

**Managing in Tough Times** is a guide covering key issues that may affect Third Sector organisations during periods of financial insecurity.

It offers a framework for identifying and assessing current risks and offers guidance on how an organisation can manage and adjust to change. Should the difficult decision be made to close the organisation, it offers guidance on the steps that are required depending on the legal structure of the organisation.

# Managing in Tough Times

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capacity  
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Social Enterprise Works 

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# Managing in Tough Times

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# Contents

## Chapter 1 Managing Risk

1. Why manage risk? ..... 3
2. Identifying and assessing risk ..... 5
3. Addressing risk ..... 8


## Chapter 2 Adjusting to change


1. Managing pressures on staffing ..... 10
2. Preparing for redundancy ..... 13
3. Collaboration and mergers ..... 15
4. Managing finances ..... 19

## Chapter 3 Preparing for the worst

1. Warning signs ..... 24
2. Worst case ..... 25
3. Keeping in control ..... 28

## Appendix 1 Further Information

Symbols used  = Tips and helpful hints

 = Documents and resources  
(these are hyperlinks on the pdf version)

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# Managing Risk

## What would the ideal organisational environment look like?

### It would have:

- Strategic plans in place
- Funding in place for all organisational costs
- A stable, fully funded staff team
- A committed and informed management committee

### However .....

Given the level of changes in funding programmes, it is more likely that:

- Funding is uncertain
- Staff posts are vulnerable – delivering on short term programmes
- Strategic and business plans are often out of date
- And it may be difficult to get committed members on management committees

In this environment, there are a lot of risks to be balanced and so there is a real danger that **unwanted “stuff” happens!**

## 1. Why manage risk

It is important to manage risk even in secure times as any organisation needs to ensure that it protects its reputation and that its operational delivery is meeting its objectives. However, when times become tougher and there is a lower level of stability, the danger of key risks being unmanaged becomes more extreme and could make the difference between effectively steering through choppy waters and sinking with all hands.

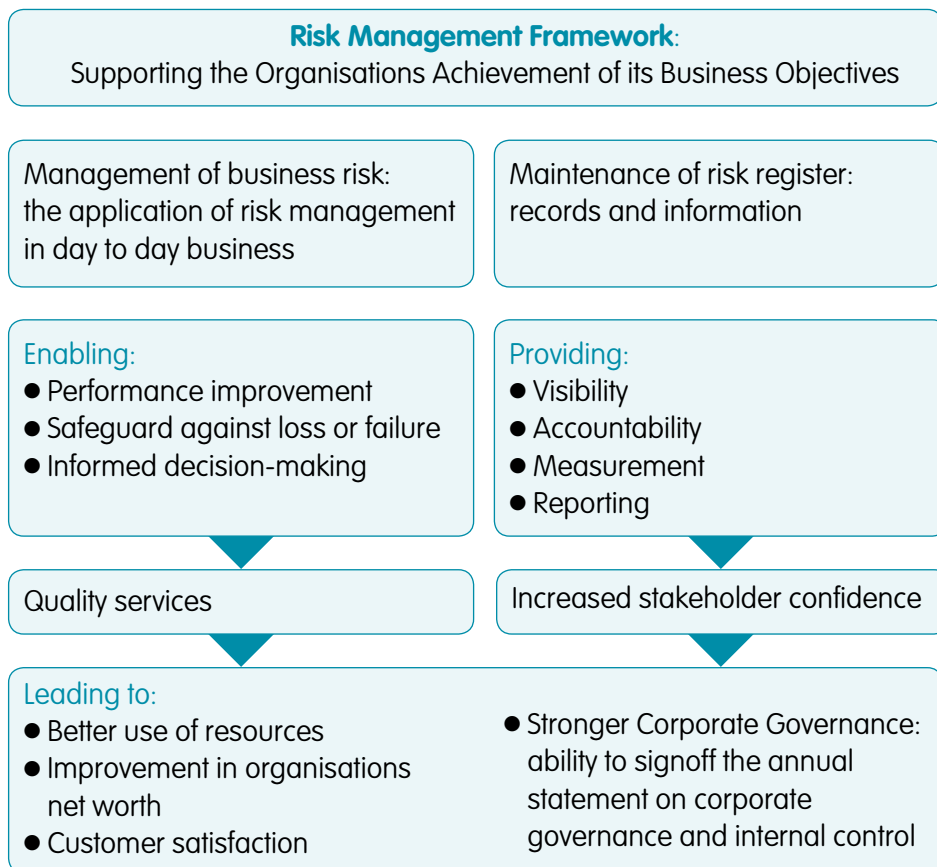
If you are a larger charity (income over £500K) or larger than a small company (turnover over £5.6 million!) it is a requirement of accounting regulations that you report on your risk management framework.



**Charity Commission – Charities and Risk Management**

**What are the benefits of managing risk?**

Here is a model from the commercial world – but that can be easily used by Third Sector organisations.



RSM Bentley Jennison – Business Risk Management, Benefits Model

**2. Identifying and assessing risk**

Prioritising and controlling the range of risks that an organisation generates is a two stage process – starting with identifying and assessing the risks and then putting in place a management system to address risk.

**How to identify risks – what should you be covering and in what detail?**

Each organisation is different – but you will need to cover:

- **Strategic risks** - risks to your service through changes in policy or political environment
- **Commercial risks** – your organisation may be undercut by another supplier
- **Operational risks** – impact of loss of reputation if service delivery is flawed, failure to achieve targets/outcomes, reliance on volunteers, thinking about the potential impact of global warming and environmental change on your services and products
- **Technical risks** – failure of database, equipment breakdown
- **Financial & systems risks** – lack of reserves, poor financial control, costs spiralling out of control, no systematic activity and outcome reporting to management committee
- **Compliance risks** – meeting health and safety requirements, meeting charity accounting reporting requirements, inadequate reporting to Companies House, inadequate insurance.

The question of what level of detail to go into is a subjective one – covering all the potential risks you may come across could turn into a massive paper exercise and be very time expensive. It is a matter of judgement to ensure that you are identifying those risks that are material to your organisation now or have the likelihood of becoming more crucial.

Remember to think about risks being both internally and externally driven – for example an external commercial risk could be through changes in customer demand while an internal risk could be the resources you might need to respond to developing or adapting new services.


When it comes to the second stage, the risk register, there will always be movement in the priority of individual risks over time.

Using the above areas – you can create a risk map, scoring the risks as high, medium or low.

**There are two stages:**

- Listing potential risks in all the areas above (and ensuring that any particular risks your organisation may face are covered in these areas.)
- Scoring them - at this stage, just on the basis of high, medium and low in terms of their impact on your organisation and on the likelihood of it happening.

**Who should be involved?** – both Board and staff team should be involved in this process, even if there is only time for the headlines to be discussed and there is delegation to staff and/or Board in a sub-group to work up the detail and to work up the risk register. Behind this is the need to ensure that this is embedded in the reporting and decision –making processes of the organisation.

 Try to wordstorm the risks under each category and then simplify as far as possible so you reduce multiple symptoms down to the key issues.

NCVO have an excellent Risk Map in Tools for Tomorrow. It is set out below:

		IMPACT		
		High	Medium	low
LIKELIHOOD	High			
	Medium			
	Low			

Here’s a framework that should help you with this – you can set the level of financial risk that is appropriate to your organisation

**Eg: Level of impact of a financial threat**

<b>High</b>	<ul style="list-style-type: none"> <li>• Financial impact on the organisation is likely to exceed £x</li> <li>• Significant impact on the organisation’s strategy or operational activities</li> <li>• Significant stakeholder concern</li> </ul>
<b>Medium</b>	<ul style="list-style-type: none"> <li>• Financial impact on the organisation likely to be between £x and £y</li> <li>• Moderate impact on the organisation’s strategy or operational activities</li> <li>• Moderate stakeholder concern</li> </ul>
<b>Low</b>	<ul style="list-style-type: none"> <li>• Financial impact on the organisation likely to be less than £y</li> <li>• Low impact on the organisation’s strategy or operational activities</li> <li>• Low stakeholder concern</li> </ul>

Thinking about levels of risk – whether they are high, medium or low in relation to both impact and likelihood

**Eg: Likelihood of occurrence in a given period (say 2 years).**

Estimation	Description	Indicators
<b>High</b>	Likely to occur each quarter, or more than 25% chance of occurrence.	Potential of it occurring several times within the time period. Has occurred recently.
<b>Medium</b>	Likely to occur in a two year time period or less than 25% chance of occurrence.	Could occur more than once within the time period. Could be difficult to control due to some external influences. Is there a history of occurrence?
<b>Low</b>	Not likely to occur in a two year time period or less than 10% chance of occurrence.	Has not occurred. Unlikely to occur.

### 3. Addressing risk: the management of risk by creating a risk register.

For each of the high and medium level risks identified, your risk management system will help you consider any additional action that needs to be taken to mitigate the risk, either by lessening the likelihood of the event occurring, or lessening its impact if it does.

We tend to think about only internal controls as ways of managing risk, but there are some other responses that can be explored, for example:

- the risk could be transferred to a third party (eg a trading subsidiary, outsourcing or other contractual arrangements with third parties);
- the risk could be shared with others (eg a joint venture project);
- the risk may need to be insured against ( eg employers liability, third party liability, theft, fire)

#### Use of a risk register:

The most common tool used is a risk register, which incorporates an assessment of the level of risk together with an action plan for its management. This will also identify someone to take actions forward and give timescales or other milestones. This is not a science and can

be subjective, so it is important that it is understood and used by a range of people in the organisation and becomes a living tool to ensure appropriate responses are put in place.

The risk register below is the framework recommended by the Charity Commission. It combines the medium/high/low assessment from the risk map with a score, enabling an overall ranking by score of risks that your organisation may be subject to. In this model, the scales for both likelihood for occurrence and severity of impact are based on 1 to 5, with 5 being the highest level of likelihood or severity.



- Put your highest scoring risk as the first on your register with lower scoring risks below.
- The Board needs to agree how regularly to review the risk register at their meetings, or it may decide to only review risks over a certain score.



**Institute of Risk Management**

**NCVO - Tools for tomorrow**

Risk areas Risk identified	Likelihood of occurrence (score)	Severity of impact (score)	Overall or "gross" risk	Control procedure	Retained or "net" risk	Monitoring process	Responsibility	Further action required	Date of review
E.g. Lack of capacity for fundraising – reserves very low	<b>High</b> (5)	<b>High</b> (5)	<b>High</b> (25)	Reserves policy set by board.  Fundraising targets set.	<b>Medium</b>	Finance and fund-raising reports reviewed quarterly by board.	Board/ treasurer	Agenda item for board meeting	Monthly

# Adjusting to Change

In this chapter we offer suggestions for managing and responding to changing financial circumstances whether caused by the economic downturn or by changes to funding. It is important for your organisation to plan its response and implement changes effectively in order to continue providing the best service it can.

This chapter offers introductory advice and links to further information and support in four key areas:

1. Managing pressures on staffing
2. Preparing for redundancy
3. Collaboration and mergers
4. Managing finances

## 1. Managing Pressures on staffing

During difficult times pressures on staff will more than likely increase, there are a number of things an organisation can do to try and ease these pressures. In this section we will cover three strategies that could help:

- 1.1. Communication and consultation with staff
- 1.2. Strengthening team leader capabilities
- 1.3. Supporting the health and well being of staff

### 1.1. Communication and consultation with staff

Good **communications** are central to the smooth running of any organisation; large and small. During periods of uncertainty and change the way the organisation communicates with staff is vital.

The key thing to ensure is that there is a **consistency of approach** in a) the information provided; b) the channels in which it's communicated, and c) the way in which it is communicated. An organisation should plan the best ways to deliver its communication and inform staff so that everyone feels as though they are in the loop.

Staff **consultation** is the process by which management and staff (or their representatives) jointly examine and discuss issues of mutual concern. In certain circumstances consultation with independent recognised trade unions is a legal requirement.

Consultation with staff can be lengthy and resource hungry process, the organisation will have to weigh up the pros and cons of such an action. If an organisation starts a consultation process there is an obligation that the views of staff will be sought and considered before decisions are taken. However, ultimately the final decisions will be made by the senior managers and the Board.



- Manage expectations and set a clear sense of direction.
- Keep employees in the picture even when there is little concrete news.
- Keep communication up to date to keep rumours to a minimum.



**Acas guide** - Employee Communications and Consultation

### 1.2. Strengthen team leader capability

Providing support for team leaders and supervisors will mean that they are better able to operate in periods of traumatic change. In particular, staff with line management responsibilities may need support to acquire the skills required to reduce and **prevent stress at work**.

**Identifying stress:** There is a clear distinction between pressure, which can be a motivating factor, and stress, which can occur when this

pressure becomes excessive. Stress is the adverse reaction people have to excessive pressures or other types of demands placed upon them.

The Health and Safety Executive (HSE) have developed 'Management standards for reducing stress' and also provide a 'line management competency tool' (see resources). It is imperative that team leaders and anyone with line management responsibility can demonstrate positive appropriate behaviours, for example:

- Show a positive attitude to stress and mental health issues.
- Demonstrate awareness, recognition and early identification, of possible problems so that intervention at an individual level can take place as soon as possible.
- Show that they know how to approach issues sensitively.
- Know what systems and policies are relevant and keep that knowledge up-to-date.



- Brief team leaders in full on developments so they can talk to their teams.
- Recognise the vital role that team leaders play in every aspect of the employment relationship – make sure they are properly trained in day-to-day people management skills.
- Team leaders also need support and leadership from senior management to equip them to manage difficult situations and avoid burning out.



#### Health and Safety Executive (HSE)

**HSE** - Management competencies for preventing and reducing stress at work

**HSE** - Management standards for reducing stress

**HSE** - Line management competency tool

### 1.3. Supporting the health and well-being of staff

It is recognised that a recession can have a **psychological impact** on staff. You can reduce or even prevent high levels of work-related stress by providing workplace support and occupational health provision.

#### For example:

- Where possible provide opportunities for flexible working to help employees balance their work and home lives.
- Ensure you have mechanisms in place to deal with workplace stress and potential conflict at an early stage.
- Recognise the potential negative impact of 'survivor syndrome' if your organisation has made redundancies – staff that remain in organisations where there have been job cuts often suffer from guilt while coping with increased workloads.
- Think about creative, non-financial ways of motivating employees such as recognition schemes, team-building days and employee awards.



**Acas guide** - Health, Work and Wellbeing

**Acas guide** - Flexible Working and Work-life Balance

**Acas guide** - Stress at Work

**Acas guide** - Mediation: An employers' guide

## 2. Preparing for redundancy

During tough times it will be prudent for an organisation to develop a **strategy for redundancy** so it's ready if it's needed. The planning process will help the Board consider the best way forward for the organisation. This section will cover key areas for consideration:

**2.1** Planning ahead

**2.2** Ways to minimise redundancies

**2.3** Consultation Process

**2.4** Redundancy selection criteria

**2.5** Supporting redundant staff to find other work

### 2.1. Planning ahead

It is advisable to start thinking about how you will handle significant redundancies **at least three months** before you anticipate they might need to take effect. Planning ahead will help the organisation manage any redundancy situation in a fair and equitable manner.

It is imperative that the Board have a clear understanding of the **law relating to redundancy**. The risk of getting it wrong can be detrimental to both the organisation's finances and reputation. If the Board is unsure whether their understanding of redundancy law is up-to-date it is advisable to get expert advice, from Acas for example.



**Acas advisory booklet** - Redundancy handling  
CIPD factsheet Redundancy

## 2.2. Ways to minimise redundancies

Redundancies can have a serious **negative impact** on morale and performance. If staff reductions are inevitable the Board may wish to consider ways to minimise redundancies, for example:

- Nonreplacement of departing staff
- Offer voluntary redundancy terms
- Cut back recruitment
- Review your use of temporary staff.
- Retrain staff whose skills are no longer in demand
- Redeploy staff to other parts of the organisation where possible.
- Reduce or eliminate overtime working.
- Consider short-time working, temporary lay-offs or sabbaticals.
- Encourage staff to suggest how jobs can be done more efficiently and costs saved.



**Acas leaflet** - Lay-offs and Short-time Working

## 2.3. Consultation Process

In law, employers who propose to dismiss as redundant **20 or more employees** over a period of 90 days or less, have a statutory duty to consult representatives of any recognised independent trade union, or if no trade union is recognised other elected employees.

If an employer is thinking of dismissing an employee on the grounds of redundancy, and the employee is **not being consulted** under any collective redundancy arrangement, they must follow a **statutory dismissal procedure**.

## 2.4 Redundancy selection criteria

It's never an easy job to select people for redundancy; you can offer voluntary redundancy, but while this might mean that the Board can avoid making those difficult decisions there is also a chance that it will lose skills vital to the organisation.

At the end of the day it's advisable to identify and agree on objective criteria that can be applied in an unbiased way. Objective criteria can include:

- attendance records (not including agreed leave)
- disciplinary records
- skills, experience or competence
- skill requirements for the new organisation

Ensure that the selection criteria are based on accurate records and are not discriminatory, directly or indirectly. And remember failure to follow a fair selection procedure may give rise to claims of unfair dismissal.

## 2.5 Supporting redundant staff to find other work

Any member of staff facing redundancy will need support and advice on how to cope; it is good practice to offer the following.

- Allow time off to let affected staff look for other work or arrange training.
- Explore the possibilities of help or financial support for training and advice from government agencies such as Jobcentre Plus and Train to Gain.
- Remember your treatment of staff that leave the organisation will impact on the attitudes and loyalty of those who remain.

## 3. Working collaboratively

NCVO's Collaborative Working team defines collaborative working as a partnership between two or more voluntary organisations. Collaborative working can be seen as a spectrum, from informal networks, through joint delivery of projects to full merger. Collaborative working can last for a fixed time or be permanent.

Collaboration can help maintain important services whilst reducing overheads and making income go further. In this section we will look at what collaboration could do for you - from finding ways to stretch a limited budget to more efficient service delivery.

This chapter offers introductory advice and links to further information in the following areas:

- 3.1 Collaborating to reduce costs
- 3.2 Collaborating to develop the organisation

### 3.1 Collaborating to reduce costs

Finding ways to **reduce costs** and stretch limited budgets may offer ways to keep the organisation going during tough times, here are a few ways that organisations can join up their resources or functions for **mutual gain**.

#### Sharing resources and back office functions

Organisations can collaborate on just one support service or many. They can do so from separate locations or by sharing premises. Each organisation can maintain its own identity or partners can create a **new organisation** to share services.

**Employment law:** Organisations taking on functions previously carried out by another organisation or transferring work to another employer may be affected by TUPE, the Transfer of Undertakings (Protection of Employment) Regulations. These concern the rights of employees to protection for their terms and conditions. Legal advice should be taken on whether and how TUPE affects you.

#### Examples of ways to cut costs through collaboration:

- Sharing staff – the most popular are HR and Finance functions
- Sharing premises
- Sharing back office services (e.g. admin, marketing) and equipment
- Joint purchasing arrangements
- Shared IT systems



- If you choose to outsource back office functions try an incremental approach. Prioritise, then start small and gradually increase the services that you share, this will allow you to build confidence among partners, clients and their staff and volunteers.
- Set up a system to maintain regular contact with partner organisations. Poor communication can lead to misunderstandings which may damage a shared project.



**Bassac** - Sharing without merging. A review of Collaborative working and Sharing Back Support in the VCS

**Bassas** - Sink or Swim: Towards a 21st century community sector ICT hub, NCVO, March 2008 - Shared systems research

### Joint Service Delivery

As well as financial efficiencies, collaboration promotes more **efficient service** delivery by highlighting areas of overlap and duplication. Voluntary and community sector organisations are often well placed to develop formal collaborations to bid to deliver public services. The size of some competitive tenders means that collaborative working may be the best way for smaller organisations to secure a role and share their **specialist knowledge** and reach.

#### Benefits include:

- a wider range and reach of services
- opening up opportunities for funding and the potential to go for bigger contracts
- reduced duplication of services

#### Better buying power

Bulk buying isn't a new concept but it may be worth considering on items that you use a lot of regularly, by teaming up with other organisations with similar requirements you may be able to negotiate a better deal for buying more. The Charities Buying Group provides dedicated services to serve all charities and not for profit organisations irrespective of size offering a wide range of buying agreements that will help your organisation reduce costs.

#### It offers the following range of services:

- On-line access to a full range of buying agreements to reduce your costs
- On-line ordering
- On-line direct enquires to our suppliers
- Invoice price comparisons
- Telephone purchasing help and advice



**Charities buying Group** - [www.charitiesbuyinggroup.com](http://www.charitiesbuyinggroup.com)

### 3.2 Collaborating and merging to develop the organisation

'...all charities should consider seriously and imaginatively whether there are ways in which they could do more and better for their users by working together.' *Charity Commission, Collaborative Working and Mergers (RS4) 2003*

Collaboration has been suggested as one response to the recession, but organisations should ensure that they are exploring collaboration or merger from a position of strength. They should plan early, identify potential partners, and make informed decisions about whether and how to proceed with collaborative projects.

#### Working with others can offer opportunities to:

- Deliver new, improved or more integrated services
- Make efficiency savings through sharing costs
- Develop a stronger, more united voice
- Share knowledge and information



**Bassac** - Collaborate Resource Kit Housing Association's Charitable Trust, HACT, July 2008.

**Office of the Third Sector, Cabinet Office, Dec 2008** - Working in a consortium: A guide for third sector organisations involved in public service delivery

**NCVO Collaborative Working Unit, Feb 2006** - Joint working for public service delivery

**The Prince's Trust Making Partnerships Work, 2005**. A study of partnership-working in The Prince's Trust and a practical guide to building and maintaining effective partnerships

NCVO's guidance sheet '**Should you collaborate? Key questions**' provides a checklist to help organisations decide whether to embark on formal collaborative working or merger. It identifies the key issues which organisations need to consider, giving an idea where problems and complications might lie and enabling them to make informed decisions.



**NCVO** - Should you collaborate? Key questions

**NCVO** - Guidance for organisations exploring Merger

#### What kind of support is available?

Bassac have developed a **cluster support package** which may be useful for organisations who want to pursue partnership working, the package includes:

- Establishing the partnership or 'cluster' in defining roles and ground rules (including model agreements if wanted)
- Collecting data from partners that will build a picture of the local context
- Defining and agreeing the group's goals & developing an action plan
- Specific issues such as proposing an appropriate legal structure, business plan review, developing a fund-raising strategy etc.



For more information on **Bassac's Cluster Support package** visit their website (see appendix 1)

## 4. Managing Finance

When your income is reduced, costs need to be reduced too. In this section we discuss the steps needed to manage your cashflow and keep on top of your costs by doing more with less.

This chapter will cover:

- 4.1** Mind the cashflow!
- 4.2** Doing more with less

### 4.1 Mind the cashflow!

Cashflow is the balance of money entering and leaving a business. Many organisations can **experience short-term cashflow difficulties**. Often these problems can be anticipated, which means that solutions can usually be found before the problem is urgent. During uncertain times it is important to know how much money your organisation has in the bank, how much it owes and how much it is owed. Regularly updating your financial records enables you to do this.

**The importance of forecasts**

Forecasting will help you to **anticipate** potential financial problems before they happen. Cashflow forecasts show likely income and expenses as they affect your bank account and will enable you to identify when additional funds might be required. Income and expenditure forecasts will help you identify whether you have enough income to cover your intended expenditure.

Take practical steps to maintain **healthy cashflow** by routinely checking actual income against the forecast and actual costs against the budget set. Routinely revise the forecasts with updated information.

By keeping an eye on costs you can keep them to target. One way to do this is to develop and share the budget and assign **responsibility to staff members** to bring it in on target.



- Understand exactly what your finances are telling you.
- Review and update changes to cashflow
- Issue invoices promptly and chase up debtors
- Ensure that your funding is received in advance rather than in arrears
- Negotiate longer credit terms with suppliers
- Keep in touch with the bank



**Social Enterprise Works** - Cashflow projection template  
**Social Enterprise Works** - Financial Management and Accountability - Guidance Notes  
**Social Enterprise Works** - Financial forecasting & planning guidance notes  
**Finance Wales**, A Practical guide to cashflow management  
**BERR** – Managing Cashflow guides  
**The Better Payment Practice Campaign**

**4.2 Doing More with Less**

On one hand, your organisation would like to increase its capacity and on the other there is a requirement to cut costs – ideally you would like to do both. However, developing a cost-reduction strategy that maximises

efficiency without compromising growth potential can be difficult. The organisation should resist pressure to make indiscriminate cuts, focus on identifying core areas where efficiency can be improved, trim and consolidate non-core functions.

**Outsourcing** (getting another organisation to do the work) might seem to be an easy answer. Even in the third sector contracting out non-core business functions such as human resources or payroll to third-party providers is gaining acceptance. But once a company decides to outsource, it also exposes itself to new forms of risk, for example quality, confidentiality, reliability, escalating costs. It is vital to consider potential ways to minimise outgoings and be prepared to implement them if necessary.

**Reducing costs**

Assess your **fixed costs** (often called overheads), which you pay for regardless of your service delivery. They include rent, rates and wages. Many organisations fail to realise that savings can sometimes be made on these, try negotiating with your landlord or suppliers or consider sharing premises with an organisation in a similar situation.

The organisation can also try to make savings on its **variable costs**. Variable costs are linked to your service delivery and include materials, transport costs, phone calls, marketing & printing etc. There are a number of price comparison websites available to help you cut cost on utilities etc. Cutting costs by too much or in the wrong areas can have a negative effect, so be careful.

You may find that your business needs to adjust staff costs in order to survive the economic slowdown. This may mean that you could make savings by employing part-time workers for certain areas of your organisation and it may mean that circumstances oblige you to downsize and make certain roles redundant. (See previous chapter)

**Getting the most out of suppliers**

To minimise your costs, you will need to **manage your relationships** with suppliers effectively and assess their performance regularly. Your bank is also a supplier, check whether you are paying too much and consider

using a bank that works with third sector organisations such as Charity Bank.

**Understanding the cost of change**

You will have contracts with your suppliers (including your landlord) and if you want to change your suppliers you will need to understand whether you will incur any penalties by terminating the contracts, or when those contracts come up for renewal and you therefore have a chance of making savings.

The following table gives a framework for auditing your supplier contracts:

Service	Supplier	Length of contract	Notice period if any	Any penalty for early termination
Landlord	X company	Licence to Mar 2010	3 months	Up to three months rent if move within notice period
Telephone system lease	Y company	Lease agreement for 5 years to 2012		LIABLE for residue of cost of equipment £XXXXXX
Water cooler	Z company	Rolling contract	1 month	None



**Chartered Institute of Purchasing & Supply (CIPS)** website - supplier relationship management:  
**Environmental guidance for your business**



- Make sure that your organisation has written financial procedures that are understood both by the Board and by staff.
- Managing your cashflow and ensuring that senior staff and Board are really competent to understand the implications of the cashflow is crucial.
- Project committed costs up to the point when the organisation has decided to cease activities
- Boards may want to check that bank reconciliations and the books are up to date so they have confidence that figures are really accurate.
- Boards may also want to check with their accountants on the status of recent accounts – to help assess outstanding liabilities and to value assets.
- When your accounts are up to date and accurate, the balance sheet is the key indicator and the Board may need to call for professional support to help them to understand their position.
- Make your organisation greener, help save the planet and reduce costs at the same time.

# Preparing for the Worst

**In the commercial world, an exit strategy usually means making sure the company can be sold on to someone else at the highest profit. Unfortunately, this is not the case for Third Sector organisations. The loss of major funding programmes can mean that organisations find they are unable to continue to deliver their activities and that even after reducing their costs and taking on board all the actions in the previous chapter, there comes a point at which the organisation is no longer viable and needs to close its operations. The current recession may also impact on Third Sector organisations as private Trust Funds may have less to distribute as interest rates dwindle, the charitable donations from the public may decline and the Government switches funds to recession tackling priorities.**

In this chapter we look at:

1. Warning signs and understanding liabilities
2. Worst case – insolvency and compulsory liquidation
3. Keeping in control – voluntary closure and how to do it

## 1. Warning signs

- Are you running down any reserves to support funding gaps?
- Have you no committed funding or contracts three months ahead?
- Are creditors chasing you for unpaid bills, in particular are any of these over £750?
- Have you been turned down for overdraft or loan finance?

## Understanding your liabilities

Having an understanding of all of your organisation's finances is crucial at this time if you are to avoid becoming insolvent with the implications that this brings for the reputation of your organisation and potential consequences for your Board.

As discussed in the previous chapter, maintaining a list that details all your contracts with their notice periods and the penalty that you may incur by failing to meet the notice period is vital. You will also need to look at all funding contracts to understand the implication of failing to meet that contract – are there any penalties or are you open to having to pay back any funds already received.

Understanding your closure costs means ensuring that you have adequate funds to pay staff redundancy, plus legal costs incurred as well as meeting all the costs of ending your contracts and paying for actual bills up to the date of the closure of your organisation.

## 2. Worst case – insolvency and compulsory liquidation

**An organisation is deemed as insolvent when:**

- it is unable to pay its debts as they fall due; or
- when the value of its assets is less than the amount of its liabilities taking into account its possible and prospective liabilities.

Once an incorporated body (registered with Companies House or FSA) becomes insolvent, the duties of its Board are to ensure that the creditors are protected and that no steps are taken that would disadvantage creditors or increase their losses – this generally means winding up the organisation.

It is important that there is a clear understanding when this point is reached as there are two offences that the Board need to avoid. In the circumstances described below directors are NOT protected by limited liability.

**Wrongful trading** is when the organisation carries on running the operation and incurring debts once it has become clear, or should have become clear to a reasonable person, that there is no prospect of the organisation being able to meet those obligations. It can be

described as “when in a hole, don’t keep digging!” Directors become personally liable for liabilities incurred through wrongful trading

This is to ensure that the organisation is not deliberately setting out to act fraudulently and there are a number of safeguards for Directors who find themselves in a wrongful trading position through a range of unforeseen circumstances. However – if there is **fraudulent trading**, which is where the Directors carry on trading deliberately with the intention of defrauding creditors, not only are Directors liable for the debts, but they can be liable to criminal proceedings.

Once you cannot meet your obligations to all creditors, you also need to be careful not to prefer one creditor over another.

### Liability of Board members

Keeping a close eye on cashflow and liabilities is crucial if Board members are to be protected. Their **personal exposure** will vary depending on the legal status of the organisation.

If the organisation is not incorporated and cannot meet its obligations then the Board members will be personally liable for its debts. If the organisation is incorporated as a company limited by guarantee or shares, or a Community Interest Company or an Industrial and Provident Society then the Board member has protection above the level of the guarantee (usually £1). It is very rare that any Board member may have a personal guarantee for any loans made to the organisation – but again, that Board member would be liable for the outstanding liability on the loan.

However, if the company (or other incorporated body) goes into formal insolvency proceedings and has been wrongful trading and it can be demonstrated that this was not unforeseen, then the Board members lose the personal protection for the debts incurred and can also be liable to be disqualified from being a director for up to fifteen years. Other common reasons for **disqualification** are failing to keep proper accounts, not filing them and other returns with Companies House and not paying tax that is due. This could have devastating impact on the individual Board member – so their personal protection from this risk is tremendously important.



- Get professional advice from your solicitor or accountant immediately if you have any concerns about your organisation being insolvent.
- Boards need to ensure that their decisions are very carefully minuted if they are getting close to being insolvent as this is evidence of their intentions.

### What types of liquidation are there?

- Compulsory liquidation (or compulsory winding up) - this is when the court makes an order for the company to be wound up (a 'winding-up order'). This order can be triggered by a creditor who is owed more than £750 who can apply to the court to ask it to wind up the business because the company owes a sum of money and can't pay it. Then an Official Receiver is appointed to sell the assets and pay the creditors.
- Creditors' voluntary liquidation (or creditors' voluntary winding up) - this is when the shareholders of a company decide to put the company into liquidation, but there are not enough assets to pay all the creditors, i.e. the company is insolvent.

### But there is also

- Members' voluntary liquidation (or members' voluntary winding up) - this is when the shareholders of a company decide to put it into liquidation, and there are enough assets to pay all the debts of the company, i.e. the company is solvent.



### Charity Commission:

#### Managing financial difficulties and insolvency in charities

**Companies House** - Liquidation and Insolvency - GBW1

**Companies House** - Strike-off, Dissolution and Restoration - GBW2

### The Insolvency Service:

**A guide for directors** – to compulsory liquidation

### 3. Keeping in control - managing voluntary closure

Making the decision to close will always be a difficult one, but in the light of the section above, it is crucial to make that decision while solvent and able to make voluntary arrangements rather than having creditors file for insolvency in the courts.

The decision rests with the Board and needs to be carefully minuted as it then starts a process which will vary with the legal structure of the organisation.



- The Board will need to maintain bank signatories until the end of the process and need to be available to complete everything once paid employees have gone.
- The company needs to ensure that all documents are filed at Companies House and that Companies House is notified about any changes to the Board or registered office (until the company is finally struck off the register)
- Note that this is often the role of the Company Secretary, who in many Third Sector organisations is an employee so may need to be replaced by a remaining Board member.

#### Alternatives to liquidation

If there are only a few creditors, it may be possible to make an informal arrangement to restructure your organisational payments to enable you to keep going. If that is not the case, there are a range of routes that can be taken.

Company Voluntary Arrangements and Administrations both give companies protection from being forced into liquidation for a limited period. They are designed to help keep the company going while trying to find a solution to its financial difficulties. However if a solution can't be found then the final outcome will be liquidation.

**Company Voluntary Arrangement (CVA):** If a company is in financial difficulties, it may attempt to enter into a CVA. The company proposes an arrangement for repaying creditors, and a meeting of creditors is held for the creditors to vote whether to accept the proposal. If a majority in excess

of three-quarters in value of creditors present (in person or by proxy) accept the proposal, all creditors are bound by the arrangement. The CVA is managed by an Insolvency Practitioner.

The effect of a CVA is that such creditors cannot commence action against the company to recover money owing, unless the company fails to fulfill the terms of the CVA

**Administration:** Administration is managed by an administrator, who is an authorised insolvency practitioner appointed to manage the affairs, business and property of a company.

A company may take itself into administration, or be taken into administration through a court order. The Administrator has the objective of rescuing the company wherever possible.

Administration effectively protects the company from any action by creditors to recover money for a limited period, e.g. a creditor cannot petition for the winding up of a company whilst it is in administration.



- This is a complex area and professional advice on options should be taken from a solicitor or insolvency practitioner.
- You may also come across a company going into administration when they owe you money. If so, you should treat the possibility of being paid with great caution.

#### Members' voluntary liquidation

There is a prescribed process to go through which would need to be carefully timetabled to ensure that the appropriate notices are met. This can take place when the directors of a company believe that the company is solvent.

1. A majority of the company's directors must make a **statutory declaration of solvency** in the 5 weeks before a resolution to wind up the company is passed.

The statutory declaration will state that the directors have made a full inquiry into the company's affairs and that, having done so, they believe that the company will be able to pay its debts in full within 12 months from the start of the winding-up. The declaration will include a statement of

the company's assets and liabilities as at the latest practicable date before making the declaration.

2. Notice of the **special resolution** for voluntary winding-up of the company must be published in the London Gazette within 14 days of the general meeting. The company must also send a copy of the declaration and the special resolution to the Registrar within 15 days of the general meeting.
3. The liquidation starts when the members, in general meeting, having been given the requisite amount of notice in the company's articles of association, pass a resolution (Companies Act 1985 or Companies Act 2006) (usually a special resolution) to wind up the company voluntarily.

### Closing an Industrial and Provident Society

An industrial and provident society is an organisation conducting an industry, business or trade, either as a co-operative or for the benefit of the community, and is registered under the Industrial and Provident Societies Act 1965.

If the IPS is solvent, but has decided to close, it does so through an Instrument of Dissolution which is a form available from the Financial Services Authority. It requires the signatures of at least two thirds of the Society's members.



### FSA Instrument of Dissolution

#### Charity closure

**The law says:** A charity can only be wound up if:

- all of its property is expendable and has been disposed of; or
- the governing document contains a dissolution or winding-up provision; or
- in the case of a charity with permanent endowment, the trustees have used the powers in sections 75, 75A or 75B of the 1993 Act to remove the permanent endowment restriction on their charity's capital and have then decided to wind the charity up; or
- the trustees have decided to transfer their charity to another with similar objects. This can be quite simple for charities whose capital is entirely expendable; for charities with permanent endowment, it is still possible

to make a transfer either by using the power in section 74 of the 1993 Act (for charities whose yearly income is £10,000 or less) or (for larger charities) seeking a Scheme from the Charity Commission to allow such a move.

**After winding up:** Whenever a registered charity is wound up or ceases to operate because all its property has been spent or transferred to other charities, the trustees must send a copy of the final accounts (showing a nil balance and how the remaining assets were distributed) to the Charity Commission, with a request to have the charity removed from the Register of Charities.



### Charity Commission - Bringing your charity to an end

#### Closing an unincorporated organisation

This is the simplest legal process, through no less traumatic for those involved. The organisation needs to follow its constitution, which should include a process for its dissolution. This would normally be done through a resolution to a special meeting with a defined majority and should also consider the distribution of any residual assets after all liabilities have been met.

#### After the decision – what comes next?

There is a large amount of work to be done, here's a checklist of key steps:

- Send a notice to customers (including funders), suppliers (including landlord), creditors, contractors
- Closing the operations
- Sell or transfer the ownership of assets
- Pay off debts
- File business dissolution papers
- Complete final accounts and pay any tax due
- Close bank account
- Store the business records according to legal requirements – the officers of the company must retain the accounting records for six years from the date of closure.

### Closing the operations

Of course, this means giving notice of termination of employment to all staff (which can be up to 12 weeks notice for staff with 12 years or more service). The Board will need to ensure that it retains the capacity to work through the closure checklist above so may for example retain the senior manager or finance director slightly longer than other staff to ensure this is possible.

Many Third Sector organisations have client records which are sensitive and the disposal of these records will need to have consideration to the Data Protection Act. Advice on best practice will need to be sought from sector infrastructure bodies.

The same is true for other intellectual assets such as databases. You may want to hand them to another not for profit organisation as a legacy, but again you may need to get permission under Data Protection arrangements.

In order to close solvently, the organisation may need to sell some or all of its assets at market value in order to pay creditors. Any limitations of the disposal of those assets, if for example they have been purchased through a particular funding stream and have covenants attached to them, need to be acted upon.

However – having done all this, any remaining assets (including cash) should be passed on to another not for profit organisation identified by the Board.



- Board members will be required right up to the final closure point as bank signatories and to sign off final accounts.
- Check previous funding records to see how long records need to be kept – this can be up to nine years for some EU funds.

### Local Support

Consortium members provide a range of support activities and training on a range of issues, both generalist and specialist, including trustee responsibilities and governance. They also may have access to professional support such as lawyers, HR professionals and others on a pro-bono (ie: free) basis. Please check their individual websites for details.

Bath & North East Somerset  
Racial Equality Council  
[www.bathnesrec.org.uk](http://www.bathnesrec.org.uk)  
01225 442352

Black Development Agency  
[www.blackdeva.org.uk](http://www.blackdeva.org.uk)  
0117 9396645

Community Action  
[www.community-action.org.uk](http://www.community-action.org.uk)  
01275 393837

CVS Bath & North East Somerset  
[www.banescvs.org.uk](http://www.banescvs.org.uk)  
01225 330090

CVS South Gloucestershire  
[www.cvs-sg.org.uk](http://www.cvs-sg.org.uk)  
01454 865205

Social Enterprise Works  
[www.socialenterpriseworks.org](http://www.socialenterpriseworks.org)  
0117 9070080

The Care Forum  
[www.thecareforum.org](http://www.thecareforum.org)  
0117 9654444

Voluntary Action North Somerset  
[www.vansweb.org.uk](http://www.vansweb.org.uk)  
01934 410192

Volunteering Bristol  
[www.bristolvolunteers.org.uk](http://www.bristolvolunteers.org.uk)  
0117 9897733

Voscur  
[www.voscur.org](http://www.voscur.org)  
0117 9099949

## Appendix 1 Further Information:

### Useful websites

Health and Safety Executive (HSE)  
**[www.hse.gov.uk](http://www.hse.gov.uk)**

Advisory, Conciliation and Arbitration Service (Acas)  
**[www.acas.org.uk](http://www.acas.org.uk)**

Chartered Institute Personnel Development (CIPD)  
**[www.cipd.co.uk](http://www.cipd.co.uk)**

Department of Business, Enterprise & Regulatory Reform (BERR)  
**[www.berr.gov.uk](http://www.berr.gov.uk)**

British Association of Settlements and Social Action Centres (BASSAC)  
**[www.bassac.org.uk](http://www.bassac.org.uk)**

National Council for Voluntary Organisations (NCVO)  
**[www.ncvo-vol.org.uk](http://www.ncvo-vol.org.uk)**

Office of the Third Sector, Cabinet Office  
**[www.cabinetoffice.gov.uk](http://www.cabinetoffice.gov.uk)**

Social Enterprise Works  
**[www.socialenterpriseworks.org](http://www.socialenterpriseworks.org)**

Finance Wales  
**[www.cimaglobal.com](http://www.cimaglobal.com)**

Chartered Institute of Purchasing & Supply (CIPS)  
**[www.cips.org](http://www.cips.org)**

Charity commission  
**[www.charity-commission.gov.uk](http://www.charity-commission.gov.uk)**

The Institute of Risk Management  
**[www.theirm.org](http://www.theirm.org)**

Charities buying Group  
**[www.charitiesbuyinggroup.com](http://www.charitiesbuyinggroup.com)**

Environmental guidance for your business  
**[www.netregs.gov.uk/-](http://www.netregs.gov.uk/)**

Companies House  
**[www.companieshouse.gov.uk](http://www.companieshouse.gov.uk)**

The Insolvency Service  
**[www.insolvency.gov.uk](http://www.insolvency.gov.uk)**

NAVCA (National Association for Voluntary and Community Action)  
**[www.navca.org.uk](http://www.navca.org.uk)**

Business Link  
**[www.BusinessLink.gov.uk](http://www.BusinessLink.gov.uk)**

FSA (Financial Services Authority)  
**[www.fsa.gov.uk](http://www.fsa.gov.uk)**

ACEVO (Association of Chief Executives of Voluntary Organisations)  
**[www.acevo.org.uk](http://www.acevo.org.uk)**

Capacitybuilders  
**[www.capacitybuilders.org.uk](http://www.capacitybuilders.org.uk)**