



climbing the ladder



step by step finance
for social enterprise



edited by Andrew Bibby

social enterprise london



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Money. It's what every social enterprise needs.

No matter how good the business idea or how worthwhile the work being undertaken, if the money isn't there when it's needed then the social enterprise will flounder and fail.

So the first question for each new social enterprise naturally enough is: Where do we look for the money we need? The answer could be this booklet. As you will discover as you read on, social enterprises in London now have a growing number of places to turn for help in their search for finance. In fact, if the idea is a viable one, then it's more than likely that - out there somewhere - will be the finance that is needed, ready to be invested.

But there was an 'if' in that last sentence, which suggests a second question to be asked: How do we know if our idea really will be viable?

The creativity and imagination of the community organisations, groups and individuals who are developing social enterprises in London has meant that this sector has blossomed in recent years. But unfortunately creativity and imagination alone are not enough. Social enterprises also have to operate in the sometimes tough world of business.

This booklet, therefore, begins by helping social enterprises through the necessary financial planning stages involved in developing a new venture, including the components of the business plan, budgeting and cash flow forecasting. It's this planning process which will demonstrate whether or not the business idea is likely to be viable in the longer-term and which will lay the foundations for future success.

This preparatory work will also help to convince funders and investors that the venture is a good home for their money. The second section of the booklet, therefore, moves on to look at the different ways in which social enterprises can be capitalised. The pros and cons of grant-funding, loan finance and equity are, in turn, explored.

The work of business planning and raising capital is just the start, of course. Once a social enterprise is up and running, the task becomes one of keeping adequate financial records - and of knowing how to use these records to manage the business strategically. The third section of this booklet includes suggestions for book-keeping (including handling petty cash systems and coping with VAT) and, more generally, for the effective financial management of a trading venture. We also discuss briefly the issues to consider when planning for expansion.

The final section moves on to look at the two central components of the annual accounts, the profit and loss account and the balance sheet. Social enterprises, however, are not run just to maximise the 'bottom line' - so the booklet also gives some ideas and suggestions for ways to include an annual social and ethical audit as part of the annual accounting process.

introduction

The children's board game Snakes and Ladders can be a frustrating experience: a few good dice throws can see you rapidly making your way up the board towards the finishing square, when suddenly the counter lands on a snake, and you tumble back down. Running a social enterprise has its ups and downs too, of course. But to help you in your progress, we've included in this booklet what we hope will be helpful tips - some 'ladders' to give you a step up and some 'snakes' to warn you of possible pitfalls.

We hope you'll agree having read to the end of this booklet that understanding the money side of a business really isn't difficult. And we hope your own venture will flourish, knowing how to find the ladders and how to avoid the snakes.

Allison Ogden-Newton
Chief Executive, Social Enterprise London



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A viable business?

Social enterprises, unlike conventional businesses, are not run simply to make profit.

Nevertheless, social enterprises do have to be profitable. Unless at the end of the day there is more money coming in than going out, even the most committed or well intentioned social enterprise will be unable to keep going.

Like conventional businesses, therefore, social enterprises are strongly advised to check in advance that the proposed venture can be viable. This means undertaking some careful planning.



Social enterprises have an advantage, in that the business planning stage can be a collective endeavour. It's helpful to be able to talk through and criticise ideas together.

Profitability can be elusive.

For example, imagine that there are plans to launch a community-run shop in an area which has lost all its traditional shops. On average, the shop can expect sales of £6000 a month, and the goods sold only cost at wholesale price £4000. (In other words, the shop is operating on a **mark-up** of 50%). Surely a **gross profit** of £2000 a month sounds encouraging? Unfortunately not!

Take off the £1500 monthly wages bill, and the profit falls to £500.

Take into account all the overheads - everything from the premises costs to phone bills, stationery to bank charges - and what's left is the **net profit**. If overheads are £2000 a month, this shop will be making a net loss of £1500 a month:

Sales a month	£6,000
Cost of sales	(£4,000)
Direct labour costs	(£1,500)
Overheads	(£2,000)
Net loss a month	(£1,500)

Clearly, this business will soon be gone. To make it profitable, something has to be changed. There are various options to discuss:

- The mark-up could be increased
- Perhaps the sales could be increased? (better range of goods? better location?)
- Perhaps the other costs could be reduced?

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These revised figures look slightly more promising:

Sales a month	£7,000
Cost of sales	(£3,500)
Direct labour costs	(£1,500)
Overheads	(£1,800)
Net profit a month	£200

Still, even now there's very little room for error.

The Business Plan

The process of planning and discussing a new enterprise conventionally culminates in the production of a business plan. A business plan is not:

- a mysterious document which only those with business degree will know how to complete
- a tedious task required by banks or funding agencies
- a quasi-magical talisman which will ensure success
- something to complete and then forget about

The business plan is:

- As much a process - of thinking, planning and research - as an end document
- A written explanation of the reasons why it is more likely than not that the enterprise will be viable
- A guide to help you once the enterprise is launched

Business plans conventionally include the following types of information:

- **The people**
Who will be involved? What skills and experience do you already have? What other skills might the enterprise need, and what can be done to meet this need? What will happen if key people are unable to carry on working (illness, moving away, new jobs, etc)?
- **The products or services being offered**
What is special about the products being manufactured or sold, or the services being offered?
- **The market**
Why do you think there is a market for your products/services? (What efforts at market research have been done?) Is the market increasing, static or declining? Who are the

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competitors, and why will you be able to compete successfully with them? What is a realistic level of sales?

■ Premises

What premises will the enterprise need? What is the right location for the business, and what will happen if you are unable to obtain the premises identified, or have to move?

■ Equipment

What equipment (including such things as machinery, vehicles, etc) will the enterprise need?

■ Financial projections

How do you expect your business to do financially in the first few years of its life? What pricing policy do you plan to adopt? What do the budgets and cash-flow forecasts reveal about likely prospects?

■ The capital you will need

All businesses require capital to start. The business planning process will reveal just how much capital you will need.

We will be focusing in this booklet just on the financial aspects of running a social enterprise. If you need advice on some of the other issues tackled during the development of a business plan, a list of organisations who may be able to help you is given at the end of this booklet.



All too often, people spot vacant premises and are tempted to plan a business around it. This is the wrong way round!

Pricing

All businesses need to work out how they will price their goods or services. As we saw above, a retail shop can mark up the stock substantially and yet still struggle to make a profit.

Social enterprises have an extra issue to think about, in reconciling pricing policy with core social aims. But there is no advantage in fixing prices at a level which is readily affordable to the customer if it means selling items at below unit cost.

Inexperienced businesses often price their goods or services too cheaply. Generally, this is because they have thought about just the direct costs and not fully taken into account the business overheads.

Developing a pricing policy is a combination of two things: what you think your prospective customers will be prepared to pay (what 'the market will stand') and what direct and indirect business expenses you incur.

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Below are some pricing tips:

- Create a pricing policy that is understandable to the customer, manageable and predictable in order to project your income for several years into the future.
- Consider using differential charges, for example based on income level, or providing subsidised places if you are providing a service. (This is not just good practice, it's also good business sense in that it expands the overall market. Think how train companies use price differentiation with different fare tariffs, for example, to widen the number of people who use trains.)
- It may be possible to set up block contracts with local large buyers.
- Enter into mutually beneficial partnerships where the partner pays for or subsidises some of the products or services.

Customers may be much more price sensitive for some items than others. Conventional retailers know, for example, that shoppers are very aware of the price of everyday items, such as milk or bread, but much less price sensitive about other items - the mark-up on these latter goods can be much higher and shoppers can still think that they are getting good value.

Though social enterprises are unlikely to want to emulate this fact of business life, there are even examples where charging more brings in more sales! - because people feel that, if prices are low, they may not be getting good value.

There will always be a certain level of estimation in developing a pricing policy, but one thing is clear: it's impossible to get it right, if you don't know what your business costs will be. We will now look at this in more detail.

Fixed and variable costs

Some business expenses are directly tied to your sales. If sales go up, these costs also go up proportionately. These are known as variable costs.

Typically variable costs may include:

- Raw materials.
- Distribution costs.
- Overtime payments and temporary employees.
- Wages directly linked to output levels.

There are other costs you will have to meet, regardless of however well or badly your business is doing. These are your fixed costs.

Fixed costs may include:

- Rent, rates and insurance.

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- Bank interest, financing costs.
- Maintenance and repairs.
- Utilities bills (phone, lighting, heating, etc).
- Salaries.
- Planned advertising spend.
- Administrative costs.
- Depreciation of fixed assets.

It's possible in some businesses to work out the average unit cost. Let's say that you're a social enterprise manufacturing wooden seats for use in children's playgrounds. You produce two thousand seats a year. If your fixed costs are £50,000 a year and variable costs (at £5 per seat for the timber) are £10,000, then the unit cost per item is £30. You'll have to charge at least £30 to expect to be profitable.

But the extra marginal cost of each additional seat you make and sell is much less than this - just the variable cost of £5, in fact. If there is some way in which you can maintain your sales of 2000 seats at £30+, you can sell further seats at anything above £5 and increase your profits. This is what is known as marginal cost pricing, and is one reason why companies often seek to use price differentiation techniques (think of the railways again).



Social enterprises may be able to use marginal cost pricing in creative ways, for example to offer goods and services at 'subsidised' prices to groups in the community who would not otherwise be able to be customers. But you will need to have some way to justify differentiating between your customers.

As well as your fixed and variable costs, you will also periodically have to make one-off payments for capital items of equipment which you expect to last for several years. The accounting convention here is to allocate the cost over an appropriate number of years: for example, if a new computer cost £2000 but you expect it to last four years, you could include a notional element in your fixed costs of £500 each year for four years (this is what is known as 'depreciation'). Incidentally, there are special rules ('capital allowances') when it comes to the tax treatment of these items of expenditure.

Staff costs

Usually the most significant item of expenditure in any business is the staff cost. Remember that when you have employees, you have to meet not only their wages but also the additional

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employer's national insurance contribution (this is paid as part of the Pay As You Earn payments which every employer has to make regularly to the Inland Revenue). The employer's NI contribution is currently 12.8% of all earnings above the NI threshold. You may also want to contribute as employer to a pension scheme for staff, and/or provide other benefits (for example, childcare vouchers).

Remember also that there will be other costs of employing staff. These include initial recruitment and selection costs and training costs. During holiday times and periods when staff are off work sick, there may be a need to take on temporary cover or agency workers, again at additional cost.

Preparing an operating budget

A budget is an estimate of how much you expect to pay out in expenditure and to receive in income during a given period.

Preparing an initial budget is a key part of working out if your proposed social enterprise will be viable. A budget should certainly be produced for the first twelve months, and it is often advisable to try to estimate a second year's budget as well.

An example of a rudimentary budget was given at the start of this section, in the example of the community-led shop. To prepare a useful budget, however, you will have to break down your income and expenditure into appropriate categories. Whilst it can be difficult to know in advance exactly what figures to put in for all your items of expenditure (particularly, for example, if you have yet to confirm the premises you will be using) try to be as realistic as possible.



Don't forget to include the cost of any borrowings (interest on loans, bank overdraft charges, etc).

Having given the budget your best shot, try a few 'what if' scenarios. For example:

- What if our sales are 10% less than we hope? Or 25%?
- What if our premises costs are 10% or 25% greater than we expect?
- What if we suffer from bad debt?

If you use a computer spreadsheet, it is relatively easy to undertake a number of 'what if?' scenarios. But make sure that everyone in your social enterprise planning group can understand how the figures are being calculated.

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When adjusting sales, remember that there will be a knock-on effect on some figures for expenditure: whilst fixed costs won't normally need to be adjusted, variable costs will change.

You may also want to create 'mini-budgets', that is income and expenditure for each product or service you plan to offer. This will help identify any particular strengths or weaknesses in your business concept.

Your completed budget may look something like this. This example is of a community childcare nursery taking about 30 children (by the way, don't use these figures for real!):

Income: full rate	£125,000	
concessionary rate	£ 90,000	
Total income		£215,000
Expenditure:		
Staff costs (incl NI)	£150,000	
Materials	£ 10,000	
Marketing costs	£ 5,000	
Heat, light, etc	£ 5,000	
Admin costs, phone, postage	£ 5,000	
Building repairs	£ 4,000	
Business rates	£ 4,000	
Insurance	£ 4,000	
Interest on loans, bank charges	£ 3,000	
Accountant	£ 500	
Rent of building	£ 20,000	
Other expenses	£ 2,500	
Depreciation on capital items	£ 1,000	
Total expenditure		(£214,000)
Net profit		£ 1,000

Understanding cash flow

Most people assume that businesses which fail do so because they are not profitable. Unfortunately, it's more complicated than this. It's possible to have a business which is very comfortably profitable, but which still fails - simply because it runs out of cash.

An example will make this clear: imagine a shop which has annual sales of £200,000 and annual expenditure of £175,000 - a healthy profit of £25,000. But now assume that it has to pay cash up front for its stock, that it holds its stock on average on the shelves for several months, and that it offers its customers a period of credit before they have to pay. Suddenly, the viability of the business looks much more problematic.

In fact, businesses which fail do so normally not because they have suddenly crossed a mysterious line from profitability into loss-making: they fail because of a cash-flow crisis.

The final part of planning your social enterprise to ensure that it is viable, therefore, involves

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forecasting the way in which money will flow into and out of your business - the cash flow.

The cash flow forecast is one of the most important tools in business planning. It may look complicated, but it carries a simple message: it tells you whether your business is generating cash or using it up. It also reveals exactly how much money your business will need to borrow – your business's capital requirement.

Producing a cash flow forecast means predicting when you expect money to be coming into and leaving your account.

- If you sell on credit, it is the time when you receive payment which is relevant, not when the sale is made.
- Similarly, if your suppliers give you credit terms, you should record the cash outflow at the time when you actually make the payment

The main inflow of cash is usually from sales. However, with social enterprises there may also be a mixture of grants and sponsorship payments. Capital invested in your enterprise (for example, in the form of business loans) will also appear in the cash flow forecast, at the time when the investment is made.

On the outgoings side will appear the business expenditure which you have already identified when preparing the budget. Some items of expenditure will appear regularly, every month: salaries, rent and interest payments on loans are possible example. Some (such as phone bills and electricity bills) will probably appear quarterly. There may be other payments which are only made annually - insurance premiums are one example. These appear in the cash flow forecast for the month during which they are made.

Logically enough, the full purchase price of any capital equipment acquired will also have to show up on the cash flow forecast.

Cash flow forecasts are conventionally produced on a month-by-month basis, though it is also possible to produce weekly forecasts.

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Let's look at an example - the same childcare nursery whose budget is given above. Here are the predictions for the first four months of its first year of trading. (The brackets round a figure conventionally denotes a minus number).

	Jan	Feb	Mar	Apr
Bank balance at start	0	(2,650)	(10,450)	(13,550)
Receipts				
Income from children's fees	0	10,000	13,000	17,500
Grants	0	0	0	0
Loans	20,000			
Total income	20,000	10,000	13,000	17,500
Payments				
Staff costs	2,500	12,500	12,500	12,500
Materials	5,000	0	0	2,000
Marketing	2,000	500	500	500
Heat/light	0	2,000	0	0
Admin	750	500	500	500
Building	2,000	0	0	500
B Rates	350	350	350	350
Insurance	4,000	0	0	0
Interest	0	0	300	300
Accountant	0	0	0	0
Rent	1,750	1,750	1,750	1,750
Other exps	300	200	200	200
Capital	4,000	0	0	0
Total exps	22,650	17,800	16,100	18,600
Bank balance at end	(2,650)	(10,450)	(13,550)	(14,650)

Because the nursery is starting up, there is no income forecast for the first month, and the projections sensibly assume that income will only gradually build up during the spring. As can be seen, there are considerable setting up costs, including work on the building and capital equipment purchase.

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You may want to take a few minutes to look through this cash flow projection, to see if you can work out the assumptions which the group who prepared it used and to see whether you agree with their thinking.

The net effect is that, even with a business loan of £20,000, the enterprise very quickly runs short of cash. In fact, the projection shows a projected cash deficit of almost £15,000 by the end of April – even though the figures come from a budget with an anticipated first-year profit of £1000.

What should you do if your own cash flow forecast shows a cash deficit like this? There are various possibilities:

- If there is a more or less permanent shortfall, you have underestimated the long-term capital funding requirement of the business
- Short-term deficits (for example, because a retailer has built up stocks for Christmas) are conventionally funded by bank overdrafts. Overdrafts are a very expensive and unsatisfactory way of funding longer-term capital needs, however.
- It may be possible to postpone some items of expenditure (ask your suppliers for a period of extended credit, perhaps?), or improve the speed at which your customers pay you (tighten up on your credit control, for example).



A business that purchases on credit and is paid in cash (such as a retailer) is at a great advantage in cash flow terms.



The more warning you have of approaching troughs in the cash flow, the more time you have to deal with them. That's why it pays to do cash flow forecasts.

Most social enterprises will be required to register for VAT. VAT is discussed in more detail later in this booklet, but note that VAT-registered businesses will need to include VAT payments (usually made quarterly) in their cash flow forecasts. On the income side, part of the sales income received will reflect the VAT component. It can be helpful to separate out this VAT element, to give it its own row in the income section.

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As with budgeting, a series of cash flow projections can be worked out, to cover ‘what if?’ scenarios. How would the cash flow be affected, for example, if sales income falls? If customers are slow in paying?



When tweaking your cash flow forecast to show increased sales, remember that those extra sales will also mean an increase in your variable costs – so there will need to be changes on the payments side, too. Unfortunately, it’s easy to forget this!

Remember that cash flow difficulties don’t necessarily mean that the business is unviable. It may simply be under-capitalised.

- A mature, profitable business will usually be generating cash
- A younger, growing business may be using up cash even if it is profitable.

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Having undertaken the business planning work described in the first section of this booklet, you should know two things: firstly, whether your proposed social enterprise is likely to be viable, and secondly, exactly how much capital the enterprise will need.

As the cash flow forecast demonstrated, capital is needed not just for fixed assets - the obvious capital items such as the purchase of premises, machinery, equipment etc - but also to tide the business over the everyday ups and downs in the cash flow. This is known as **working capital**.

It may not be immediately obvious where this working capital gets invested: in fact, it is the money tied up in any raw materials, stock and unsold goods you have, your bank account balance, and in the money which is owing to you for goods you have already sold on credit (less any money you in turn owe your creditors).

All businesses need capital. The key is to find the right sources of capital, on the right terms.

Conventional businesses usually look to a mix of equity funding and loan financing for their capital requirements. Social enterprises may also be able to find grant funding. We shall consider these in turn, in reverse order.

Grant funding

Social enterprises are potentially well placed to access grant funding - the obvious advantage being that grants are injections of money into your venture which do not need to be repaid. Grants also do not require servicing - in other words, they do not need interest payments or dividend payments which other forms of capital funding will require. They are therefore not a drain on the future profits of the business.

Grants may be available from a wide range of charitable trusts, government and funding bodies. Further information is provided at the back of this booklet.

If the advantages to grant funding are obvious, there are also disadvantages to be aware of:

- Grants can cause mission drift. In other words, organisations adapt what they do to meet the requirements of the funding - rather than doing what they would really like to do.
- Grant funding can frequently be tied to particular projects, leading to fixed-term projects which disappear once the money dries up.
- Some funding requires organisations not to hold cash surpluses or build up reserves. This effectively discourages a business-like approach to running a social enterprise.
- Some funders, especially charitable trusts, will make grants only to registered charities. Charitable status may not be appropriate or available for social enterprises, as trading businesses. Some social enterprises develop a parallel educational charity, which is run alongside the trading arm. (Traidcraft and Centre for Alternative Technology are two well-known examples with this sort of structure).

Loan financing

The basis to loan financing is easy to grasp. A fixed amount of money is borrowed, normally over a fixed period of time (the term). Interest is payable, and the loan (the principal) also has to be repaid, either at the end or as you go along.

When thinking about taking out a business loan, there are some questions to ask:

- What is the interest rate being charged? Normally, the best way to compare different loans on offer is to compare the **annual percentage rate (APR)** of interest. Normally, the lower the APR the better value. (Exceptionally, higher APR figures may be acceptable for very short term loans of less than a year).
- What is the term (period) of the loan? How does this relate to the anticipated first few years' development of the business? How will the repayment be made?
- What security is being sought?

Banks and other lenders try to protect their money by asking business customers to provide security - in other words, something which can be acquired and sold if the business is unable to repay its debts. A bank may take a **legal charge** over particular assets (such as equipment or property) owned by a company. Banks also frequently ask those involved in business to offer personal security - for example, a business loan may be secured against the business person's own home. If the business fails, the house may be lost.



Whilst those starting a conventional small business may feel that they have to agree to offer personal security against business borrowings, social enterprises should think long and hard before following this road. Banks will naturally try to protect their lending as much as they can, but nevertheless arranging a loan is a process of negotiation: social enterprises should not hesitate to ask banks to think again if personal guarantees are initially requested.

The government's Small Firms Loan Guarantee scheme is designed for small firms, including social enterprises, who have failed to obtain a bank loan because of a lack of security. The scheme applies to loans to start-ups of between £5000 and £100,000; the government helps remedy the lack of security by guaranteeing 75% of the loan, in exchange for a 2% a year interest premium. Information is available from participating banks and from the DTI website.

Social enterprises have a number of places to look for loan capital:

- Banks
- Specialist loan funds, for example from Community Development Finance Institutions (CDFIs)
- Specialist micro-finance schemes

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Banks

Banks are the primary source of business loan finance for smaller businesses in Britain.



Whilst banks, and their staff, vary in their experience of working with social enterprises, all are likely to respond more favourably if they are presented with a well-argued business plan. It is worth remembering that banks make their money by lending, and therefore need borrowers - the relationship is not entirely one-sided!

As well as the familiar High Street names, the Co-op Bank, Charity Bank and Triodos Bank have particular links with the social enterprise movement (this does not mean that they are any less commercial in their lending decisions). Further information is available at the end of this booklet.

One technique currently being explored by some banks to reach higher-risk business customers is to work through, or in partnership with, Community Development Finance Institutions (see below) and specialist banks.

Community Development Finance Institutions

CDFIs are a relatively new idea in Britain. They are financial institutions which have been set up to help social, economic and physical renewal in under-invested communities, including socially deprived areas where people have difficulties in accessing mainstream finance.

CDFIs can provide funds for start-up capital, for working capital, for bridging loans, for property and equipment purchase, for business purchase, for marketing campaigns and for other business and personal financial needs. Many CDFIs offer support with business plans in order to make a potentially viable social enterprise 'loan ready'. The umbrella group for CDFIs in the UK is the Community Development Finance Association.

Banks are major funders of CDFIs, and some are testing the commercial viability of CDFIs by providing loan finance. For example, Barclays has lent to Birmingham-based Aston Reinvestment Trust. NatWest has a network of regional Community Finance Funds, capitalised through its Community Bond, which invest in local projects that are not yet eligible for bank loans. HBOS (Halifax/Bank of Scotland) has provided seed funding to The Big Issue to develop BIGinvest, a wholesale intermediary that will lend to CDFIs and large social enterprises.

The provision of finance or a guarantee to a social enterprise by a CDFI can be one component in a lending package which also includes lending from mainstream banks.

Details of CDFIs of interest to social enterprises in London can be obtained from the Community Development Finance Association (see information at the end of this booklet).

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Micro-finance

As the name suggests, micro-finance schemes are targeted at small businesses that require relatively small amounts of money (up to £5,000) for a relatively short period of time.



Some larger credit unions are now in a position where they are able to undertake lending to members for business purposes.

Equity capital

Conventional businesses are owned by their shareholders, who share the profits through dividends. The original investors put equity in the business, with their financial contribution acknowledged through the share certificates they received (as the name 'equity' implies, shareholders share the rewards in accordance with the number of shares they hold). Investors hope that the company they are helping to create will do well. However, if profits are not forthcoming, they (or those who have subsequently bought the shares off them) have no legal right to any reward and could indeed lose their capital if the company goes under.

In other words, whilst loan capital requires interest payments which eat into the ultimate profitability of a business, equity capital does not. For this reason, it is considered good practice conventionally for businesses to raise a significant part of their capital needs in the form of equity rather than through loan capital.

The role of equity capital in social enterprises is a complex, and arguably controversial, one. Co-operatives, for example, have traditionally been concerned to ensure that profits are used to benefit members or to develop the business, not to reward external investors.

Note that some forms of legal incorporation used by social enterprises do not permit equity funding. This is the case, for example, with companies registered under the Companies Act and limited by guarantee (limited companies with share capital, by contrast, can of course obtain equity finance). Organisations registered under the Industrial and Provident Societies Act (as many co-ops are) have powers to issue 'shares', though these are in many respects closer to loan capital than true equity. Social enterprises which choose in future to establish themselves under the government's proposed new Community Interest Company (CIC) legal framework will have the opportunity to attract equity.



If equity is to be permitted in a social enterprise, you will need to discuss the way in which investors' interests can be squared with the social or ethical aims of the venture. Clearly, a 'social enterprise' which was concerned to maximise profits in order to maximise shareholders' dividends would be hardly distinguishable from a conventional for-profit business.

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Recent years have seen the beginnings of a discussion about possible ways in which equity capital can be utilised in social enterprises, for example through hybrid structures which recognise the social aims of the undertaking but which also acknowledge investors' interests as stakeholders.

A number of sources of equity capital may be available to social enterprises legally able, and willing, to accept it. These include:

- Investments by supportive individuals ('ethical' or 'alternative public offerings')
- Venture capital funds
- Business angels

Ethical public offerings

A number of well-known social enterprises, including Traidcraft, Café Direct, Ethical Property Co, ICOF and Centre for Alternative Technology, have all raised quite substantial (£1m-£5m) sums in share capital by appealing to supporters and others who are committed to their aims.

Because these share issues are regulated through the same mechanisms as ordinary share issues, the legal requirements to be met (including the drawing up of the prospectus) are significant and therefore the costs associated with ethical public offerings are high. As a result, this method can only be used where relatively large amounts of share capital need to be raised. (Enterprises registered under the Industrial and Provident Societies Act are likely to have slightly fewer constraints than those registered under the Companies Act).

There is, of course, no guarantee that enough individual investors will step forward with the funds a social enterprise is seeking. Nevertheless, recent issues have generally been quite successful (a small number of ethical public offerings have also managed to attract interest from institutional investors, looking for holdings for ethical unit trusts.)

These 'social' share issues provide long-term investment capital, not least because it is difficult for investors to sell their shares subsequently. Recently Triodos Bank has launched a limited 'ethical exchange' service, designed to put sellers of five shares in touch with those prepared to buy. The Co-op Bank is also considering a similar service.

Venture capital

Venture capital is high risk capital in search of potential high returns. Conventional venture capital companies look for promising start-up or expanding businesses which may be able to grow fast and produce significant profits. Hopefully, these successful companies then more than make up for those which fail to develop. To help maximise the chances of success, VC companies look to play a major part in the strategic management of the companies in which they invest, typically by taking up directorships. VC companies also look for exit strategies, in other words a way to extract their investment after a few years and move on.

When the relationship works, the close involvement and commitment of a VC company to a

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new or expanding business can help those whose business it otherwise is - though not every relationship between entrepreneur and VC company is plain sailing.

Social enterprises may feel that the VC approach clashes with their social or ethical aims. Nevertheless, recent years have seen a number of organisations set up to adapt VC principles to the needs of social enterprises.

In London, Greater London Enterprise (GLE) provides access to VC-type financing through a number of schemes whilst Foursome is a venture capital firm that invests in British, European and North American socially responsible businesses. Details of both are given at the end of the booklet.

Business angels

Business angels are private investors who want to put their money in high risk but potentially high return investments. (The name was originally given to those 'angels' who were prepared to help the theatrical profession by investing in new productions).

London Business Angels is a 'match-making' service under the auspices of Greater London Enterprise, which aims to partner angels with suitable new business opportunities.

'Patient capital'

Venture capital companies, as we have seen, look for short-term growth and profits and for fast exit strategies. This can sometimes work against long-term development of sustainable businesses and jobs.

By contrast, 'patient' capital implies a long-term financial investment with terms and conditions that do not require immediate repayment. The need for patient capital for social enterprise has been the subject of discussion in recent years, and there have been a number of pilots and programmes developed.

The aim for social enterprises is to develop sources of patient capital where the investor anticipates both a social and financial return, and is prepared to tailor the terms of the investment to the potential of the individual community or social enterprise. Patient capital includes both equity and loan finance.

For patient capital to become an established method of finance, understanding of its potential and how it can be used has to be substantially raised among social enterprises, their advisers and funders.

Current efforts are being made, through the Adventure Capital Fund and elsewhere, to modify particular tools such as the 'balanced scorecard', social return on investment (SROI) and social auditing methods so that they are appropriate, feasible and cost-effective for use by social and community enterprises. These need to be simple and useable across a range of sizes and types of enterprise. They must work to timetables that recognise that the impact of many enterprises on their target communities will take time to have effect.

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Substantial further growth in social enterprise depends on private sector and charitable funders joining in partnership with public sector funders. An ideal would be a 'three-legged stool' approach to financing and supporting social enterprise, where private sector, public sector and the charitable sector work together.

Alternatives to the search for capital

There are a number of ways - apart, of course, from running a tight business, with strong credit control procedures - in which enterprises can reduce their working capital requirements, and therefore their overall capital needs.

Factoring

Factoring is a service that allows you to obtain up to 90%-95% of the value of an invoice as soon as it has been issued. For a fee, the factoring company will advance you the money you will ultimately be receiving - in other words, effectively paying the invoice in advance. The factoring company then takes on responsibility for collecting payment of the invoice.

Factoring can be a useful tool for companies with cash flow problems, but it has its costs and reduces overall profitability.

Leasing arrangements

Equipment (such as vehicles, PCs and machinery) can be leased rather than bought outright. This reduces the need for capital investment, though will have an on-going negative effect on profitability.

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Book-keeping

Record-keeping is an essential part of the work of running a business.

If you don't record the business transactions you make:

- You will find it very difficult to produce the annual accounts which you are legally obliged to submit.
- You will be less likely to pick up on your own or other people's mistakes.
- You will find your accountant will have to do more work, and will charge you more.
- You will be unable to monitor how well your business is doing.



Different businesses need different accounting needs, and there is no point in having unnecessarily complex procedures. Keep it simple.

You can choose to use business accounting software or paper-based records.

Most social enterprises will typically need records kept for the following transactions:

- Bank book: to show, on a daily basis, the money entering and leaving your bank account.
- Sales process. Sales made, including easily accessible list of your current debtors (people who owe you money).
- Purchase process. Purchases made, including easily accessible list of your current creditors (people you owe money to).
- A register of your fixed assets.
- Employee records, including Pay As You Earn records.

For businesses where sales are made for cash, rather than on credit, it may be possible to account for sales simply through the bank book.

It is good practice in the bank book to analyse income and expenditure across a series of categories. For example, a retail shop might decide to categorise expenditure in the following sections: stock for resale, wages and labour costs, premises costs, general admin expenses, telephone, advertising, motor expenses, legal/professional charges, interest/bank charges, other expenses. If the business is VAT registered, another column should be set aside for the VAT element of each item of expenditure.

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Some items of expenditure may fall in more than one category. For example, a purchase of £1175 of stock from a wholesaler might include items such as light bulbs and cleaning materials for use by the shop itself. These need to be accounted for as 'general admin' expenses, rather than as 'stock for resale'. This purchase would be entered as follows:

Date	Paid to	Total	Stock	Admin	...	VAT
1st Jan	Bulko wholesalers	1,175.00	900.00			100.00		175.00
2nd Jan	...							

In this example, as the business is VAT registered, the £175.00 element which represents the VAT component of the payment has been separately itemised in its own column.



However good your book-keeping systems, you will get into difficulties if you don't keep your records up-to-date. Do the 'books' regularly!

Petty cash

Tight procedures are particularly necessary if you intend to have a petty cash system.

Where possible, it is much better to avoid petty cash altogether: bank all cash received, and pay for all items of expenditure by means of cheques, direct debits etc.

However, if you do feel that petty cash is essential, perhaps the best way to deal with it is through what is known as an 'imprest' system. This is simple to operate. Decide first of all the maximum amount of petty cash you will need - let's say £50. Start the system by drawing out this amount from your bank account, into a secure petty cash tin.

Each payment made from petty cash should be in exchange for a receipt or voucher. At any time, therefore, there should always be cash and receipts/vouchers in the tin which together total exactly £50.

At the end of a set period of time (typically a month), replenish the cash so that once again there is £50 in the form of cash. The vouchers (which together will add up to the money drawn from the bank) are now stored with all the other records of expenditure made. The bank book will show a transaction something like this:

Date	Paid to	Total	Stock	Admin	...	VAT
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Date	Paid to	Total	Stock	Admin	...	VAT
31st Jan	Petty Cash	27.31	23.24	...	4.07
...	...							



Don't allow sales money or other income to be handled through petty cash, and don't pay for items from 'till money'. Bank all income.

VAT

Mention has already been made on several occasions of Value Added Tax (VAT). Normally, if your business has a turnover above the annual VAT threshold, you will be obliged to become VAT registered. (This is in relation to goods or services which carry VAT, even those where the VAT rate is 0%). The annual VAT threshold for 2004-5 was £58,000.

Although the details of VAT can be complex, the basic principles are straightforward:

- as a registered VAT business, your customers pay you not only your own price but also an extra VAT element on top. (The standard VAT rate is 17.5%, so that for many goods and services you would charge £117.50 for a 'real' sale of £100).
- you pay VAT on the goods and services you buy for your own business
- periodically, you pay the VAT office the VAT money which you have collected from your customers; at the same time, you can claim back the VAT you paid on your own purchases.



If you are VAT registered, remember that some of the money you are receiving from your customers is not your own money – it belongs to the government and will in due course have to be paid across. Don't get confused and think you're better off than you really are!

Try to look at VAT in a positive way. Although you are being asked to collect tax from your customers, you are allowed to hang on to it until the next VAT payment is due – so that in the interim you are effectively being lent this money interest-free!

As a VAT registered business, you can also claim back the VAT element on your own business expenses. If you weren't VAT registered, all these items of expenditure would cost you more.



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VAT is charged at various rates. Whilst 17.5% is currently the standard rate, some items (such as fresh food, books and children's clothes) have a 0% VAT rate. Domestic energy charges for electricity and gas carry a 5% VAT rate.

Some things (such as some forms of travel, insurance and property transactions) are exempt from VAT altogether.

Even if your business turnover is below the compulsory VAT threshold, in some instances it may be worth considering voluntary VAT registration since you will then be able to claim back the VAT you pay on your business purchases. This is particularly advantageous if you are selling 0% rate goods, since you will not have to charge your customers any more than you were before. If you are selling standard rated goods or services, you will only be more expensive in real terms if your customers are individuals or non-VAT registered businesses - and because you will be saving the VAT on your own purchases, you may be able to bring down the prices you are charging.

For VAT-registered businesses, there are rules about the way in which VAT invoices should be produced. A full VAT invoice should include a unique identifying number and your name, address and VAT number. It should also include the invoice date, the tax point, the date of issue (if this is different from the tax point), the type of supply (such as sale or rent), a description of the nature and amount of the goods or services, your cash discount rate, the VAT rate, the total excluding VAT, the VAT amount and the total payable.

If VAT is likely to be a concern for your social enterprise, more detailed advice is available from business advice agencies and from the VAT authorities.

Corporation Tax

Corporation tax is a tax on company profits. At time of writing, however, small businesses have no tax to pay on the first £10,000 of profits. The standard small business corporation tax rate is 19%, payable on profits above £50,000 (a graduated rate applies for profits between £10,000 and £50,000).

Management accounting

One of the most important reasons for keeping adequate business financial records is so that you can monitor how your business is performing. Are you meeting the sales targets you predicted, for example? Are your costs at the level you anticipated?

In other words, you need to check the predictions you made when preparing the business plan with real life. This means going back to the key financial projections, particularly the cash flow forecast.

Conventionally, cash flow forecasts are drawn up with two columns - one on the left which you complete when you first make the projections, and one on the right where you enter, month by month, the actual figures.

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Let's look again at the cash flow forecast produced by the community childcare nursery, and imagine that the business has now started, and is in its third month of trading. The actual figures for January and February can be entered in the forecast, as follows:

	Jan	actual	Feb	actual
Bank balance at start	0	0	(2,650)	(128)
Receipts				
Income from children's fees	0	0	10,000	12,215
Grants	0	2,500	0	0
Loans	20,000	20,000	0	0
Total income	20,000	22,500	10,000	12,215
Payments				
Staff costs	2,500	2,432	12,500	10,704
Materials	5,000	3,798	0	0
Marketing	2,000	2,405	500	380
Heat/light	0	0	2,000	0
Admin	750	960	500	620
Building	2,000	1,880	0	0
B Rates	350	352	350	352
Insurance	4,000	4,617	0	0
Interest	0	0	0	0
Accountant	0	0	0	0
Rent	1,750	1,772	1,750	1,772
Other exps	300	441	200	253
Capital	4,000	3,715	0	0
Total exps	22,650	22,372	17,800	14,081
Bank balance at end	(2,650)	(128)	(10,450)	(1,994)

In this example, the cash flow deficit has turned out to be much less serious than originally predicted, partly because of an unanticipated grant of £2500 and partly because staff costs and some other costs have been lower than expected. (Some items of expenditure may be payable later than anticipated: for example, the fact that there is no payment in February for heat and light suggests that this bill is now likely to fall for payment in March).

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Unfortunately, sometimes the projections turn out to be too optimistic, rather than too pessimistic!

Analysing income and expenditure against the forecast allows you, if necessary, to take remedial action. For example, if your cash flow looks less strong than you hoped, you can approach your bank in good time to arrange or extend an overdraft facility.

Here are some of the questions which you might be asking, once you have analysed your actual income and expenditure against your predictions:

- Did a lower sales volume than expected, lower prices or a different sales mix cause the shortfall?
- Is the market less buoyant than you expected or is your market share below target?
- Was a particular product responsible?
- Is a particular location under-performing? If turnover was higher than budgeted, analyse the reasons.
- Were your budget targets too low?
- Was the increase in sales a one-off or the start of a trend?
- Have sales been brought forward from future months? Will sales in those months now be lower than originally forecast?
- Did sales campaigns take longer to have an effect than anticipated?
- Were customers slower to pay than you expected? Analysing the differences will help you to improve your ability to set future budgets and allow action to be taken where needed.
- Do you need to change the assumptions on which you base your budgets (e.g. if the conversion rate for new enquiries has fallen)?

If, part way through a year, it is obvious that there are significant variations between projected and actual income and expenditure, it is worth going back to the projections, in order to revise them for the remainder of the year.

Annual budgeting

Producing a budget for income and expenditure, and from this working out a cash flow forecast, is not something which needs to be just in the business planning stage. At least once a year, the same process needs to be gone through again.

The advantage this time is that you have real figures from actual trading to work from. You will, however, need to be aware that some prices may rise, due to inflation. Staff costs may increase, not only through annual pay rises but also by progression by staff members up the points of a pay scale.

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Preparing budgets is a good opportunity to take stock more generally of the way you are running the business. For example:

- Are your credit control processes adequate, to ensure that your debtors pay you on time? Are you doing all you can to avoid bad debts?
- Can you negotiate longer periods of credit with your suppliers?
- Is your market stable, or can you expect your sales to fall (rise?) over the longer period?
- What are your profit margins/ratio of profits to total sales? Are these ratios satisfactory? Do you need to reassess your pricing policy?
- Can you reduce costs?
- Should you focus on your more profitable lines of business?

When producing budgets and forecasts, be aware of real world problems.

- Managers and employees are more likely to meet targets which they have agreed on collectively in advance
- Imposing a budget (for example, demanding across-the-board cuts of 10%) often fails
- Avoid setting over-ambitious and unrealistic budgets
- Equally, avoid the danger of setting 'comfortable' budgets, which managers and employees can easily meet
- Remember that budgets can build in assumptions, rather than questioning them. For example, if you automatically budget each year for a wastage rate in stock of 5%, is this really necessary? Can you improve the way the business is run, so that the wastage rate falls?



Social enterprises can use the budgeting and financial planning process to reinforce participation and involvement by staff and supporters. Instead of being a chore, it can be a key part of the year's cycle of activities.

Planning for expansion

Ironically enough, small businesses which have become successfully established often get into difficulties when they come to expand.

Normally, every business is happy to increase its sales. But rapid expansion, for example, by taking on major new orders, can also mean taking on large new financial commitments. In particular, extra staff may need to be taken on - and this involves an on-going commitment by

section 3: financial management of a social enterprise

the business to be able to generate the sales and profits to be able to keep these staff in post. As well as financial implications, there are also management implications to consider.

Major expansion may require further injections of capital in the business. As with the original business planning exercise, rapid growth should be undertaken only after careful planning first.



It's not a bad idea to restrict the growth of your business to whatever you can comfortably afford to finance. Always keep a financial reserve available for contingencies.

Using accountants

So far, we have assumed that social enterprises will be undertaking their own accounting and book-keeping.

Most small businesses choose to use an accountant to support them, however, particularly in relation to annual accounts. The service and expertise offered by accountants varies greatly and the fees charged vary accordingly. Shop around for the right level of advice at the right price level for your circumstances.

There are several firms of accountants that specialise in the 'not-for-profit' and charity sector.



Because an understanding of the financial position is central to the effective management of a business, don't be tempted to 'delegate' everything relating to your finances to your accountant to deal with.

section 4: annual accounts

Limited companies have a legal requirement to make their financial affairs available publicly, through the production of sets of annual accounts. There are two key documents:

- The Profit and Loss Account. This is a historical report on the income and expenditure of a company over a period of time, normally a year.
- The Balance Sheet. This summarises the assets and liabilities of a company at a particular moment (normally the last day of the financial year). It is sometimes described as a 'snapshot' of the company at that moment of time.

The profit and loss account

As its name suggests, this reveals how much profit, or loss, a company has made during a financial year. It shows what income has been earned (for example, from sales), and how this money has been spent.

At its very simplest, a profit and loss account looks like this:

Sales
less: direct cost of sales
less: labour costs
less: overheads
Profit

If we return to the example of the community childcare nursery, their first year profit and loss account might look, in simplified form, something like this:

Income		
Childcare fees		£200,505
Expenditure:		
Staff costs and NI	£145,441	
General admin costs	£7,509	
Premises rent	£22,134	
Other premises costs	£5,346	
Marketing costs	£4,432	
Insurance	£5,210	
Interest on loans	£3,100	
Toys, resources	£4,450	
Bank charges	£230	
Accountant	£500	
Rates	£3,456	
Other expenses	£2,203	
Depreciation on capital items	£1,245	
Total		£205,256
Net profit/(loss)		(£4,751)

section 4: annual accounts

In other words, the nursery ended up making a loss on its first year's trading - perhaps not too bad all things considered, though of course not the £1,000 profit forecast on its original budget (see above, page 11).

For VAT-registered businesses, the figures in a profit and loss account are exclusive of VAT.

Profit and loss accounts are concerned with sales and purchases made - not with the cash actually received or spent. It is possible, for example, that some of the £200,505 recorded as income in the table above was still outstanding at the year end (perhaps some parents were slow in paying their fees); similarly, there could well have been phone bills or electricity bills which were unpaid and the accountant's bill was probably settled many months later. Nevertheless because the profit and loss account is concerned with the income and expenditure for the actual trading period covered in the accounts, all these items have to be included.

The business loan of £20,000 which the nursery received when it began trading, together with the welcome £2,500 grant it obtained, do not show up on the profit and loss account (as we shall see, they appear on the balance sheet). The cost of interest payments on the loan are, however, shown.

Similarly, expenditure on items of capital equipment is not included - these are, after all, assets which are expected to last for several years and which therefore will have an effect on several years' trading profits. Instead, each year's profit and loss account shows a depreciation figure. As mentioned earlier, this is a notional element, designed to reflect the actual cost for the trading year in question of the capital items used.

The profit and loss account is designed to give an accurate statement of the trading undertaken by the company during the year in question. To an extent, however, there is an element of judgement involved. For example:

- How much of the income from a long term contract should be included in that year's profit?
- What adjustments to make for bad debts (customers who do not pay)?
- How quickly to depreciate fixed assets?

Balance sheet

The balance sheet reflects the assets and liabilities of a company at a given moment.

The assets include such things as:

- Property owned
- Capital assets (at depreciated values, not values at purchase)
- Investments
- Current amount in bank account
- Cash held
- Stocks
- Debtors (people who owe the business money)

The first three are usually described as fixed assets. Cash held in bank accounts or in petty cash, stocks and debtors are described as current assets.

The liabilities include such things as:

- Loans which need to be repaid long-term
- Loans which need to be repaid within the next year
- Bank overdrafts
- Creditors (people to whom the business owes money)

The latter three categories are described as current liabilities.

At the moment when a new business first starts trading, its assets and liabilities will directly balance. For example, when a bank loan is first received, before any trading takes place, the balance sheet would look simply like:

Assets	
Cash at bank	£20,000
Liabilities	
Bank loan	£20,000

Once the business begins trading, things inevitably become more complicated. Nevertheless, throughout the company's life, the balance sheet will stay in balance: the company assets will always be matched by its liabilities plus reserves which have been built up from retained trading profits and from equity supplied by shareholders.

section 4: annual accounts

The nursery's balance sheet on the last day of the first trading year might look, in simplified form, something like this:

Fixed assets		
Capital items	£5,246	
Current assets		
Stocks	£2,813	
Cash at bank and in hand	£9,579	
Debtors	£ 345	
Current liabilities		
Creditors	£ 234	
Total assets less current liabilities		£17,749
Bank loan	£20,000	
Net total assets		(£2,251)
Capital and reserves		
Retained profits		(£4,751)
Reserves - grant		£2,500

It is on the balance sheet that the £20,000 bank loan taken out by the business makes its appearance. So too does the annual profit (or, in this case, loss) as represented by the profit and loss account. (The brackets round a figure conventionally denotes a minus number).

This balance sheet shows a company whose liabilities are greater than its assets, by £2,251. This is one result of the nursery's reliance on loan capital, rather than equity: because of the nature of equity capital, it is not treated in accounting terms as a business liability. (This is why companies are encouraged to raise at least part of their capital requirements through equity rather than loan finance). If the nursery had been able to raise £10,000 in share capital from, perhaps, supporters in the local community, and had borrowed just £10,000 via a bank loan its balance sheet would have been transformed, as follows:

Fixed assets	
Capital items	£5,246
Current assets	
Stocks	£2,813
Cash at bank and in hand	£9,579
Debtors	£ 345
Current liabilities	
Creditors	£ 234
Total assets less current liabilities	£17,749
Bank loan	£10,000
Net total assets	£7,749
Capital and reserves	
Retained profits	(£4,751)
Reserves - grant	£2,500
Share capital paid up	£10,000

As it stands, however, the balance sheet currently shows a situation where the nursery is technically insolvent. This cannot be allowed to continue indefinitely. Nevertheless, the directors will be justified in continuing to trade if, in their professional judgement, their financial projections demonstrate that the business can move quite soon into profitable trading.

Social audits and accounting

Social enterprises, unlike conventional businesses, do not claim that their sole responsibility is to maximise profits for the benefit of their shareholders. Indeed, increasingly even ordinary companies are being persuaded that they should talk more of 'corporate social responsibility'. The idea is slowly spreading that businesses should consider their 'triple bottom line' - in other words, that as well as economic profitability, companies should also consider the social and the environmental costs and benefits of their operations.

Traditional annual accounts measure only economic performance. Social enterprises are in the vanguard in developing tools for measuring and reporting also on an organisation's social and ethical performance, through methods such as social accounting and Social Return on Investment (SROI). This is work which the New Economics Foundation (NEF) in particular is developing. NEF is currently adapting for the UK the concept of Social Return on Investment (SROI), as developed in the US. This idea is to measure those returns that are capable of being quantified in monetary terms - for example, the reduction in welfare spend or the increase in taxes raised, brought about through increasing employment.

section 4: annual accounts

Two examples of social enterprises that have already developed social accounts are Traidcraft and Furniture Resource Centre.

- **Traidcraft** is the UK's largest fair-trade organisation. It has been publishing independently audited social accounts since 1993, based on the auditing standards produced by The Institute for Social and Ethical Accountability. It measures its social impact against benchmarks agreed with stakeholders. The three core performance indicators which Traidcraft uses to assess the success of its strategy are its direct impact on poverty, its influence on others to trade, work and legislate to the advantage of the poor, and its sustainability.
- The **Furniture Resource Centre (FRC)** Group is a Liverpool-based social enterprise that provides low-income households with furniture and that recycles bulky household waste, whilst employing and training long-term unemployed people. In March 2003, the FRC was awarded the ACCA/AccountAbility award for Best Social Report, over private sector organisations including GlaxoSmithKline and BP. It published its fifth set of social accounts in September 2003. Through these social and environmental audits, the FRC tries to measure not only its social impact but also to assess its influence on policy makers and the environment.



Formal social auditing and accounting is important in demonstrating to the community, the private sector and the public sector that social enterprises, even if they create little economic value, may have significant social returns from their operations. This in turn helps funders appreciate the value created by their grants or investments.

Alternative Public Offerings (APOs) Share issues that allow people to invest in a social enterprise that is off-market. Also known as 'ethical public offerings', 'alternative share issues'.

Asset Something a business owns or is due to receive. 'Fixed assets' include machinery and vehicles; 'Current assets' include cash and debtors.

Balance Sheet A financial statement that indicates what a business owns and owes at a particular point in time, typically at the end of a financial year.

Budget A financial plan that estimates the operating costs and receipts over a certain period of time.

Business Angels Private venture capitalists, who provide money and experience to early stage investments.

Business Plan A document that describes in detail the objectives of a new or established business and the necessary steps to achieve them. It should include information on the target market, a financial plan, the required money and resources, marketing strategies and the business model.

Capital The money or wealth owned or used by a business or organisation.

Cashflow The movement of funds into and out of a business.

Community Development Finance Institutions (CDFIs) Organisations that make loans to businesses or enterprises who work towards community development.

Debt An amount owed.

Factoring A service offered by organisations whereby they will pay a company in advance for its outstanding invoices, in return for a percentage fee of the invoice value.

Finance Money that has to be returned, usually with interest, back to its owner.

Grant Funding that requires an organisation to meet certain criteria.

Micro-Finance Schemes Schemes aimed at businesses that require relatively small amounts or money for a relatively short amount of time.

Overheads A company's on-going costs, for example rent, power, research and development fees and insurance. Distinct from 'direct costs', which are those incurred in delivering a service (e.g. wages) and selling a product (e.g. the cost of stock).

Patient Capital A form of investment intended to achieve social benefits while also generating a financial return but which is neither a straightforward grant nor commercial loan.

Service-Level Agreements An agreement, typically between a local authority and a tendering body, which sets out the conditions and levels of service to be met by the tendering body in fulfilling a contract.

Small Firms Loan Guarantee Scheme Offered by the government as an incentive to small business start-ups, the loan guarantee fund will offer security on 75% of any loan up to £100,000 (for start-ups) made by a bank. On top of the normal interest on the loan, there is an extra 2% p.a. levy payable to the guarantee scheme.

appendix 1: glossary

Small and Medium Enterprises (SMEs) Usually defined as businesses with fewer than 250 employees and/or turnover of less than £25m.

Social Enterprise An organisation that is equally committed to generating economic, social and environmental profit - known as 'multiple bottom lines' - and is geared towards creating meaningful and lasting change within the community.

appendix 2: further help and useful organisations

Possible sources of loan, equity and grant finance

Access Funds

www.access-funds.co.uk

On-line database of grants for voluntary organisations and charities

Awards for All

www.awardsforall.org.uk

Awards for All is a lottery grants programme aimed at local communities, and grants of up to £5,000 are awarded in a simple straightforward way.

Baxi Partnership

www.baxipartnership.co.uk

A £20m fund which helps finance the conversion of existing companies into employee-owned businesses.

Big Lottery Fund

www.biglottery.org.uk

Launched in June 2004, the Big Lottery Fund brings together grant funding programmes from the national lottery previously dealt with by the Community Fund and New Opportunities Fund.

Bridge House Trust

www.bridgehousegrants.org.uk

Distributes £16m+ in charitable grants each year to charitable projects in the Greater London area.

Bridges Community Ventures Ltd

www.bridgesventures.com

Responsible for the management of a £40 million venture capital fund, Bridges Community Ventures Ltd invests in entrepreneurial small and medium-sized enterprises in the most deprived 25% of England (using the Index of Multiple Deprivation). Applicants to the fund must have a direct and beneficial impact on a deprived area in one or more of the following ways: at least 35% of current or future employees must live in a deprived area; the core market for the

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business must be situated in a deprived area; and/or 50% of non-salary expenditure must go to local businesses in a deprived area.

The Capital Fund

www.thecapitalfund.co.uk

A new venture capital fund which has raised £50m to back fast-growing small and medium sized enterprises in Greater London.

Charity Bank

www.charitybank.org

Charity Bank is the UK's first not-for-profit bank that lends to charitable organisations and social enterprises. It offers loans or guarantees from £3,000 up to £250,000 in the form of:

- Short-term bridging loans against delayed grants or other identified income
- Working capital loans.
- Construction and development loans.
- Mortgage loans with terms currently up to 20 years.
- Standby commitments where you need to evidence matched funding.
- Underwriting to kick-start or reinforce a fund-raising programme.
- Loans for capital equipment or other asset purchase
- Guarantees or performance bonds

Children's Local Network Fund

www.cypu.gov.uk/corporate/Inf/

This fund is designed to help voluntary and community groups provide local solutions to poverty and social exclusion affecting children up to nine years of age.

Comic Relief

www.comicrelief.com

Distributes money raised through the regular Red Nose Days, through grants.

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Community Development Finance Association

www.cdfa.org.uk

This is the trade association for Community Development Finance Institutions. They will be able to help find a CDFI near to you.

Co-operative Action

www.co-operativeaction.co.uk

Co-operative Action is a grant and a loan-making body aimed at enterprises and organisations that promote co-operative solutions. Grants are for:

- Developing and supporting new or existing co-operative enterprises.
- Promoting co-operative solutions and structures of all kinds and in all sections of the economy.
- Research into co-operative structures and solutions.
- Research into new forms of finance for co-operative enterprises.

Co-operative Bank

www.co-operativebank.co.uk

Provides normal banking services for customers but also has great experience working with co-operatives, social enterprises and small organisations. It provides a range of services and among the partners it works with is the Federation of Small Businesses.

Esmee Fairbairn Loans Programme

www.esmeefairbairn.co.uk

A three-year pilot programme, that provides loans of £10,000 to £250,000 for charitable purposes. Its guidelines are available on-line. Applications are accepted anytime.

Foursome

www.foursome.net

Foursome is a venture capital firm that invests in British, European and North American socially responsible businesses. Each project is evaluated against a number of financial criteria, including return on investment, a well-developed and achievable business plan, and a realistic exit strategy. To achieve this aim, Foursome makes equity investments of up to \$1 million in projects relating to the environment, education, technology and culture.

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Funding Information

www.fundinginformation.org

Online database of funding for voluntary organisations and social enterprises

Greater London Enterprise (GLE)

www.gle.co.uk

GLE has a number of funds available to SMEs, although there is no specific policy on social enterprises. Applications are accepted from various groups, including entrepreneurs from black and ethnic minority groups, people over 45, refugees, disabled people, lone parents, residents of housing estates and established businesses that will create jobs for the socially excluded.

London Seed Capital is a £4.8m early stage venture capital fund launched in late 2002, which co-invests between £50,000-£100,000 alongside Business Angels. GLE has also set up Independent Growth Finance, a factoring and sales ledger management company.

Hackney Business Venture

www.hbv.org.uk

Hackney Business Venture manages several loan funds that are aimed at developing social enterprise in Hackney, Waltham Forest and Finsbury Park. These funds have their own particular terms and conditions, but each requires a completed business plan. Typically, these funds can provide finance of between £3,000-£25,000.

Impetus Trust

www.impetus.org.uk

Uses the experience and techniques of the venture capital industry in making grants to charitable organisations - what is known as 'venture philanthropy'.

Industrial Common Ownership Finance

www.icof.co.uk

ICOF (Industrial Common Ownership Finance) has specialised in lending to co-operatives, employee-owned businesses and social enterprises for thirty years. (It was one of the founders of the Community Development Finance Association, and is an active member). It has raised its own capital from various sources, including public share issues.

ICOF offers business loans with terms up to 10 years. Ranging from £5,000 to £50,000, these loans are available as bridging loans against delayed grants, loans on property and working capital and loans to replace inappropriate existing finance. These are only offered to

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enterprises in the UK that practice or support:

- The principles of co-operation
- Common Ownership
- Employee/community or social ownership
- Equal Opportunities and workplace democracy

j4b

www.j4b.co.uk

Website which aims to provide a comprehensive database of business grants and loans

Local authority Regeneration Units

If you are applying for regeneration funding talk to your local regeneration unit who can refer you to wide range of regeneration partnerships including Local Strategic Partnerships (LSPs) who are responsible for the Neighbourhood Renewal Fund.

Local Investment Fund

www.lif.org.uk

Set up in 1995, Local Investment Fund offers loan finance for not-for-profit organisations, including community ventures and social enterprises. Loans are from £25,000 to £250,000. Applicants must have previously been unable to acquire sufficient funding from traditional sources (or require top-ups). They must have a viable business plan that shows a desire to reduce grant dependency and be able to demonstrate how their community enterprise will contribute to social inclusion.

There are also regional funds, offering loans of between £15,000-£100,000.

London Development Agency

www.lda.gov.uk

The government's 'regional development agency' for the London area.

London Rebuilding Society

www.londonrebuilding.com

The London Rebuilding Society provides financial support and advice to voluntary

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organisations, charities and community groups across London.

Its Social Enterprise Fund provides loans of between £5,000 and £50,000 for a range of uses - start-up capital for new enterprises, bridging loans, or resources to purchase equipment or refurbish run-down property. In some circumstances smaller or larger sums may be available.

London Rebuilding Society also manages the Mutual Aid Fund. This operates in a similar way to a credit union, offering a mechanism for social enterprises to save and then borrow small sums.

National Council for Voluntary Organisations

www.ncvo-vol.org.uk

Information and advice for voluntary sector organisations

North Hammersmith Social Enterprise Fund

www.lbhf.gov.uk/Our_Borough/regeneration/Regenfinal/Regeneration_Team/Social_Enterprise_Fund/social_enterprise_fund.htm

This loan fund is available to anyone with an idea for a social enterprise in North Hammersmith. To qualify for loans of between £500 and £30,000, projects must show how they will achieve at least four of the following goals:

- Create jobs
- Engage residents and communities
- Help get local people into work
- Establish a locally based enterprise
- Have community representatives at board/strategy level
- Improve the quality of life of local residents

Prince's Trust

www.princes-trust.org.uk

Offers low interest loans (typically between £2000-£3000) for young people aged 18-30 who are starting in business. Grants are also sometimes awarded. Business support and advice service.

SENSE (Social Enterprise Network for Social Entrepreneurs)

www.croydon.gov.uk

www.suttoncvs.org.uk/socialenterprise.htm

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SENSE is a London Development Agency Pilot working in the areas of Croydon and Sutton. The Croydon and Sutton Community Bond for Social Entrepreneurs is an interest-free loan, aimed at supporting social enterprises. There is an ongoing application process, with decisions being made approximately on a bi-monthly basis. More information from 020 8760 5692, ext. 1983

Social Enterprise Coalition

www.socialenterprise.org.uk

Includes information on accessing finance. SEC publishes a booklet *Unlocking the Potential*, on finance for social enterprises.

Triodos Bank

www.triodos.co.uk

Triodos offers a comprehensive range of banking services for social businesses, charities and groups along with a variety of savings accounts for individuals. Triodos Bank only lends money to organisations that pursue positive social, environmental and cultural goals.

Triodos, which is part of a Dutch bank with roots originally in the Rudolf Steiner movement, has recently set up The Community Investor Account, which raised over £3 million for distribution via the Community Development Finance Initiative. Loans of up to £250,000 are available from this Department of Trade and Industry-accredited fund.

UnLtd

www.unltd.org.uk

UnLtd is a consortium of charities, including Community Action Network (www.can-online.org.uk) and the School for Social Entrepreneurs (www.sse.org.uk). From December 2002, UnLtd have offered grants from an endowment fund to would-be social entrepreneurs. Two forms of grant are available: Level 1 grants of between £500 and £5,000 for start-up organisations involved in community benefit, and Level 2 grants of between £5,000 and £15,000 for developing existing projects.

Unity Trust Bank

www.unity.uk.com

The Unity Trust Bank provides low-cost banking services and support to trade unions and not-for-profit organisations through locally based development managers. This includes offering various types of bank accounts (Unity does not provide start-up loans).

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Urban Partnership Group

www.urbanpartnership.co.uk

The Urban Partnership Group has secured new funding for the development of social enterprise activities in the West London Community Economic Development zone, comprising Old Oak, White City, Edward Woods in Hammersmith and Stonebridge in Brent.

Venturesome Fund

www.cafonline.org/venturesome/

Venturesome is a risk capital vehicle for charities established and funded by the Charities Aid Foundation (CAF). The basic idea is to employ 'mezzanine' financing mechanisms, commonly available in the commercial sector, in the voluntary and community sector.

Venturesome has made two equity investments in social enterprises with a specific charitable purpose, but it does not regard social enterprises as a sector likely to supplant charities as its main market.

Other organisations

As well as the organisations mentioned in the previous section, there are a number of places to turn for support and advice.

Association of London Government

www.alg.gov.uk

London-wide association linking the individual London Boroughs.

Business Link for London

www.bl4london.com

Advice and information for small business. Telephone helpline is **0845 6000 787**

Community Action Network (CAN)

www.can-online.org.uk

A UK-wide membership organisation consisting of individual social entrepreneurs involved in a wide range of activities. Joining up gives you access to an 'extranet' that has information, notice boards and discussion groups. CAN also develop new initiatives in partnership with members involved in health, education and so on.

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Community Accounting Plus

www.communityaccounting.co.uk

This is a membership association, with charitable status, supporting the development of community accounting in the UK. Offers courses, one-to-one advice and direct services such as bookkeeping and payroll.

Co-operative Support Organisations (CSOs)

These provide business support including during the start-up phase. Click on the CSO map on the **www.co-operativeaction.co.uk/CSOmappage.html** website for details of your nearest CSO.

In London, there are a number of specialist co-operative development agencies:

- Greenwich: **www.gcda.org.uk/**
- Hackney: **www.hced.co.uk/**
- Tower Hamlets: **www.co-operation.coop/**

Co-operatives UK

www.cooperatives-uk.coop

National organisation linking retail co-operative societies and workers' co-operatives. Offers advisory service on legal structures and incorporation for co-ops.

Councils for Voluntary Service (CVS)

Local CVSs provide support to local voluntary and community groups.

To find your local branch contact the National Association of Councils for Voluntary Service (**www.nacvs.org.uk**).

Development Trusts Association

www.dta.org.uk

A membership organisation of community-based regeneration organisations. The DTA organises events, conducts research, produces publications, gives development support and publishes a quarterly newsletter.

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Directory of Social Change

www.dsc.org.uk

The Directory of Social Change is an independent source of information for voluntary organisations and groups. It also provides training, courses, conferences and produces publications, including a range of 'starter guides' for those new to the voluntary sector. They have a library based in London.

Migrant Organisations' Development Agency (MODA)

www.moda.org.uk

MODA is a support and co-ordination agency for migrant organisations in London.

Mutuo

www.mutuo.co.uk

Campaigning and research organisation for the mutual sector.

New Economics Foundation

www.neweconomics.org

NEF challenges orthodox thinking of economic, social and environmental issues.

Peabody Trust

www.peabody.org.uk

Housing association and community generation organisation

Regen.net

www.regen.net

Website for the magazine Regeneration and Renewal. Provides information on regeneration partnerships, publications and events, including a discussion forum.



social enterprise london



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