



Credit Union Base TRAINING AND SUPPORT

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Credit Unions: plan for success...

Balancing costs with income, whilst meeting FSA solvency requirements will always be a challenge for CU management. Managing change adds to this challenge.

The Credit Union Financial Model

This FREE spreadsheet tool helps CU management to plan for success.

Guide to using the Financial Model

This document is an instruction manual designed to help you use the tool within your CU.

Hornbeam Accountancy Services Ltd who wrote this model offer two important support services.

1. Training on use of the model

A training session is likely to take a full day – the cost is £800 plus agreed expenses and VAT, but can be for up to 5 delegates in your premises or premises you organise.

Existing clients are entitled to a 20% discount.

For further information about courses, see contact details below.

2. Telephone Support

We provide prepaid telephone support during normal office hours at £300 plus VAT for a support contract that expires when 8 hours of support have been provided or 12 months have passed.

Discounts available are 20% to existing clients, the first contract is free to anyone taking up the training session.

To book a training session or support contract, telephone Eileen on 01603 720424 or email eileen@hornbeam-accountancy.co.uk





Saving

When you first receive the excel workbook (by email or disk) we suggest that you

1. open a new directory with a name such as “financial model backups”.
2. save the workbook as received under a name such a “model as received”.
3. Immediately resave as “model play 1”.

You can always go back to the “model as received”, but try to get in the habit of saving different projects or different projections separately and regularly.

Overview

This model has been designed to be extremely flexible, but to get the best out of it, it is important to understand how it works.

There are three worksheets

- The first sheet we have called *DATA INPUT*. The yellow cells are the ones in which you input the data about your credit union. You can change this data as often as you like.
- The second sheet we have called the *FINANCIAL MODEL*. This sheet relies entirely on embedded formulas to convert the information on the *DATA INPUT* sheet into business projections which can be printed off or just used as a management tool – see below.

Warning: If you type directly onto the Financial Model you will break the program – this will not matter so much if you have saved a copy with the intention of doing this deliberately, for whatever reason.

- The third sheet has a number of *BACKGROUND CALCULATIONS* used by the model on it. There should be no reason for users ever to access this worksheet.

So to summarise you put the data onto the *DATA INPUT* and the projections appear on the *FINANCIAL MODEL*.

The model comes pre-loaded with some arbitrary data for an imaginary credit union, most users will be keen to overwrite the model with their own data, but an alternative strategy might be to see how the original model changes as you change the inputs provided.

The *FINANCIAL MODEL* follows best practice in having three primary statements

- 1. The Profit and Loss Account** (also known as the Income and Expenditure Account) which measures the Surplus or Loss on the activities of the credit union over the period.



2. **The Cash Flow** which tracks the cash movements and thus measures the cash balance and the cash availability throughout the period.
3. **The Balance Sheets** which record the net wealth of the credit union at the end of each period. The Balance sheets are also important because (i) they demonstrate that the model is consistent and robust and (ii) they allow us to monitor solvency ahead of the FSA.

How to have both sheets (*DATA INPUT* and *FINANCIAL MODEL*) open at the same time

1. Go to *View*, click *New Window* in the ribbon (at the top of the screen).
2. Now you have two copies of the same file open.
3. To view both at the same time; Go to *View*, click *Arrange All* and choose *Vertical*.
4. What you do on one sheet will affect the other, in real time.
5. Click on the worksheet tabs to ensure that you have *DATA INPUT* open on one pane and *FINANCIAL MODEL* open on the other – as you change *DATA INPUT* you can see the Financial Model change.
6. **Double screen. If you have a double screen set up** the first three things above all happen on one screen. You can drag the side of the overall excel document so that it covers two screens then do the same again for the individual panes so that they cover a screen each.

Ways to use the model

All Financial Models have a number of uses.

1. **Projections.** By entering the current balance sheet data, and current operational data this financial model will project forward, giving the user; the Income and Expenditure, the Cash Flow and the Balance Sheets; up to 5 years into the future. Whilst this is itself quite a useful management tool...
2. **Modelling.** It is the ability to change parameters, and instantly see the impact upon the performance of the credit union that makes the financial model really useful. By saving and printing series of data such as increased lending, reduced bad debts or whatever, the impact of each factor can clearly be understood. This is hugely helpful with establishing strategy as well as setting more specific targets.

One variation on the above is to save a new model and clear all the data, then start from scratch and see immediately how different factors affect the performance of a theoretical CU

3. **Budgeting.** The financial model can thus form the basis of a system of budgets enabling performance to be measured against budget, perhaps leading to “flexing” of the budget which can be remodelled.



4. **Solvency.** Finally this model has a number of FSA solvency measures built into it and generates red ALERTS when solvency tests are breached.

Detailed instructions how to use the Financial Model

I am assuming you have the *DATA INPUT* sheet open (preferably with the *FINANCIAL MODEL* also visible on screen (see above) and that you have saved under some suitable name (as well as model as received).

Headings

If you click on cell F2 – this is a yellow highlight box so you can alter it – It says “Model Credit Union” – overtype the name of your credit union.

If you click on cell F3 - this is a yellow highlight box so you can alter it – It says “01 January 2013” – Overtyping it with the first day of your projections, usually this will be the day after the balance sheet that you are about to input for the opening balances. So if your balance sheet is 30 September 2013, your projections start from 1 October 2013 and that is the date to input.

The name and the dates on the *FINANCIAL MODEL* should now be those of your model.

Fixed Assets

We now have to input the opening balance sheet, anchoring the projection firmly in reality, unless of course this is a new venture. So equip yourself with a set of accounts and input the data...

Click on H9 and input the net asset value of the fixed assets per the accounts.

Rows 13 and 18 allow you to input any expected fixed asset purchases at cost (net of any grants) or sales at written down value. The model is designed to calculate depreciation at 25% reducing balance. We don't recommend you to change this but if you want to you must change the formulas in rows 14 and 19. Rows 15 and 20 track the changing level of the fixed assets and agree with row 164 of the *FINANCIAL MODEL*.

Members Loans

The first thing is to get the **opening balances**, if you input a figure into row 71 (presumably taken from the balance sheet) this will overwrite the opening figure.

As an alternative, if you clear row 71 then the *BACKGROUND CALCULATION* takes the data from rows 32 to 34 and row 50 to calculate an expected balance. This can work out a net balance quite accurately, but the older balances on your books (which are fully provided under FSA rules) are not modelled.



Generally speaking you will want to input the actual figures at row 71 before proceeding, but playing with the figures at this stage

- Helps you see and understand how the model works (and how the business works).
- Helps confirm the relationship between your average loan size, number of loans issues and bad debt provision on one side and the loan portfolio and income on the other – and thus how the portfolio is composed.

You will see that this section is set up for **3 loan types**, you have the option of only using one loan type, but many credit unions will want to distinguish between their smaller, higher interest, higher risk loans and the rather larger lower interest, lower risk loans.

It is a quirk of the Model that having worked out how the credit union got to its current state of being this is quite unlikely to be the same as the figures projected for the next year, so that in particular row 36 (line 4, Number of Loans per month) and perhaps row 50 (line 14, Annual Percentage Write-off of Bad Debts) will have to be amended again for **the first year** of the projection.

Rows 38 to 41 (lines 5 to 8) enable you to increase or decrease the amount of **loans issued in years 2 to 4**. In each case the percentage refers back to the value in year 1 (not the value in the preceding years).

If you want to use a geometric progression (such as a 20% increase each year) you will have to do this on the data input sheet. This is quite easy on a spreadsheet; F38 input 120%; F39 input as “= F39*120%”; then repeat this formula down.

The **costs of issuing loans and collecting debts** are the fundamental cost of operating a credit union. Small volunteer credit unions will have no staff costs but larger credit unions may have substantial costs. We think that the cost of issuing a loan should be recorded as about

$$= \text{Time taken} \times \text{staff pay rate} \times 2 \text{ (to allow for idle time, holidays, NI etc)}$$

Put your best estimates of the costs in at rows 44 and 45.

These costs show up on rows 21 to 27 of the financial model.

We come back to looking at total labour costs and efficiency below.

The proportion of loans in arrears (row 47, line 11) is a major driver for the cost of credit control. The percentage you input will be multiplied by the number of loans that there would be if everyone was up to date. Obviously your figure for loans in arrears at any one time will be based on a higher figure because of the backlog. We take the view that much of the backlog will be fairly dormant so the model will work reasonably accurately. The number of loans in arrears is then multiplied by the controller’s time chasing a loan in arrears each month (row 48, line 12) and the associated overhead cost per loan (telephone, postage, space costs tend to be quite high for credit controllers) (row 49, line 13).



These costs show up on rows 32 to 38 of the financial model.

The annual percentage write-off of bad debts is a pretty crucial figure for any credit union. This can be expressed in a number of ways, but this model works on the

P & L cost of write-offs / Net Balance Sheet value of loans
(expressed as a percentage)

Thus if at the end of last year you had £300,000 of loans before provision but decided to provide £30,000 against those loans the percentage would be 10%. Actual credit union provisioning rates vary widely, but if they exceed 26.4% they are exceeding income and generally only a level below 5% might be considered sustainable.

This model does not recognise bad debt provision in the Balance Sheets but treats the provision as a cost in the P & L and in the cash flow, whereas in practice it is a loss of cash receipts rather than an additional outflow.

If you think the annual write-off of debts will reduce or increase in years 2 to 5 this can be modelled on rows 51 to 54 (lines 14a to 14d), but a provision rate must be entered, an empty cell means no provision.

If you plan to reduce the cost of issuing loans or collecting debts compared to year 1 over the next 4 years these improvements can be input in rows 57 to 66 (lines 15 to 22). For example if you think that your costs of issuing a loan type 1 are £40 labour and £40 overhead now, but you expect to reduce this to £30 labour and £30 overhead in year 2 this is a 25% improvement and should be input in box F57 as 25%.

In the event that you expect your costs to move up from £30 labour and £30 overhead per loan in year 1 to £40 labour and £40 overhead in year 2 this is a 33% increase and should be input in box F57 as -33% (a negative improvement).

All changes in years 2 to 5 relate to the position in year 1 not the position in the previous year.

Managed Accounts

The model has provision to record income and expenses from a variety of managed accounts, which is pretty much self-explanatory.

Grant Income

Basically the model allows you to record any grants received but not yet released to P & L in box I88. You will normally get this figure off the most recent balance sheet.

Each month some grant will be released from balance sheet to P & L, in accordance with the terms of the grant. This is not so much modelled as manually input in rows 91 and 96.



Hopefully some new grants will be won and paid into the bank account again this is manually recorded on rows 92 and 97 of the data input sheet. The system shows you the balance left in the creditors in rows 93 and 98 – this acts as a bit of a check, the figure should not go negative.

These figures are now scattered to the Financial Model

1. From rows 88, 93, and 98 to row 175 “Revenue Grants in Advance” in the Balance Sheet.
2. From rows 91 and 96 to row 11 “Revenue Grants” in the Profit and Loss Projections.
3. From rows 92 and 97 to row 94 “Revenue Grants” in the Cash Flow Projections.

Some grant funding may be to cover operating activities such as issuing loans or operating managed accounts, these costs are already modelled above, and should not be re-input. However some grants might be for other activities, for example providing money management education to target groups. The cost of delivering these services should be entered in boxes F101 to F103.

Other income

Credit unions may have other sources of income, many will charge a membership fee for example. This is manually input on rows 107 to 110.

Interest on Bank Loans and Investments

Many credit unions will earn a little interest on the money they have that is not lent to members. Row 114 allows you to input an expected average rate of interest on this money. As this income is taxable you need to enter the rate net of tax deducted.

Other Costs Labour

Here you input the predicted total labour cost of the business for each period. Don't forget to include Employers NI.

The system will deduct the amounts you have included (it has calculated) for issuing loans, credit control, and other services. On row 65 it posts the figure for “Other Labour”. Obviously this is quite a powerful tool for assessing the efficiency of the credit union workforce. It may also be seen as a commentary on the actual costs of issuing and collecting debts. A specially saved model might be used to calculate back the “real” cost of the labour intensive functions.

Other Overheads

Almost inevitably there will be “Other Overheads”. We calculate this figure by taking the “Total Overheads” per your accounts and deducting the figures for functions which have been shown individually.



You may prefer to arrive at the Other Overheads by adding up individual cost. In which case you should overwrite rows 155 and 158. You will have to overwrite boxes J158 to M158 which are not automated.

As with labour costs the model then deducts the other overhead costs that have been allocated to other functions to come up with an amount for unallocated overheads. This is shown as Other Overhead Costs on row 66 of the Profit and Loss Account.

Members Funds

Members Savings are modelled in a similar way to Fixed Assets, Grant Aid, and Other Income, with you inputting any predicted changes manually onto the *DATA INPUT* sheet.

The all important payment to savers, the dividend, is calculated by the system based on the dividend rates that you input at rows 172 to 177.

Bank Account

Obviously a major function of the model is to predict and monitor the level of the bank balance, however before it can do this you must enter the opening balance taken from the latest accounts at cell I181.

Other Assets and Liabilities

Most credit unions will have balance sheet items other than the ones already modelled. To get the model to reconcile to reality the final piece of the jigsaw can be entered in this section.

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