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SOCIETE IMMOBILIERE PUBLIQUE (S.I.P.)

REPUBLIC OF BURUNDI

PLAN FOR THE IMPROVEMENT OF THE FINANCIAL MANAGEMENT

EXECUTIVE SUMMARY FROM THE ORIGINAL IN FRENCH

COOPERS & LYBRAND
WASHINGTON, D.C.
JULY 1984

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(Executive Summary From the Original in French)

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PLAN FOR THE IMPROVEMENT OF THE FINANCIAL MANAGEMENT OF THE SOCIETE IMMOBILIERE PUBLIQUE (S.I.P.) OF BURUNDI

PRELIMINARY OBSERVATION

The Societe Immobiliere Publique (S.I.P.) has received as a grant from the State a certain number of dwellings and has had others built. Most of the dwellings are sold to civil servants on a 15-year installment plan, the interest charges being borne by the State. The installments are withheld from the civil servants' pay and passed on to S.I.P. with delays of unpredictable length of time. Under these conditions, no proper financial management is possible.

This state of affairs has obliged S.I.P. not only to increase its borrowings to finance its construction programs but on some occasions to defer the payment of its obligations under the loans. S.I.P. should, at least, be able to measure the costs incurred in consequence and to have elements of information on which to base its decisions as to the best course of action to accomplish the company's aims at the lowest financial cost. For this purpose, S.I.P. would really need multiple cash-flow projections drawn up under various assumptions regarding the question "what if collections were delayed one, or two, or "n" months. This calls for two kinds of requirements:

- to organize the accounting in such manner as to provide more detailed information than is presently available, principally regarding amounts receivable and payable.

- to have access to adequate means of processing such information in order to assess the impact of various courses of action among which to choose, in order to restore financial equilibrium in cases of delayed collections.

Unfortunately, S.I.P. is obliged to keep its accounts in accordance with the National Accounting Plan which is designed principally to provide data for national statistics and is of very little value for corporate financial management. It will therefore be necessary to graft the management information onto the official accounting base as explained hereinafter.

The additional information needed involves too many accounts to be processed manually. The accounting should therefore be computerized and a microcomputer would probably be sufficient for that purpose. Based on our experience of similar situations, we believe the best solution would be to develop an integrated accounting and management information system and the recommendations presented in this report are formulated accordingly.

A. ACCOUNTING POLICIES APPLICABLE TO S.I.P.

S.I.P. is under the obligation to draw up its published annual financial statements in accordance with the nomenclature and classification prescribed by the National Accounting Plan. This does not preclude the preparation, for internal use, of other financial statements of greater informative value for the conduct of its affairs.

The National Accounting Plan is compatible with generally accepted accounting principles. However, for management accounting purposes, it would be desirable to adopt, in addition, the following accounting policies:

1. to set up a system of revaluation of the fixed assets (a reserve based on the revaluation of the rented buildings would set off, to some extent, the foreseeable erosion of its equity, in real terms, as a result of having sold dwellings at a fixed price payable over fifteen years).

2. to record the commitments incurred on account of construction contracts.

3. to record in the accounts: unaccrued interest income from the sales of dwellings on the installment plan and unaccrued interest charges on borrowings.

It will not be necessary to incorporate the above items in the set of official accounts - they can be introduced directly into the parallel management accounting system derived from the former by a conversion-key as explained hereinafter.

B. ACCOUNTING AND BUDGETARY CONTROL SYSTEM

The rules of internal control should be fully spelled-out in an Accounting Practice Procedures Manual, the contents of which are tentatively outlined in Section D.

If the accounting can be computerized, the budgetary control should be integrated therein. The expenses and revenues budgets should be drawn up in keeping with the nomenclature of Classes 6 and 7, respectively, of the National Accounting Plan. It will then be possible, with the Computer, to control these budgets automatically, in the manner described in Exhibit A. If the accounts cannot be computerized by the beginning of 1985, it would nevertheless be desirable to implement manually the budget control system described in Exhibit A, using the accounts specified in Exhibit B.

C. FINANCIAL MANAGEMENT SYSTEM

This should be based on a management information system integrated into the accounting system. It should comprise the following features:-

(1) Programming

The principal programs to be drawn up are the following:

(a) Construction Programs - to build new dwellings (or complete the construction of unfinished dwellings transferred to S.I.P. as grants from the State).

These programs should be based on an assessment of civil servants' lodging needs by geographical area - and of priorities.

Scheduling of execution will depend on availability of resources; these consist of:

- Collections, principally from the three following sources:

  (i) 80% of the selling price of the dwellings payable by the buyers in installments over 15 years

  (ii) the balance of 20% contributed by the State

  (iii) the interest on the buyers' outstanding balances, also payable by the State

- Such borrowings as S.I.P. can obtain from the Banks and appears able to repay.

(b) Sales Programs, which must take into account construction schedules, prices obtainable, and credit terms granted.

(c) Programs of works to be performed by S.I.P. for account of the State (sewerage, water and power lines for future construction sites). These programs should be, but have not always been, correlated with the construction programs, possibly due to the delayed reimbursements of those works by the State (the accounts at December 31, 1983 showed the outstanding balance on this account amounted to FBU 437 million, or 127% of the paid-up capital of S.I.P.).

Normally, it should be feasible to draw up cash-flow projections to determine the amount of borrowings needed to finance the construction programs. Unfortunately, the installments withheld from the Civil Servants' pay are passed on to S.I.P. with unpredictable delays and the interest due by the State, unpaid at December 31, 1983, amounted to FBU 129 million.

Under these conditions, no reliable cash-flow projection can be drawn up.

Moreover, with the accounting based on the National Plan, items which should be differentiated for cash-flow projections and other analyses are grouped under common accounts. We therefore recommend setting up a "Management Accounting System" grafted on to the "basic accounting system" modeled on the National Plan, by converting asset and liability accounts into a more meaningful nomenclature and classification for management purposes. This will help, among other things, the programming function. It will be necessary, however, to reckon with the uncertainty of the timing of collections and that should be done by drawing up sets of multiple cash-flow projections under various assumptions, which will become feasible only if the accounting is computerized.

2. <u>Budget Control of Revenues and Charges</u>

As already mentioned, budget control should be conducted as prescribed in Exhibits A and B. For it to become a valuable management tool, the following conditions will also be required:-

(a) The budget must be drawn up with the participation of the executives responsible for its execution.

(b) To facilitate control of the expenses, both the budgeted amounts and the actual charges should be subdivided in accordance with the organization units to which they are allocable. This can be done only after lines of authority and responsibility for incurring expenses have been clearly defined (which is beyond the scope of our present assignment). The variances by organization unit will be very helpful to keep expenses under proper control.

3. Mobilization of Financial Resources

This problem would be greatly simplified if the State would pay its debts to S.I.P. on time; these consist of:

- the unpaid portion (FBU 25 million) of its subscription to the Share Capital which, according to the Articles of Association, should be fully paid-up (the total unpaid subscriptions amount to FBU 55 million).

- The outstanding accounts which, as shown by Exhibit E amounted to FBU 662 million at December 31, 1983.

The total overdue amounts owed by the State, viz FBU 717 million, account for 39% of S.I.P.'s outstanding borrowings. An analysis of the operating results should show the amount of extra financial charges incurred on that account, as explained in Section D.

4. Development of a Management-Oriented Accounting System

The present accounting system modeled on the National Accounting Plan is of very little value for management purposes. Since this form of accounting may not be discarded, we recommend setting up a parallel system as explained hereinafter:

(a) First, certain amendments must be made in the nomenclature and codification of the basic accounting, not only to bring it into closer conformity with the official Plan but also to permit the conversions required for management accounting. Since it will be necessary, in order to fully develop the latter, to computerize both the basic accounting and the process of conversion into the parallel set, it is desirable to start right away with the preliminary measures. The present codification is disorderly (there are codes with 2, 3, 4, 5, and 6 digits and different sub-account codes to subdivide different accounts by the same criteria). It is necessary to correct the account codes of the basic accounting, to consist uniformly of five digits, the first three in accordance with the official plan, and the last two for sub-accounts as needed.

(b) Next, it will be necessary to adopt, for management accounting purposes, a chart with a different structure. The two structures are compared in <u>Exhibit C</u>.

(c) All third-party accounts (receivables and payables) will be maintained, in the parallel set, in Class 3, regardless of maturities. When the accounts are computarized, they will be subdivided into sub-accounts by month of maturity, thus avoiding the need for transfers from "long term" to "short term" and the risk of confusion between the two. For the preparation of accounting statements, the computer will distribute the sub-account balances between "short term" and "long term" according to the instructions given to it regarding the number of months to be considered as "short term" (not necessarily the traditional 12 month period which generally gives a distorted image of the liquidity position).

(d) The balances of the basic accounts with their codification amended as explained above will be converted by the computer into the management accounting nomenclature in accordance with the conversion-key set up in Exhibit D, which shows, for each account of the basic accounting, the present code, the amended code and title, the converted code, and the balance as at December 31, 1983. These balances, reclassified in the order of the converted codes as presented in Exhibit E, provide a preview of the presentation of the Balance Sheet for management information. Balance Sheets for internal use should in future be prepared monthly in this form, which offers a much more meaningful image of the financial condition than the Balance Sheet on the model of the National Plan. Certain peculiarities of the conversion are explained in Exhibit F.

(e) The Balance Sheet as presented in Exhibit E, however, still gives an incomplete image of the financial condition. It should be completed by incorporating the "Commitments" which can profoundly modify the liquidity position and the prospects for future operating results. Since such accounts have no place in the National Plan they will not be obtained by conversion of any "basic" account, but introduced directly into the parallel accounting in the form of Memorandum Accounts with counterbalancing debits and credits. The nomenclature of such accounts is shown in Exhibit H. They will be maintained in the following manner:

(i) Commitments incurred under Construction Contracts. (The original of the Report, in French, spells out the entries to be put through these accounts - the resulting balances will show, at any time, the unexecuted portion of construction works under contract and the corresponding payment-commitments outstanding, by estimated payment-date - less any advance payments.)

(ii) Commitments on Account of Borrowings. (The original of the Report, in French, likewise spells out the entries to be put through these accounts. The resulting balances will show, by due dates, the total amounts repayable on account of each loan, including all unaccrued interest to be paid in the future, the counterpart being included as "deferred charges.")

(iii) Control of the installments due by the buyers of dwellings. These accounts will show the amounts as yet unpaid by the buyers, to be withheld from their future paychecks.

(iv) Control of the portion of 20% of the cost of the dwellings, to be received from the State (as a subsidy to the buyers). (As explained in detail in the original, these accounts will show, at any time, for each group of dwellings, the total amount to be contributed by the State and the portions paid up and outstanding.)

(v) Control of the interest accrued and unaccrued calculated on the installments due by the buyers of dwellings and the portions paid and unpaid by the State.

(The entries required for this control are spelled out in the original.)

The commitment accounts indicated under items (i) through (v) hereinabove, will be taken into account as receipts and disbursements under their due dates in the cash-flow projections developed by the computer and the counterpart deferred charges and revenues for unaccrued interest will be incorporated in the computerized projections of operating results. These automatically-produced projections will have the advantage of completeness and accuracy due to their linkage with the double-entry financial accounting, and will be obtainable on demand, at any time, constantly updated up to the last transaction recorded.

5. Financial Statements for Internal Use

For internal use by the Management, the following statements should be prepared:

(a) Monthly Statement of Assets and Liabilities in the form of presentation shown on Exhibit J. After twelve months, besides showing the figures at the end of the previous month, the statement should show the figures at the end of the same month of the preceding year. Exhibit E, albeit with the figures incomplete, will serve to illustrate this form of presentation.

(b) Monthly Budget Control and Analysis of Operating Results

We do not consider indispensable to make changes in the nomenclature and codification of the expense and revenue accounts of Classes 6 and 7 of the National Plan.

To make the Budget Control more meaningful, as already mentioned, the charges should be allocated to the organization units and variances should be explained by the executive responsible for each unit.

In addition to the formal budget control, it would be desirable, on a routine basis, to measure the financial consequences of certain situations such as the delayed payments of accounts due by the State (The method prescribed to determine what portion of the financial charges on borrowings should be ascribed to such delays is explained in detail in the original).

The Income Statement for the year ended December 31, 1983 shows that revenues and charges, in order of importance, are as follows:

Revenues:

1. financial revenues (i.e., principally, interest payable by the State on the outstanding balances on buyers of dwellings accounts)
2. rentals
3. fees
4. miscellaneous revenues

Charges:

1. financial charges on borrowings
2. other charges (i.e., essentially, operating and administration expenses)
3. taxes.

There is no interdependence between the financial revenues from the sales of dwellings and the financial charges on borrowings, since the volume of these could be substantially reduced if the State paid its debts more promptly. As for the "fees" inputed to the cost of the dwellings, they should be considered not so much as "revenues" but rather as a recovery of expenses incurred. We therefore recommend that the Income Statement for internal use be presented in the form shown in Exhibit K (with the figures for the year 1983 by way of illustration).

One desirable improvement would be to segregate under separate sub-accounts those charges that are incurred in planning, managing, supervising and controlling the construction of new dwellings, so as to compare the cost thereof with the amounts calculated at the fixed rate of 6.5%, charged as "fees" to the costs of the dwellings built by S.I.P.

(c) Cash-flow Projections

These should become the keystone of the financial management system, their particular importance, in this case, being due to the delayed payments by the State.

As already explained, all accounts receivable and payable (including the "commitment accounts" of Class 9), should be subdivided into sub-accounts by month of due date (coded AAMM for year AA and month MM). Consequently, the (parallel) set of management information accounts contains all the potential data required to project future cash flows at least on the basis of contractual or theoretical due dates. The model form of presentation for such cash-flows is shown in Exhibit L which indicates the codes of the accounts to be included therein. These projections can be produced by the computer, on demand, to show the monthly figures separately or grouped, as desired. In practice, it will generally be sufficient to show the monthly inflows and outflows separately for the period up to the end of the subsequent fiscal year and thereafter yearly or by groups of years.

However, as long as present conditions prevail, any cash-flow projection based on theoretical dates of collection would be illusory. Consequently, it will be necessary to develop computer programs to produce cash-flow projections with the months of the movements brought forward or pushed back under various assumptions, until the most acceptable solution is found to cope with the most likely delay in the collection of the payments due by the State. This amounts, in effect, to the computerization of an operational research technique to solve the contingency confronting S.I.P.

(d) <u>Projections of Operating Results</u>

The computer can be programmed to produce, on demand, projections of future operating results, month by month, for the remainder of the current fiscal year (and for the following fiscal year as soon as the revenues and expense budgets for that year have been drawn up). These projections will include for each future month: the budgeted figures (adjusted for past months' variances, if appropriate) of the accounts of Class 8 (see Exhibit B), except the budgeted financial revenues and charges; these will be included for the deferred financial revenues and charges recorded in the accounts of Class 9 (as previously explained in Section C-4-e - paragraphs ii and v).

The projections of operating results will be produced by the computer in the same form of presentation as the actual results for past periods (model as per Exhibit K) with a separate column for each month and for the total period covered by the projection.

6. Control of Construction Costs

Costs of construction of new dwellings and cost of works carried out for the account of the State are currently recorded in appropriate accounts by program and appear to be controlled in a satisfactory manner.

However, on completion of construction of new dwellings, the costs thereof, as accumulated in work-in-progress accounts, should be transferred to a new fixed-asset account - "Completed Dwellings, for Sale" from which the costs of individual dwellings sold would be charged out to the buyers' accounts (presently the charges are made directly out of the work-in-progress accounts). For management accounting purposes, the new account could then be converted into a Memorandum Account of Class 9 of the parallel accounting system, in order to keep a record, on the one hand, of the cost of each group of dwellings of the same type and in the same location and, on the other hand, of the prices obtained for dwellings sold.

D. MEASURES TO BE CONSIDERED IN ORDER TO IMPROVE THE FINANCIAL MANAGEMENT

1. Preliminary Steps

Before leaving Bujumbura, we handed the Head of the Administration and Finance Department a Program of tasks to be performed by the Accounting Section after our departure, by way of preliminary steps to improve the accounting and pave the way for the development of improved financial management practices. These tasks are summed up hereunder:

1. the adjustment of the Bank Accounts at June 30, 1984;
2. the control and adjustment of the auxiliary-ledger accounts of individual buyers of dwellings;
3. the preparation of an age-analysis of amounts due by buyers of dwellings;
4. the preparation of a statement of future maturities for the accounts of buyers of dwellings;
5. the preparation of a cash-flow projection (for the time being, incomplete).

A copy of this Program is reproduced in Exhibit M.

2. Decision of Principle, to be taken by the Management

Before any detailed plan to improve the financial management can be drawn up, the Management of S.I.P. must, first, decide, in principle if it wishes to computerize the accounting, and if so, if that is practically feasible. The principal points bearing on this decision are as follows:

(i) Is it to be expected that a computer firm will install a branch in Bujumbura capable of providing adequate maintenance service for the appropriate equipment (presumably a microcomputer)?

(ii) What will computerization cost? Management should take into account not only the purchase cost of the hardware and software but also of installations to handle possible power failures, operating costs and supplies, and the cost of training the personnel.

(iii) What administrative measures, if any, will be called for, to computerize?

(iv) Is management fully conscious of the benefits that it could derive from a system of financial management based on a computerized accounting system such as we recommend in this Report?

Those benefits may be summed up as follows:-

- the parallel accounting system will be almost entirely derived automatically by the computer (by code conversion) from the basic accounting system maintained strictly in compliance with the requirements of the National Accounting Plan.

- The additional accounts (of Classes 8 and 9) for budget control and commitment accounting (including future interest revenues and charges) will be inserted directly into the parallel accounting system by means of simple initial entries subsequently updated automatically by the computer.

- The parallel accounting system will greatly contribute to improve the financial management, viz.

  - .. it will produce financial statements containing valuable information for the management, on which to base its decisions;

  - .. it will facilitate the control of the revenues and expenses budgets;

  - .. it will measure the financial consequences of certain untoward conditions (such as the delayed payments of amounts due by the State);

.. it will make it possible, by means of a simple adaptation of the codification, to allocate the operating expenses between functional sectors and also to control recoverable costs (such as the costs of works carried out for the State) and capital expenditures (new dwellings);

.. principally, it will be able to produce from the recorded accounting data, cash-flow projections under various assumptions regarding the delays in collections and the possible options for remedial action, which will enable the management to select the most appropriate measures to maintain a balanced treasury position at the lowest financial cost.

3. Measures Called for in Case of Computerization

If the Management decides to computerize the accounts, the following measures will be called for:-

(i) to draw up an "Accounting Practice Procedures Manual" as outlined in the tentative "Table of Contents" presented in Exhibit N;

(ii) to train the personnel of the Accounting Section in the use of the equipment, to produce the accounts and the financial statements (in accordance with the above Manual);

(iii) to train the Management and Department Heads in the use of the information obtainable from the computer, to improve the financial management.

4. <u>Limited Scope for Improvement of the Financial Management with the Present Type of Manual Accounting</u>

Theoretically, all or most of the accounting treatments recommended in this report could be implemented manually. In practice, however, that solution would be costly (it would require a substantial increase of the clerical staff) and would have little chance of success.

In the absence of computerization, therefore, S.I.P. can expect only slight improvements of detail, such as outlined in the work Program (Exhibit M). Even so, the fifth and last recommendation of that Program - i.e. the preparation of Cash-Flow Projections, would be no easy matter; and it is absolutely out-of-the-question that S.I.P., with purely manual processing, could develop the sets of multiple projections under varying assumptions, as envisaged with the computer: manually prepared projections based on theoretical due dates are illusory; and a single projection based on revised estimates of due dates may show up an unbalanced projected position but will be of little value to decide on the best option for remedial action.