables an organisation to predict future expenditures
- Organisations do not have to use it (although most do in some form).

Cost accounting is:

- Information may be approximate.
- Can be produced for any segment of an organisation.
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Cost accounting is:

- The **cost accountant** provides answers to the following questions:
- What has been the costs of goods and services provided to the consumer?
- What are the revenues related to the costs to assess profits?
- What is the value of stocks of goods for balance sheet purposes?
- What are future costs of goods and services?
- How do actual costs compare to budgeted costs?
- What information does management need to make informed decisions about profits and costs?

Direct vs. Indirect

- **Direct costs**
- These are costs that can be economically traced, identified and matched to the product being produced or service provided
- The sum of the direct costs for a product or service is often referred to as prime cost.

Three types of direct costs:

Direct Labour

Direct Materials

Direct Expenses

Direct vs. Indirect

- **Indirect Costs**
- These are also referred to as overheads
- Indirect costs can be thought of those costs which are incurred to support to an organisation's main activities
- By breaking down costs in this way, it becomes possible to identify the cause of costs within an organisation. From this it becomes possible to develop cost control and cost reduction strategies.

Three types of indirect cost:

Indirect Materials

Indirect Labour

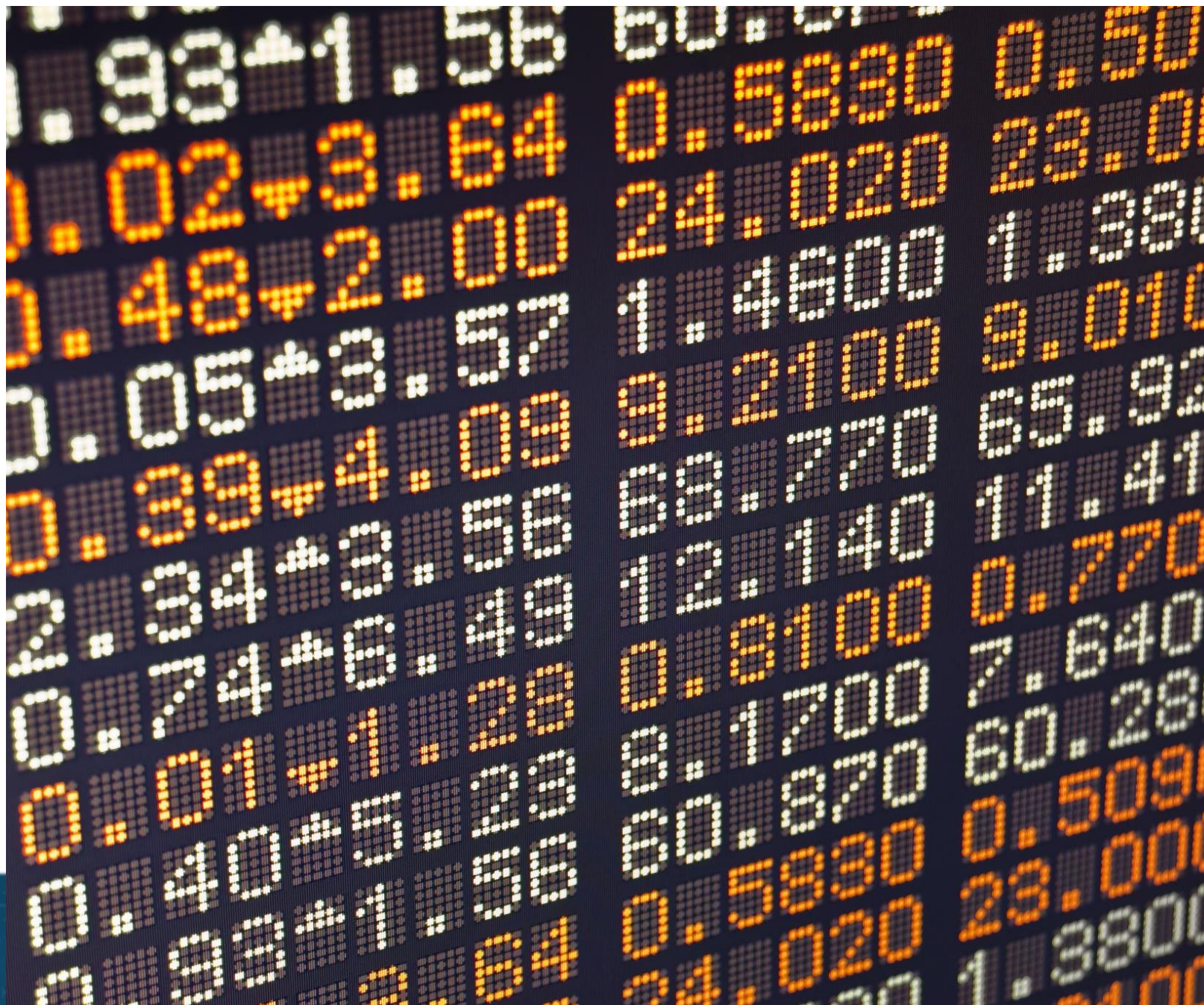
Indirect Expenses

Cost Behaviour

Planning and decision making are two key areas of management, an understanding of what our costs are and how they behave under certain conditions is of crucial importance to the decision-making process.

Costs can be seen from the **perspective of how they behave, react and fluctuate** according to organisational activity; this is a very powerful management tool. In this context costs are either

- **Fixed costs**
- **Stepped fixed costs**
- **Variable costs**
- **Semi-variable costs**



Internal Sources

Normally it is wisest for a firm to use money it already has. But why?

This is possibly the cheapest source of finance available

Unfortunately, there are not too many sources of internally generated finance



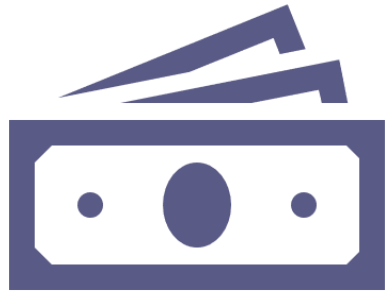
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Y Drindod Dewi Sant
University of Wales
Trinity Saint David



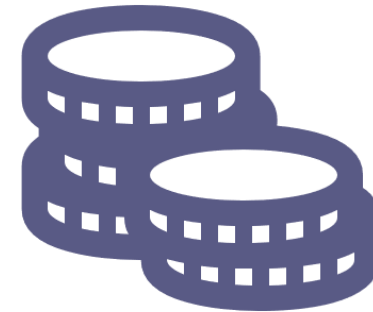
- Internal Sources
- Retained Profits
- Goods and Services
- Debtor Control - represents all the money that you are owed by your customers



External Sources



External sources require the firm to seek finance from outside itself.



This will always result in additional costs. Nobody will give money to a firm without expecting some recompense.

External Sources

Debt

- Debt is simply the firm borrowing finance
- You owe money

Equity

- Equity refers to the firm raising finance by issuing shares
- Equity is measured for accounting purposes by subtracting liabilities from the value of the assets owned.
- On a company's balance sheet, the difference between its liabilities and assets shows how much equity the company has.

The method of external sources depends upon a number of factors

- The period of time that finance is needed
- The cost of finance
- The retention of control of the firm
- The level risk
- Capital gearing - the ratio of debt a company has relative to equities. Capital gearing represents the financial risk of a company.

- External sources should be sought for only the length of time that the money is needed.
- If finance is required **for long-term** expansion, then long-term sources should be sought. Similarly, if a firm is suffering from a **very temporary shortage of cash**, then only short-term sources of finance should be sought.
- **Debt is usually described as short term**
- **Equity is usually described as long term**

External Sources – Period of Time

Short-term is less than one year

Medium term is more than one and less than five years

Long-term would be any period over five years.

Provision of External Finance

Short-term sources

- Overdrafts
- Creditors
- Factoring
- **Definition:** Factoring is a type of finance in which a business would sell its accounts receivable (invoices) to a third party to meet its short-term liquidity needs. Under the transaction between both parties, the factor would pay the amount due on the invoices minus its commission or fees.

Medium Term Sources

- Bank Loans
- Hire Purchase
- Leasing



Provision of External Finance

Long-term Sources

Mortgages

Debentures - *is a long term yielding rate of interest issued by a company and secured against assets.*

Equity

Borrowing

- When an organisation considers borrowing, it needs to ensure that it can **afford to do so**
- As well as consideration of the costs associated with the borrowing of money externally, a key role for the **management accountant** is the consideration of the costs associated with the day to day running of the organisation



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- Stepped fixed costs
- Variable costs
- Semi-variable costs

If a business cost £750,000 to run last year, how much will it cost to run this year if business activity is forecast to increase by 25%?

To answer this question, we need to understand how costs behave i.e., how do costs change as business activity changes?

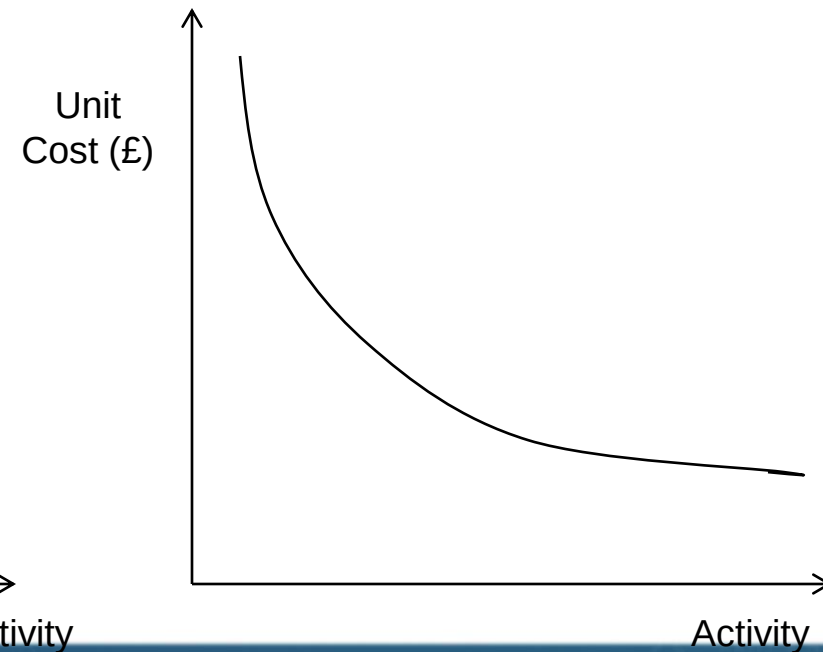
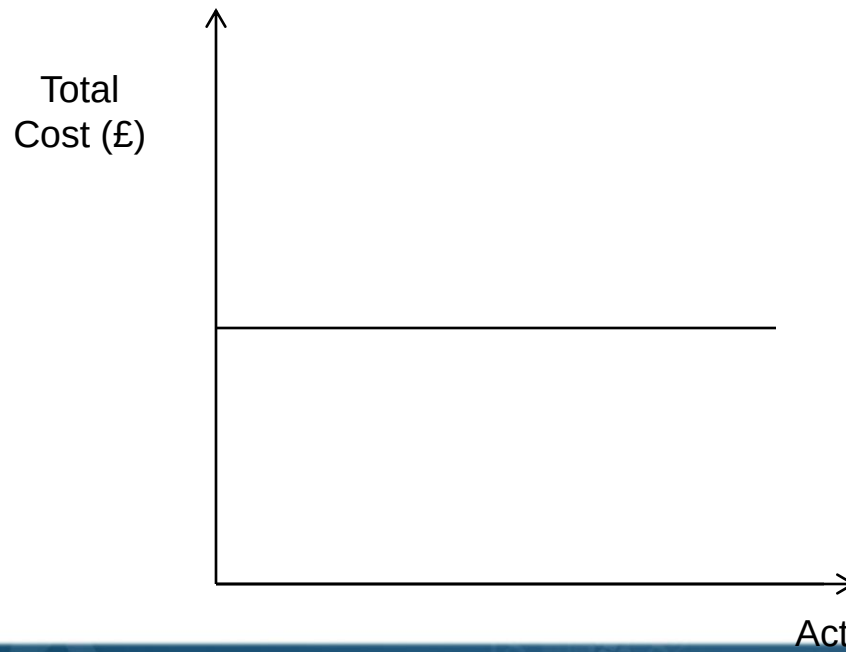
Cost Behaviour - Fixed Cost

This type of cost is incurred for a period and within certain output limits tends to be unaffected by fluctuations in the level of output.

- Salaries
- Rent / mortgage

Fixed Costs also called **non-controllable costs** remain the same whatever the level of activity that an organisation does over a period of time, e.g. cost of car road tax will be the same whether we drive it 200 miles a year or 15,000 miles.

Other costs that will be largely fixed in nature, include: Wages and salaries – fixed amounts; Insurance; Rent and rates; Depreciation on assets; Leasing charge. If business expands fixed costs may alter.



Cost Behaviour - Variable Cost

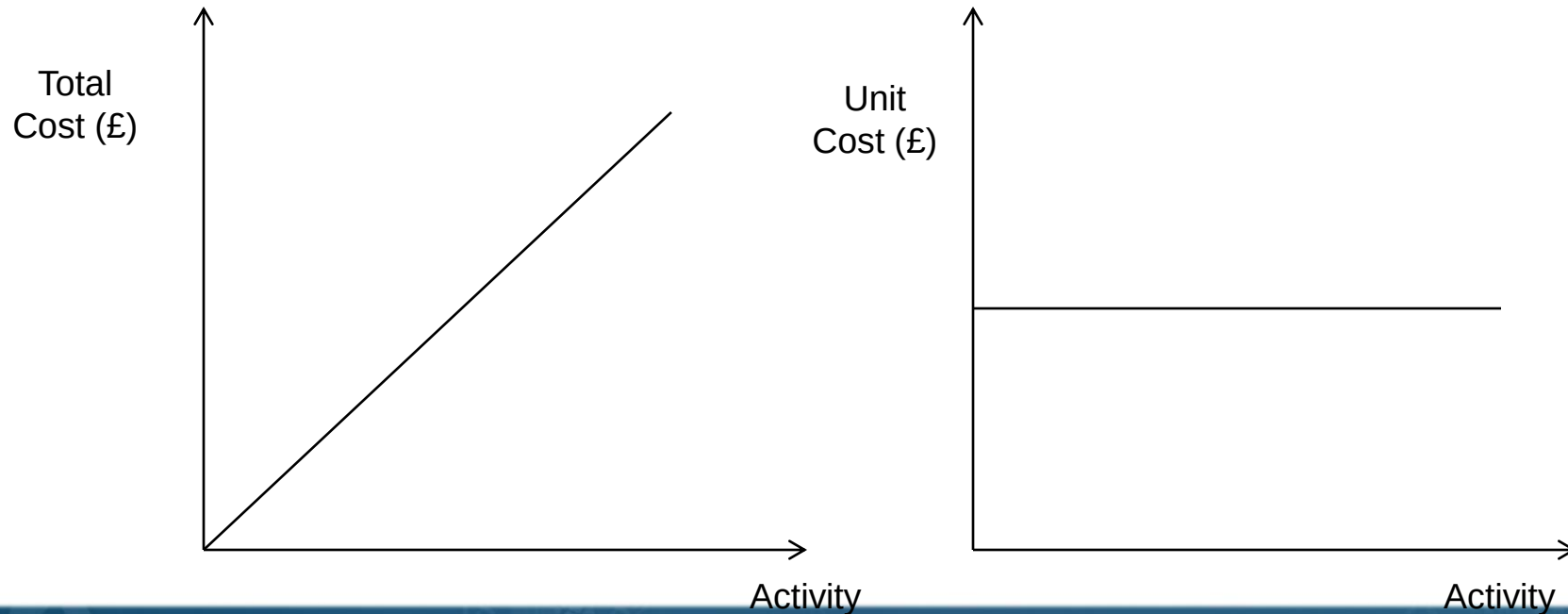
A cost which varies with the level of activity

– the more that is produced the higher the variable cost.

Variable Costs also called **avoidable/controllable costs** and fluctuate according to activity.

If we refer to our car example a variable cost would be petrol, which **will vary according to the amount of mileage** that we do. Other examples of variable costs are:

Inventory; Wages – paid on the basis of piecework, hourly rate etc. Bonuses; Sales commissions



- Cost of raw materials
- Direct labour costs

Revenue or Yield Management

- It is essential that management manage all costs to prevent wastage, plan budgets and set prices for goods and services.
- **Revenue Management (RM)** - offering the correct type of inventory at the appropriate price. In many organisations price fluctuations do not happen on daily. Price changes generally refer to sales or in direct relation to inflation or deflation (or VAT rate amendments).
- However, in the hospitality/Tourism sector the price can change daily
- **Yield management** is a pricing strategy, which is commonly utilised by businesses in hospitality, air travel and other tourism related fields, in order to **generate maximum revenue from a perishable inventory** (e.g. hotel rooms, or airline seats).
- With regard to cruises, this could be the type of cabin offered i.e. cabin or staterooms



RM

- A simplistic way to look at yield is in regard to the Cruise industry:
- Yield is the function of both the price charged for differentiated service options (pricing) and the different cabins/staterooms sold at each price
- The perishability of the inventory be it cabins of a cruise ship, seats on an aircraft, hotel rooms or theatre tickets drives the RM pricing policy.
- RM is applied when service organisations have a fixed capacity and how success or failure is dependent on how this capacity is made use of.
- These type of organisations generally **have high fixed costs** that are covered when a certain **level of sales is reached**.





Event finance

Events management

Learning Objectives

1. Understand the role of financial management in the overall management of an event
2. Create an event budget
3. Understand the methods of event costing and ticket pricing
4. Monitor and control the event spending and incoming finances
5. Identify the key elements of budgetary control and explain the relationship between them
6. Understand the advantages and shortcomings of using a budget

Introduction



Very often event costs increase dramatically; especially in sports events, cost overruns seem to be one of the biggest issues on the agenda of event organisers.



Therefore, it is important to have a good overview of the costs of an event and the potential benefits event organisers face.

Preuss and Schnitzer (2012) debates the economic impacts of major events (e.g., Preuss, 2009; Matheson, 2009; Baade and Matheson, 2004)

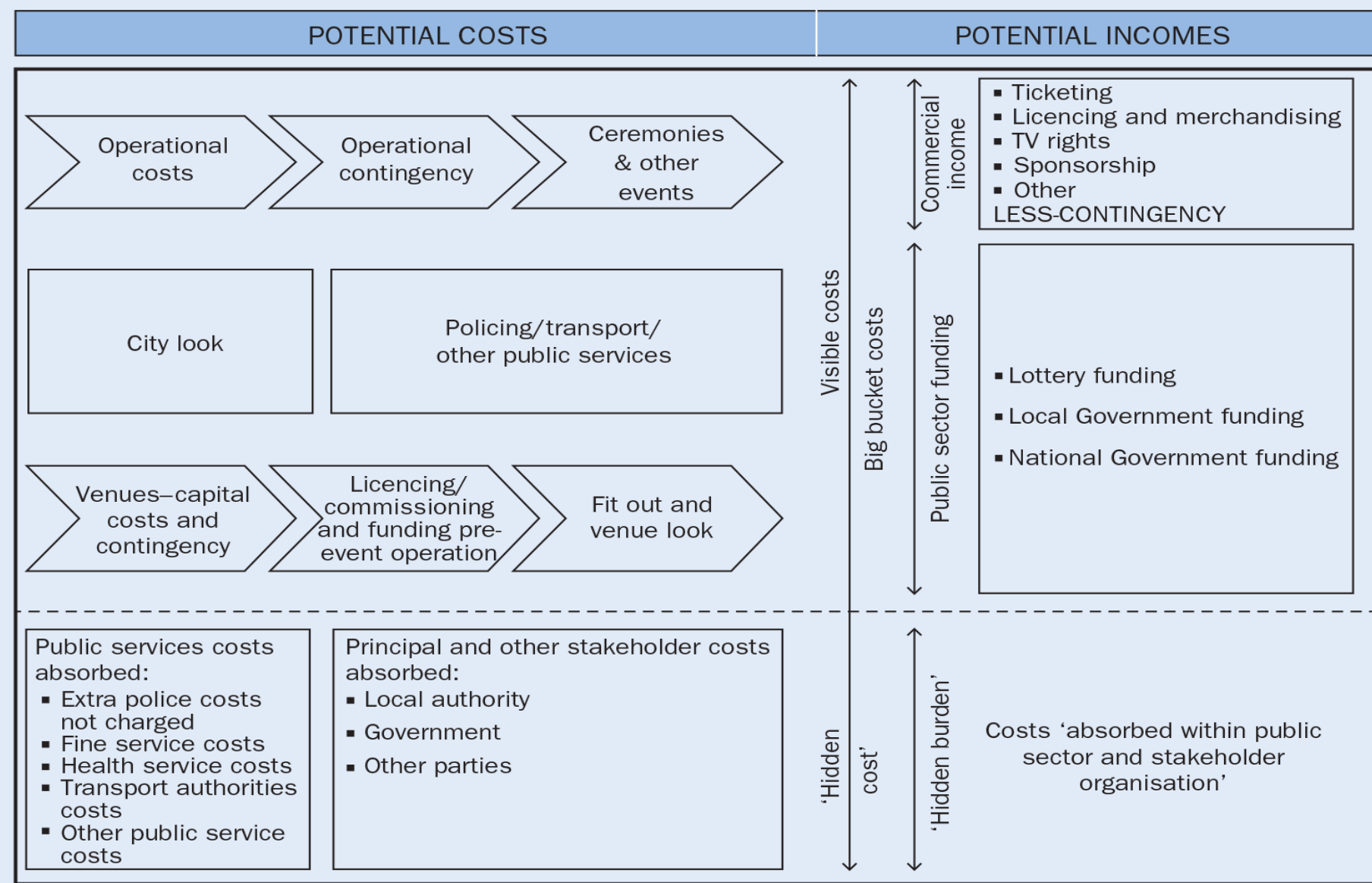


Figure 8.1 Potential costs and incomes of events

Source: Own illustration adapted from Games Legacy (2002: 26)

<i>User Groups</i>	<i>Areas of interest</i>
Event managers	Managers require financial information so that they can make present and future plans for the event and see how effective their decisions have been.
Trade contacts (e.g. suppliers)	Suppliers and other trade contacts need to know if they are going to be paid on time by the event organiser.
Providers of private finance (e.g. banks and so on)	Banks and other lenders of finance need to ensure that any loans and interest payments are going to be made on time before they lend money and during the repayment period.
Providers of public finance (e.g. government agencies, quangos and so on)	Funding bodies will want to ensure that their funds are being used for the appropriate purpose and that those funds are helping to meet their performance objectives.

Table 6.2 Users of financial information and their information needs

<i>User Groups</i>	<i>Areas of interest</i>
Tax authorities	The tax authorities require information about the profits/surplus of the event so that they can work out how much tax the organisation owes. They also need details for VAT and employees' income tax.
Employees/volunteers	Organisations' employees and volunteers often wish to know whether their jobs are safe and that they are going to be paid on time or that the event is likely to go ahead.
Spectators	It is normal for spectators to know if goods/services purchased are going to be delivered/provided.

Table 6.2 Users of financial information and their information needs (contd.)

Forecasting finance and ROI

- Finance for events can come from:
 - Sponsorship
 - Ticket sales (e.g. concerts)
 - Sales on the day of the event
 - Money made after the event has taken place (e.g. product launches)
- ROI can be different for each of the stakeholders
- Can be hard to express ROI in purely financial terms (e.g. community happiness)



The Budget

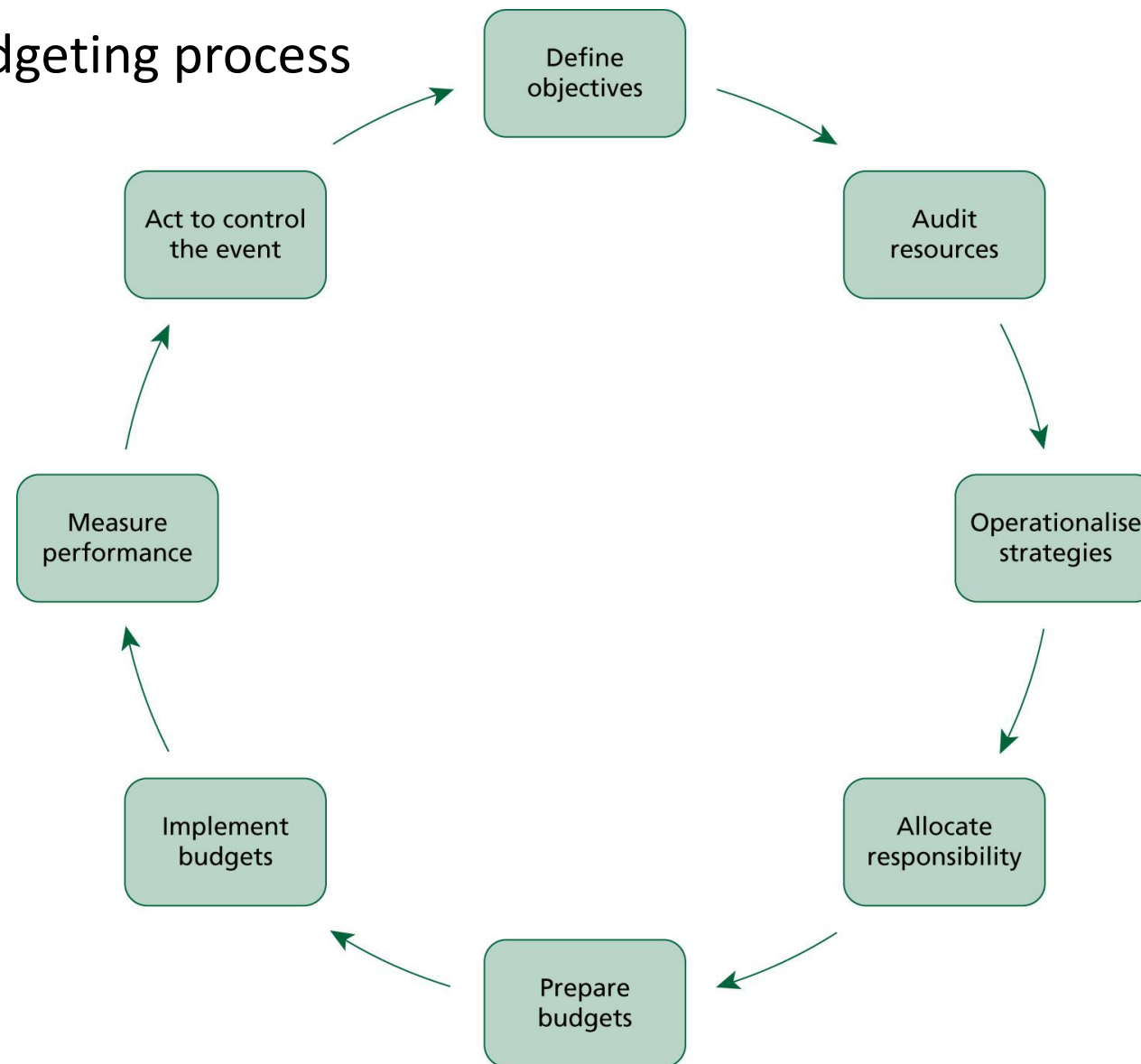
- An event budget is used to compare actual costs and revenues with projected costs and revenues
- Cash flow is important as most aspects of an event require expenditure before revenue is obtained
- Funding or sponsorship bodies need to see a budget before committing to the event



Organisational objectives (MASTER)

- **M**easurable – e.g. a profit of £3 million in the financial year, or simply to break even.
- **A**chievable – the organisation must have the capability to attain its objectives; capability means staff, other resources, and competitive advantage.
- **S**pecific – objectives must be specific: e.g. '£3 million profit', not 'to do well this year'.
- **T**ime limited – objectives must have a stated date for achievement.
- **E**nds related – objectives must relate to achieving outputs (ends) rather than describing means (how).
- **R**anked – ideally, objectives should be ranked in order of priority.

Figure 6.1 The budgeting process



The budget

Constructing the budget

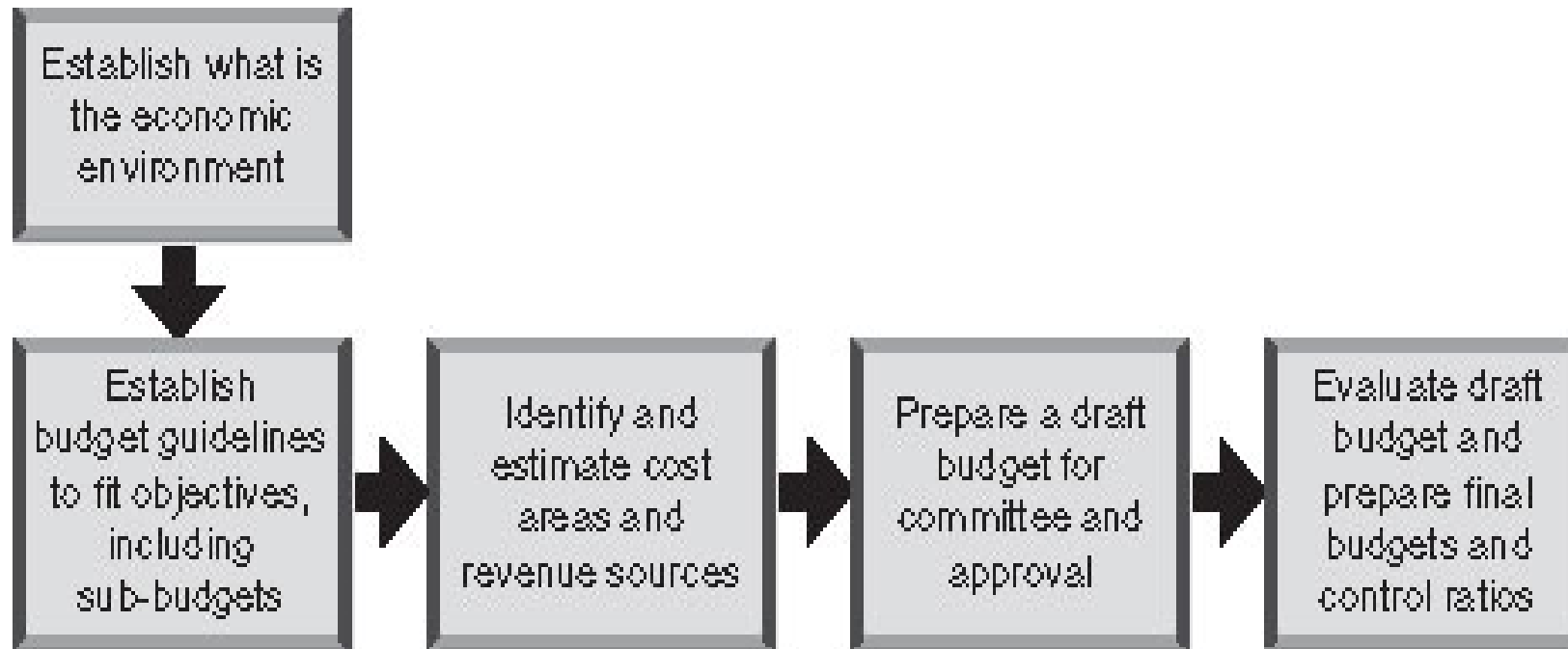


Figure 9.4 The budget process

Direct and indirect costs/benefits of events – tangibility of costs/benefits

- It is crucial to understand not only the event's direct costs and benefits (balance of accounts), but also the costs/benefits that are not related to the event organisers.
- These costs are often defined as tangible and intangible costs/benefits.
- Tangible costs/benefits are monetarily impacting stakeholder groups pertaining to the event organisers, while intangible costs/benefits are difficult to quantify in monetary terms.

The Budget

Constructing the budget

Income	£	Expenditure	£
Grants		Administration	
Donations		Publicity	
Sponsorship		Venue costs	
Ticket sales		Equipment	
Fees		Salaries	
Special programmes		Insurance	
Concession		Permits	
Security			
TOTAL		Accounting	
		Cleaning	
		Travel	
		Accommodation	
		Documentation	
		Hospitality	
		Community groups	
		Volunteers	
		Contingencies	
		TOTAL	

Figure 9.5 Generic budget - first level



Income	£	Ticket sales	£
Grants	Local government	Ticket sales	Box office
	Central government		Retail outlets
	Millennium Fund		Admissions
	Arts Council		SUB-TOTAL
	Other		T-shirts
	SUB-TOTAL	Merchandise	Programmes
Donations	Foundations		Posters
	Other		Badges
	SUB-TOTAL		Videos
	SUB-TOTAL		SUB-TOTAL
Sponsorship	In kind	Fees	Stalls
	Cash		Licences
	SUB-TOTAL		Broadcast
Individual contributions		Advert sales	Programme
	SUB-TOTAL		Event site
	SUB-TOTAL		SUB-TOTAL
Special programmes	Raffle	Concessions	
	Auction		
	Games		
	SUB-TOTAL		SUB-TOTAL
			SUB-TOTAL

Figure 9.7 Generic budget e third level

Table 6.4 An income statement

<i>INCOME</i>	<i>This year (£)</i>
Spectator Tickets	1,450
Other Ticket Sales	250
Sponsorship	1,700
Catering	220
Merchandising	130
Total Income	3,750
<i>EXPENDITURE</i>	
Volunteer Kit	700
Pool Hire	2,500
Marketing Activities	136
Administration	342
Total Expenditure	3,678
PROFIT/(LOSS)	72

<i>INCOME (£)</i>	<i>Actual</i>	<i>Incurred</i>	<i>Total</i>	<i>Budget</i>	<i>Variance</i>	<i>Direction</i>	<i>Note</i>
Spectator Tickets	1,450		1,450	1,350	100	F	1
Other Ticket Sales	250		250	0	250	F	
Sponsorship	1,700		1,700	1,800	−100	U	2
Catering	220		220	200	20	F	
Merchandising	130		130	100	30	F	
Total Income	3,750	0	3,750	3,450	300	F	3
<i>EXPENDITURE</i>							
Volunteer Kit	700		700	600	100	U	4
Pool Hire	2,500	0	2,500	3,000	−500	F	5
Marketing Activities	136		136	140	−4	F	
Administration	342	50	392	400	−8	F	
Total Expenditure	3,678	50	3,728	4,140	−412	F	
PROFIT/(LOSS)	72	−50	22	−690	712	F	6

Table 6.6 Actual versus budget comparison

Control and financial ratios

- Establish standards of performance
 - The budget, indicator ratios, success factors, milestones
- Identify deviations from the standards of performance
 - Comparison of budget to actual spend
- Correct deviations
 - By cutting costs, finding more money, or shifting resources

Control and financial ratios

The break-even chart

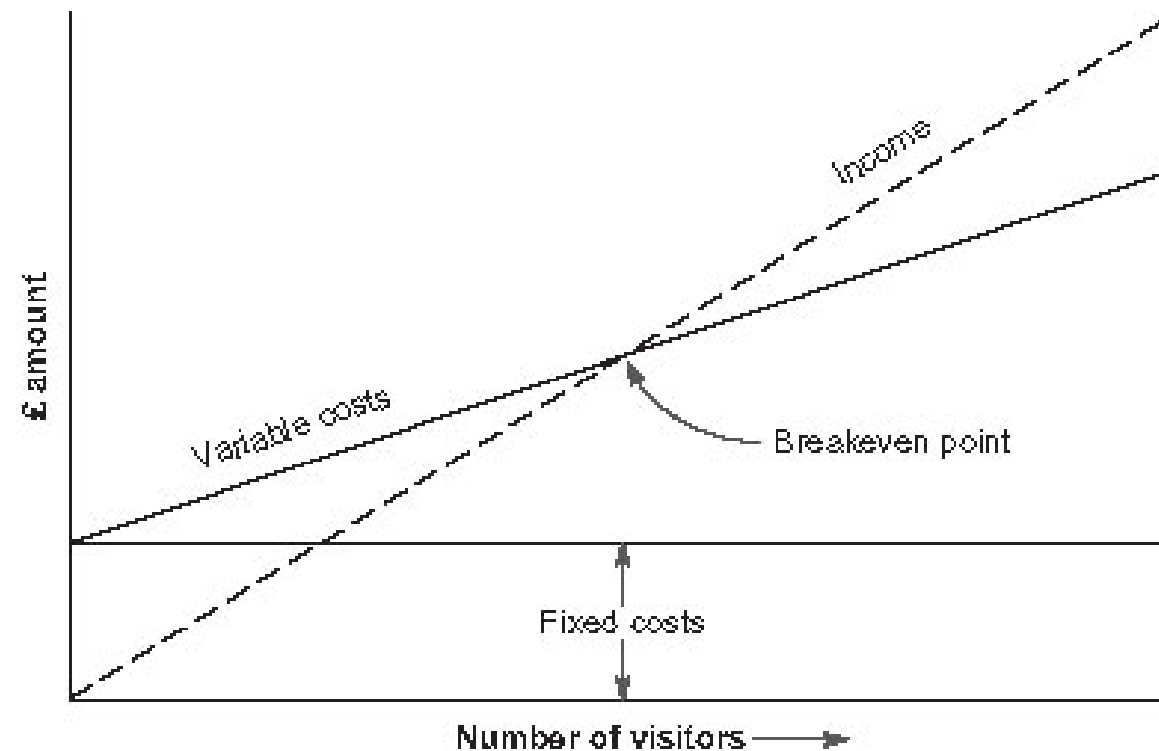


Figure 9.8
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Where Higher Education Began in Wales

Control and financial ratios

Ratio analysis

- $$\frac{\text{Current assets}}{\text{Current liabilities}} = \text{Financial strength}$$
- $$\frac{\text{Net revenue}}{\text{Investment}} = \text{Return on investment}$$
- Perceived value/cost pax = value for money

Control and financial ratios

Cash flow

- Importance to event management
- Tips in dealing with suppliers
 - Background information
 - Flexibility
 - Proper documentation
 - Full description of goods or services
- Change is more costly the closer to the event date

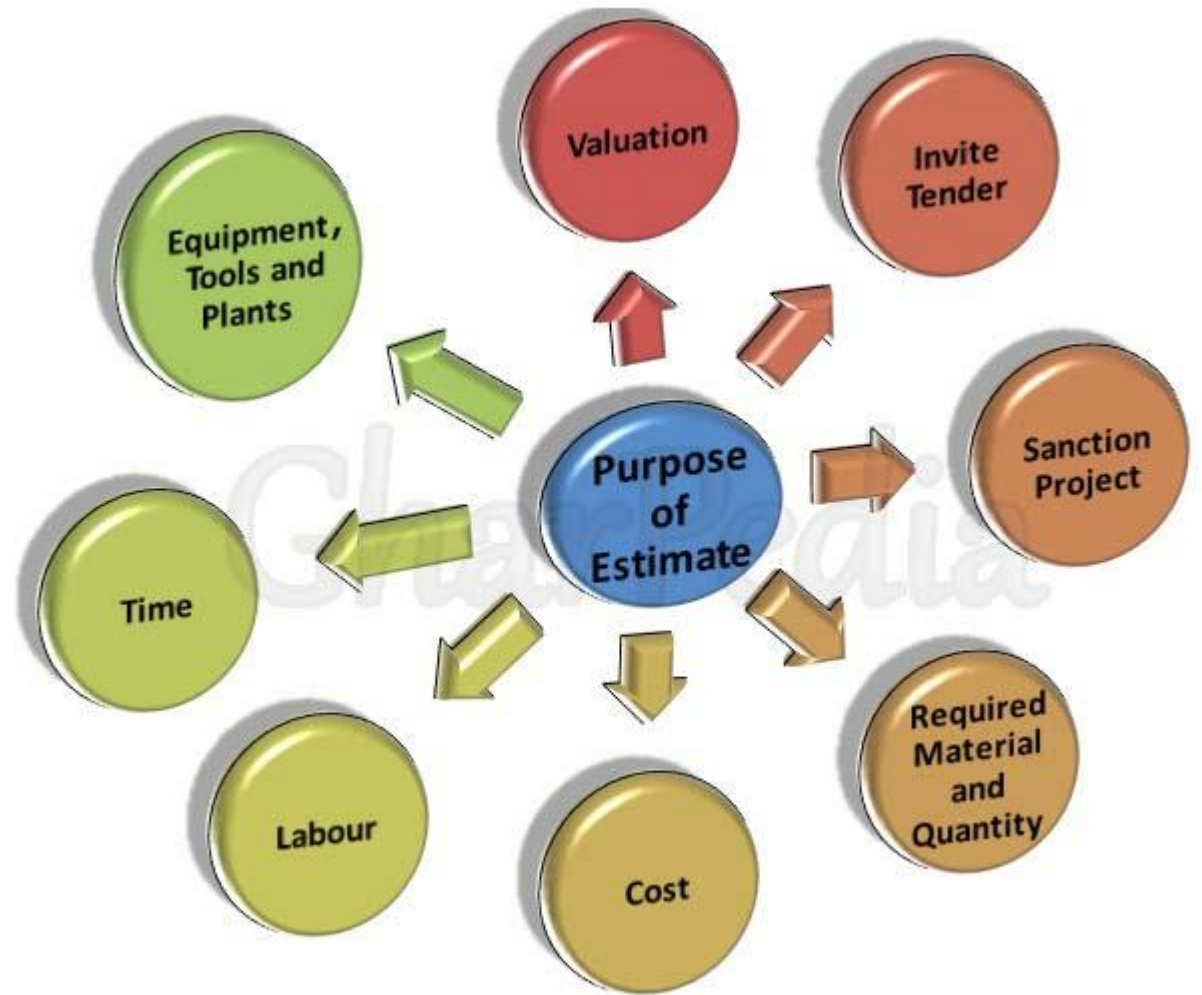
Costing and estimating

- Costing time:
 - A percentage of the overall event budget
 - A fixed fee as a lump sum or per hour rate
 - An incentive fee
 - A mixture of all three
- Sensitivity analysis:
 - The degree of influence the changes in costs have

Costing and estimating

Tips on reducing costs

- Publicity
- Equipment
- In-kind gifts
- Hiring charges
- Priorities cost centres
- Volunteers



Costing and estimating

Revenue

- Various revenue sources including:
 - Ticket sales
 - Sponsorship
 - Merchandising
 - Grants and fundraising
- Ticket pricing
 - Covering costs
 - Market demand perceived value



Costing and estimating

Tips for increasing projected income

- Ticket scaling
- In-kind support
- Merchandising
- Broadcast rights
- Sponsorship leverage
- Special features



Critical success factors for financing events

- 1. The dynamics of budgets**, especially in the bidding stages (inflation, exchange rates) need to be understood, tracked, continuously evaluated and discussed within the organisation delivering the event.
Thinking through different scenarios and playing through different situations helps to avoid making big financial mistakes.
- 2. Contingency planning** is crucial – some event owners ask the organiser to add 10% of all costs to the ordinary budget as a reserve.
Events have many, mainly negative surprises, where finances are concerned.
Showing stakeholders that the organiser is aware of potential surprises and has allowed for a reserve is also a sign of professionalism.

Critical success factors for financing events (Continued)

3. Very often **'big bucket' costs are not quantifiable** and need to be borne by **third parties**, mainly the public. Be honest with public funders and make them understand that **variability of costs is part of managing expectations**.
Especially working in a political context involves being very clear about the financial implications of the events.
4. The costs and potential revenues depend on situations that cannot be influenced. The **unpredictability of the results of a sports event** can have massive impacts. Such implications may also have impacts on the consumer behaviour of event tourists, positively in the case of sporting success and negatively in the case of unsuccessful sporting outcomes.

These situations need to be considered and may be part of an overall risk management strategy.

Critical success factors for financing events (Continued)

5. The **principles of good governance** (transparency, accountability, democracy, responsibility, equity, effectiveness, efficiency) may also be used as guiding principles for financing events.

For example, transparent decision-making policies within the event organisation may prevent conflict in the team.

6. **Planning liquidity** is also crucial to success.

Event budgets 'explode' just before and right after the event and high amounts of financial resources are required during this peak period.

It is crucial to guarantee good planning - who will be paid, spreading pay deadlines with service providers over longer periods before and after the event.

Critical success factors for financing events (Continued)

7. Written agreements have not always been part of the agenda in the event business and many organisers have had to learn from bad experiences.

Where financial management is concerned, a contracting service provider also means that there is a clear understanding of the costs, fewer problems and fewer misunderstandings whilst a legal framework also helps handle potential conflict.

8. Empowerment also on a financial level leads to increased motivation amongst employees.

Also, giving financial responsibility to the team members leads to increased commitment.

a clear frame and power limitations and control are crucial if unpleasant surprises are to be avoided after the event.

Critical success factors for financing events (Continued)

9. **Setting priorities** in terms of understanding the essentials and the desirables when budgeting and decision making.

In the event planning phase, internal (between the different functions) and external forces (from stakeholders) must try to bind as many **economic resources** as possible.

Clear strategies and shared goals help distinguish between the desirables (e.g. fancy opening ceremony) and the essentials (e.g. security measures required by the authorities).

10. The importance of **value-in-kind sponsorships (VIK)** is often underestimated.

Very often sponsorships are related only to cash income in an organisation, but for many sponsors, providing their products (e.g. cars, food, drinks, IT solutions) is cheaper; the products can be tested on potential clients and gain increased visibility among potential consumers.

Critical success factors for financing events (Continued)

11. Budgeting and control is a very important discipline in event management. Get the **right people** for this job who are prepared to be the 'bad cops' and to say 'no' more often than 'yes'. These people need to have a certain amount of experience and be completely opposed to a laissez-faire style.
12. Finally, it is very common to contract sponsors and providers at the very last minute, just before the event starts, so negotiating till the end to gain resources also requires a lot of energy and stamina.

References

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