FINANCIAL REPORTING IN HOUSING ASSOCIATIONS

Professional 2 examination
5 June 2001

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

Paradise Housing Association is a Large Scale Voluntary Transfer (LSVT) Association which has been in existence since 1996 and was completely funded by private loans at the time of transfer. The following list of balances (rounded to the nearest £000) has been taken from its accounts at 31 March 2001:

	£000
Turnover	5,387
Operating costs	3,899
Gain on sale of fixed assets	23
Interest receivable	27
Interest payable and similar charges	1,091
Deficit brought forward at 1 April 2000	41
Housing properties (at revalued amount)	23,840
Housing properties under construction (at cost)	874
Shared ownership properties under construction (at cost)	74
Office property (at cost)	330
Improvements to office property (at cost)	110
Equipment (at cost)	100
Grants received (housing properties under construction)	505
Grants received (shared ownership under construction)	46
Debtors	204
Cash and bank (Dr)	461
Creditors due within one year	1,161
Loans	13,638
Share capital	0
Revaluation reserve	9,238
Accumulated depreciation (housing properties)	783
Accumulated depreciation (office property)	134
Accumulated depreciation (improvements)	51
Accumulated depreciation (equipment)	30
Suspense account (Cr)	1

The following information needs to be taken into account in producing the financial statements for the year:

(i) At 1 April 2000 there were only 50 members holding a fully paid up share of £1. However, a marketing drive during the year resulted in an extra 950 members being admitted after paying for their £1 share; this amount had been credited to the suspense account.

(ii) In accordance with the 1999 SORP, the Association has to provide for depreciation in the accounts. The value of land included in the revalued properties above has been calculated as £10.5m; the estimated useful life of the properties themselves is 50 years from 1 April 1996.

(iii) Housing properties under construction include £52,000 in respect of central overheads which had been capitalised.

(iv) Depreciation is to be charged on a straight line basis on other fixed assets as follows:

Office property	10 years

Improvements to office property	5 years
Other equipment	5 years

During the year, a new computer server was bought at a cost of £20,000 (which is included in the equipment in the trial balance); the old server (which had cost £10,000 in 1997/98) was obsolete and was taken away by a hardware disposal firm for a fee of £1,000, which is payable by the Association before the end of April 2001. This disposal has yet to be accounted for by the Association.

The Association's policy is to charge a full year's depreciation in the year of acquisition and none in the year of disposal.

(v) £270,000 is to be transferred from the revaluation reserve.

(vi) Because of the nature of its funding profile, no designated reserves have yet been created. However, the Committee of Management has taken the decision to create a Capital Repairs Reserve of £100,000.

(vii) A one-off bonus of £5,000 has yet to be paid to the Chief Executive for the period 1 January 2000 till 31 December 2000. No provision was made in the previous year's accounts for this payment and it has been agreed with the external auditors that no prior year adjustment is necessary.

(viii) During the year further borrowing was secured of £1.2m to fund some new build housing. Grants were secured of £700,000 from the funding body to assist with the cost of this development. The construction costs up to 31 March 2001 were £1.9m. The receipts and payments have been recorded through the bank account and suspense account. Interest costs of £62,000 need to be accrued on these borrowed funds.

- **Requirement for question 1**

(a) Prepare the income and expenditure account of the Paradise Housing Association in respect of the financial year ended 31 March 2001, together with the balance sheet as at that date. (Round figures to nearest £1,000.) *23*

(b) Outline two of the main differences between an LSVT Association and a traditional one. *2*

(25)

2

The following information relates to the Nirvana Housing Association:

Balance sheets as at 31 March

	2001	2000
	£000	**£000**
Fixed assets		
Housing properties	72,265	64,100
Social housing grant	(57,820)	(53,100)
Non housing fixed assets	1,435	1,315
	15,880	12,315

Net current assets	2,236	1,948
	18,116	14,263
Creditors: amounts falling due after more than one year	(9,600)	(8,150)
Provisions for liabilities and charges	(980)	(800)
Net assets	7,536	5,313
Capital and reserves		
Called up share capital	1	1
Designated reserves	1,250	985
Restricted reserves	644	500
Revenue reserves	5,641	3,827
	7,536	5,313

The following information has also been provided:

(i) Fixed assets comprise:

	31 March 2001	**31 March 2000**
	£000	**£000**
Housing properties held for letting	61,000	55,100
Housing properties depreciation	(750)	(500)
Housing properties under construction	12,015	9,500
Offices at cost	1,000	1,000
Office fixtures and fittings	675	395
Fixtures and fittings depreciation	(300)	(200)
Motor vehicles at cost	100	150
Motor vehicle depreciation	(40)	(30)

(ii) The increase in housing properties held for letting was due to:

- the acquisition of stock from another social landlord for £1,000,000;
- capitalised major repair costs amounted to £600,000; and
- schemes under construction reaching completion and transferred from the housing properties under construction account (the remainder).

(iii) During the year ended 31 March 2001 the Association also disposed of properties, which had previously been held for letting, for £500,000. These properties appeared in the accounts at £400,000, of which £350,000 had been funded from social housing grant. No depreciation had been charged on these properties.

(iv) Net current assets comprise:

	31 March 2001	**31 March 2000**
	£000	**£000**
Debtors	2,550	1,995
Investments	500	1,000
Cash	965	810
Repayments of loan principal	(400)	(500)

Other creditors	(1,379)	(1,357)

(v) Creditors: amounts falling due after more than one year comprise:

	31 March 2001	31 March 2000
	£000	**£000**
Long term loans	9,350	8,300
Deferred financing costs	(100)	(150)
Recycled capital grant fund	350	0

(vi) Non-amortising loans amounting to £1,450,000 were raised on 1 December 2000. All other loans are amortising and repayments of principal in respect of these loans took place on the due date (30 September 2000).

(vii) The weighted average interest rate on amortising loans was 8%; the rate of interest on the non-amortising loans raised on 1 December 2000 was 6%. £200,000 interest was capitalised and charged to the housing properties under construction account. The rate of interest on the average investment balance was 4%.

(viii) Five motor vehicles had been disposed of during 2000/2001 for £5,000 each. The vehicles, which had cost £50,000, had accumulated depreciation of £10,000 at the time of disposal.

- **Requirement for question 2**

Prepare the cash flow statement for the Nirvana Housing Association for the year ended 31 March 2001, together with the supporting notes.

25

SECTION B (Answer two questions)

3

Utopia Housing Association has a small team (the R&M Team) who carry out minor non-urgent repairs and maintenance work to the housing stock. Major repairs, programmed maintenance and emergency repairs are contracted out. The R&M Team target is to break even each year. For the year ending 31 March 2002 the budgeted position of the R&M Team is as follows:

	£000
Income	700
Labour	320
Materials	156
Supervision	50
Overheads	100
Administration	74
	700

The income is based on a schedule of rates for which a standard charge per job is estimated at the start of the year and then applies throughout the year. Experience has shown that the work is carried out evenly throughout the year: there are no seasonal variations.

The R&M Team has a labour force of eight, with supervision being provided by a foreman. Each member of the labour force is paid at the same rate and the budget is analysed as follows:

	£000
Basic pay	220
Overtime	0
Bonus	70
Employers' NI & pension contributions	30

The budgets for labour and supervision include provision for a pay rise of 3% which came into effect on 1 April 2001.

For costing the standard charge for each category of job, the cost of supervision, overheads and administration are recovered by an oncost rate which is applied as a percentage of the labour cost.

The R&M Team carries out tasks which fall into six job categories for which budgeted figures are:

Job	Budgeted cost per job		Budgeted volume (p.a.)	Standard charge (per job)
	Labour	Materials		
	£	£	No.	£
A	80	40	500	176
B	100	60	400	230
C	200	100	300	440
D	300	150	200	660
E	400	200	150	880
F	600	220	100	1,240

The following is an analysis of the total expenditure actually incurred on each category of job carried out during April and May 2001; the number of jobs completed is also given:

Job	Labour	Materials	Jobs completed
	£	£	No.
A	9,680	4,180	110
B	6,580	4,900	70
C	11,880	5,170	55
D	9,600	5,100	30
E	12,900	5,700	30
F	6,160	2,600	10

The following information relates to the two months, April and May 2001:

	£
Basic pay	36,660
Overtime	1,200
Bonus	13,940
Employers' NI & pension contributions	5,000
Supervision	8,340
Overheads	15,600
Administration	12,600

The quality of the work completed by the R&M Team has always been regarded as good.

The R&M Team has failed to meet its financial target in the last two years and as a result the Housing Association's Management Team is anxious to ensure that in 2001/02 the target of breaking even is achieved. The Management Team has required that the Management Accountant produce a report on the R&M Team's performance every two months with effect from June 2001 when the performance for the first two months of the financial year will be assessed.

- **Requirement for question 3**

In your role as Management Accountant of Utopia Housing Association, you are required to prepare a report for the Management Team assessing the performance of the R&M Team for the two months of April and May 2001.

25

4

You have recently taken up a post as trainee accountant at Shangri La Housing Association. The Director of Finance is also newly appointed and has made a review of the Housing Association's systems for internal financial reporting his first priority. You have received the following memo:

To: Trainee Accountant

From: Director of Finance

Subject: Internal Financial Reporting Systems

In the short time that I have been here I have realised that our financial reporting systems need some attention. I am concerned that they have not been reviewed for some years and are therefore not appropriate to the challenges we now face. Although we all understand the need to control our costs and stick to budgets, we're still not achieving this. We usually don't seem to realise we have a problem until it's too late.

I'm hoping you can give us the benefit of your current studies by outlining why this is happening and how we can address it.

- **Requirement for question 4**

Prepare a briefing note for the Director of Finance which:

(a)	identifies external factors which have made monitoring financial information more important to housing associations, and outlines the implications of each for internal reporting systems;	*9*
(b)	gives key uses of financial information within the organisation;	*4*
(c)	identifies characteristics of good information; and	*3*
(d)	addresses characteristics needed within the financial reporting system to produce effective budgetary control information, and explains briefly why each is important.	*9*
		(25)

5

Three new non-executive directors have been appointed to the board of your housing association. Your Director of Finance has asked you to represent her at their induction seminar.

In particular, you have been asked by the Director to provide a briefing paper on the following topics:

(a) The Cadbury Report. *5*

(b) Corporate Governance. *6*

(c) The application of good corporate governance within your association. *9*

(d) Basic financial information which non executive directors need to receive in order to discharge their responsibilities. *5*

- **Requirement for question 5**

Prepare a briefing paper for presentation at the induction seminar. *(25)*