FINANCIAL REPORTING IN HOUSING ASSOCIATIONS

Professional 2 examination
8 June 1999

From 10.00 am to 1.00 pm
plus ten minutes reading time from 9.50 am to 10.00 am.

Instructions to candidates

Answer ***four*** *questions in total.* ***Both*** *questions from Section* ***A****, and* ***two*** *questions from Section* ***B****. The marks available for each question are shown in italics in the right-hand margin.*

All workings should be shown. Where calculations are required using formulae, calculators may be used but steps in the workings must be shown. Calculations with no evidence of this (for example, using the scientific functions of calculators) will receive no credit. Programmable calculators are not permitted in the examinations room.

Formula sheets, statistical tables, graph paper and cash analysis paper are available from the invigilator, where applicable.

SECTION A (Answer both questions)

1

The following list of balances has been taken from the accounts of Emmerdale Housing Association on 31 March 1999.

Trial Balance 31 March 1999

	£000
Turnover	8,400
Operating Expenditure	5,320
Investment income	696
Interest	1,380
Repairs reserve	3,112
Rent surplus reserve	1,200
Housing held for letting	140,808
Housing under construction	18,768
Grants – HAG	131,528
Other fixed assets – buildings	4,000
Other fixed assets – equipment	1,692
Depreciation (other fixed assets)	1,252
Current assets	23,532
Creditors less than 1 year	1,296
Creditors after 1 year	28,104
Grant redemption fund	212
Share capital	4
Accumulated surplus	19,696

Additional Information

The following transactions are not included in the above trial balance:

(i) The rent surplus for the year was £1,228,000 and should be transferred to the Rent Surplus Reserve.

(ii) Operating expenditure includes repairs of £892,000 that should be financed from the Repairs Reserve.

(iii) Authorisation has been given to transfer £668,000 from rent surpluses to fund future major repairs.

(iv) Properties were sold during the year for £3,000,000 which originally cost £2,400,000. These properties were originally 90% funded from Housing Association Grant. From 1998/99 surpluses from sale of properties after Housing

Association Grant should be set aside in a capital reserve for the funding of future developments. Any Housing Association Grant adjustments will be paid in April 1999.

(v) Capital construction expenditure during the year amounted to £24 million which was 20% funded by borrowing, the rest being funded from Housing Association Grants. The new loans have still to be entered in the accounts.

(vi) It is the Association's policy not to depreciate housing properties. Other assets should be depreciated in 1998/99 by charging a full year's depreciation in the year of acquisition and assuming nil scrap value, normally using the following asset lives:

- buildings over 40 years; and
- equipment over 5 years.

(vii) The letting management computer system was replaced at a cost of £2,000,000 and is expected to last for 5 years. The old system was sold for £4,000. It originally cost £1,200,000 six years ago, and had a net book value equivalent to its estimated scrap value of £40,000.

- **Requirement for question 1**

(a) Prepare the Income and Expenditure Account for the year ended 31 March 1999.

8

(b) Prepare a Balance Sheet as at that date.

12

(c) Outline five measures which could be used to assess the financial performance of a housing association.

5
(25)

2

The following information relates to Brookside Housing Association:

Balance Sheet as at 31 March

	1998	**1999**
	£000	**£000**
Fixed assets	21,600	25,400
Net current assets	4,200	4,920
Creditors due after 1 year	(13,000)	(15,520)
Provisions	(600)	(1,500)
	12,200	13,300
Share capital	40	60
Designated reserves	4,400	4,980
Accumulated surplus	7,760	8,260
	12,200	13,300

Notes

(i) Fixed assets comprise:

	31 March 1998	**31 March 1999**
	£000	**£000**
Housing properties	75,600	88,400
Housing association grant	(58,000)	(67,600)
Office equipment (at cost)	7,000	7,600
(depreciation)	(4,400)	(4,600)
Vehicles (at cost)	3,200	3,600
(depreciation)	(1,800)	(2,000)

(ii) Net current assets comprise:

	31 March 1998	**31 March 1999**
	£000	**£000**
Stocks	180	160
Debtors	3,100	3,720
Short term investments	6,800	8,800
Bank	700	(180)
Creditors	(320)	(360)
Housing loans	(5,200)	(6,280)

Non-housing loans	(1,060)	(940)

(iii) Creditors due after one year comprise:

	31 March 1998 £000	31 March 1999 £000
Housing loans	10,000	12,600
Non housing loans	3,000	2,920

(iv) Designated reserves comprise:

	31 March 1998 £000	31 March 1999 £000
Repairs reserve	2,400	3,020
Rent surplus reserve	1,400	1,200
Sales reserve	600	760

(v) During the year the following amounts were received/(paid):

	£
Bank interest	40,000
Interest on short term investments	420,000
Interest on bank overdraft	(20,000)

(vi) During the year the housing association made an early repayment of a housing loan of £1,000,000 which was not due for repayment until 2001.

(vii) Interest paid on loans was equal to 8% of the average of loans outstanding at the beginning and end of the year.

(viii) Derelict properties to the value of £140,000 were sold to a property developer for £260,000 during the year. This disposal also resulted in a repayment of HAG amounting to £100,000.

(ix) Other fixed assets were sold as follows:

	Asset Cost £000	Net Value £000	Proceeds £000
Office equipment	400	80	140
Vehicles	1,000	600	380

(x) Any surpluses arising from the sale of housing stock are credited to the sales reserve. Changes to other reserves arise as a consequence of transfers to and from the accumulated surplus.

- **Requirement for question 2**

(a) Prepare the Cash Flow Statement for the Housing Association for the year ended 31 March 1999, together with the appropriate supporting notes. *20*

(b) Why was a revision of FRS1 necessary and what are the main differences in the revised format? *5*

(25)

3

SECTION B (Answer two questions)

Annfield Housing Association wish to build and equip a special needs housing complex in accordance with its integrated living policy. Outline estimates of costs have been undertaken by the association which show that the total capital costs of the complex are likely to be in the region of £15 million and the on-going net revenue costs approximately £3 million.

The Association's Finance Committee are due to consider the different methods of funding the proportion of the capital cost not met by Housing Association Grant, and have requested that the Finance Manager provide the committee with a report considering the various methods of financing the shortfall and their financial and accounting implications.

The Finance Manager has requested that you draft a report for the Committee. She is keen that the report not only considers the various methods of funding that are available to the Association from external sources, but also considers the implications of entering into a Private Finance Initiative deal.

- **Requirement for question 3**

Write a report for the Finance Committee which:

(a) Identifies the methods of capital finance which may be available to the Association to finance the non HAG proportion of the capital cost. *5*

(b) Explains in detail the accounting implications of each of the funding methods identified (including journal entries where appropriate). *12*

(c) Outlines the implications of a PFI deal for the complex. *8*

(25)

4

S.T. Michael has recently joined the Board of your Housing Association. He is recently retired from a long career with Sparks & Mensa plc, where he was the Group Financial Controller.

Mr Michael has recently written the following memo to your Finance Officer:

From: S T Michael, Board Member
To: Penny Pincher, Finance Officer
Date: 7 June 1999

While I am settling in well to my new role and feel that, after a suitable period of familiarisation, I can make a useful contribution to the Association, there are some points I would like to have clarified regarding the material you sent me.

First of all, I am used to thinking of the users of the accounts as being senior managers, shareholders and institutional lenders (as was the case in good old S & M), and, consequently, I am a bit puzzled about just who the main users of the Association's published accounts are and what use they make of them?

Secondly, I have some detailed queries about a number of issues:

- what is our statutory framework and what is the position with regard to SSAPs and FRSs?
- what is this SORP I hear so much about just now?
- why don't we depreciate our housing stock?

Turning to the internal reporting arrangements, what are the main uses of these internal reports, and who uses them?

A fairly brief reply, covering these points would be greatly appreciated.

- **Requirement for question 4**

Draft a suitable response on behalf of the Finance Officer, which covers:

(a) The users and main uses of published accounts. *12*

(b) The detailed queries raised by Mr Michael. *5*

(c) The use and users of internal reports. *8*

(25)

5 Attached is the budget statement for the Estates Department as at month 7 (October). The budget statement shows that the department is currently underspent. However, as the newly recruited management accountant you have some concerns about the figures. After carrying out an analysis of the figures, and through discussions with the estates manager, you discover that the following changes need to be made:

(i) The pay awards for 1998/99 have recently been finalised but no adjustments have been made to the department's budgets. The details are as follows:

Estates Manager: 2.5% pay award for the year from the 1 April 1998. This award has been paid from 1 July 1998 with backpay being received in month 5.

Security/cleaning/maintenance staff: 3% for the year from 1 April 1998. This award has been paid from 1 October 1998 with backpay being received in month 8.

Grounds staff: 2% pay award for the year from 1 April 1998. This award will be paid from 1 November 1998 with backpay being received in month 8. Also, a bonus payment to all staff of £250 (gross and including employer's costs) was received on 1 July 1998.

(ii) The budget for electricity and gas needs profiling to reflect the seasonal climate variations. The Estates Manager suggests the following weightings:

Months 9, 10, 11	-	4
Months 1, 8, 12	-	3
Months 2, 3, 6, 7	-	2
Months 4, 5	-	1

(iii) Telephone bills have been paid monthly by direct debit from 1 April 1998.

(iv) Maintenance contracts are all paid on 1 January each year.

(v) An agreement has been reached with a stationery company to purchase in bulk every quarter a standard stationery supply of £375 per quarter.

(vi) Water charges are paid on 1 January each year.

(vii) Insurance premiums payments are made twice yearly on 1 April and 1 October.

Estates department budgetary control statement 1998/99 Month 7

1998/99 Actual Month 7 £	1998/99 Budget Month 7 £	Account Code	Description	1998/99 Actual FTE staff	1998/99 Budget FTE staff	1998/99 Actual YTD £	1998/99 Budget YTD £	1998/99 Variance £	1998/99 Annual Budget £
			Pay Costs						
2,375	2,317	01230	Estates Manager	1.00	1.00	16,625	16,217	408	27,800
4,759	3,750	01335	Security Staff	3.08	2.50	32,479	26,250	6,229	45,000
1,931	2,500	01340	Cleaning staff	2.25	3.00	16,306	17,500	-1,194	30,000
6,437	5,000	01345	Maintenance Staff	5.00	4.00	43,937	35,000	8,937	60,000
2,000	3,000	01445	Grounds staff	2.00	3.00	14,500	21,000	-6,500	36,000
			Total Pay			**123,847**	**115,967**	**7,880**	**198,800**
			Non Pay Costs						
1,950	2,542	03305	Electricity			12,790	17,791	-5,001	30,500
1,600	2,142	03310	Gas			10,800	14,991	-4,191	25,700
750	0	03405	Telephones			5,250	4,500	750	9,000
0	0	03500	Maintenance contracts			0	14,500	-14,500	14,500
353	417	03505	Cleaning materials			4,650	2,917	1,733	5,000
125	167	03605	Office equipment			125	1,167	-1,042	2,000
500	125	03610	Stationery			1,500	875	625	1,500
0	1,250	03620	Furniture and Fittings			5,000	8,750	-3,750	15,000
0	146	03705	Uniforms			1,500	1,021	479	1,750
600	375	03805	Grounds maintenance			3,500	2,625	875	4,500
3,200	1,042	03810	Maintenance & Repairs			10,500	7,292	3,208	12,500
0	0	03900	Water Charges			0	1,250	-1,250	2,500
2,250	0	04100	Insurances			4,500	0	4,500	4,500
			Total non-pay			**60,115**	**77,679**	**-17,564**	**128,950**

Total	**183,962**	**193,646**	**-9,684**	**327,750**

During your discussions, the Estates Manager raised a number of issues for clarification.

- What is the purpose of budget profiling?
- What action should he be taking on receipt of his budgetary control statement?
- How are the expenditure items profiled?
- Why don't we adopt exception reporting?
- Is commitment accounting any good?
- Why am I held responsible for items over which I have no control, e.g. water rates, salary increases, insurance, etc.?

- **Requirement for question 5**

(a) Prepare a revised budgetary control statement for month 7 which takes the above information into account. *13*

(b) Reply to the queries raised by the Estates Manager. *12*

(25)