

**CIPFA PROFESSIONAL EXAMINATION 3**  
**FINANCE AND MANAGEMENT CASE STUDY EXAMINATION**  
**NOVEMBER 2002**

**BILDING CORPORATION**  
**TUTORIAL GUIDE**

**1. General comments**

- (a) It is important that candidates answer all the questions as set.
- (b) Where illustrative figures or information are asked for in a question, or their use is implied in the data, then they must be shown in the candidate's answer.
- (c) Evasion of the terms of the question on the grounds that the situation depicted in the Case Study is unlikely to have arisen or occurred, or is improbable in concept, should be penalised.
- (d) Working papers submitted with answers should be scrutinised and used to test the candidate's line of argument in unfinished work and as a guide to the method by which the candidates have utilised their acquired knowledge to deal with the various aspects of the Case Study.
- (e) Detailed calculations are set out in the appropriate attached appendices. It must be emphasised that these are not 'model answer' figures but are based upon what are judged to be the 'best' assumptions made in answering the question. Candidates should not therefore be judged on whether they got the figures 'right', but on how they reached their figures and how reasonable are their assumptions and arguments.

**2. Synopsis of case**

The case is set in Constructia, an independent kingdom in North Western Europe. The case concerns the affairs of Bilding Corporation, a unitary local authority serving the needs of the ancient and historic City of Bilding. The Corporation is keen to promote urban regeneration to offset the effects of declining industries. The population is now rising, and the Corporation is keen to continue to foster economic development in the locality.

There is a strong emphasis on improving the effectiveness, quality and efficiency of public services. This requires the Corporation to provide high quality, responsive services, if necessary by innovative service delivery provision. The Corporation has recruited a new Chief Executive from a private sector background with a strong commitment to these objectives. However, some parts of the Corporation are steeped in a traditional culture of defined direct service provision, and do not see that there is any merit in introducing new customer-led approaches into the Corporation's service provision, especially those involving the introduction of market disciplines. In particular, the Estates Section of the Property Services Division has an insular culture based on providing a defined professional service based on its traditional working practices. This Section is attracting criticism from users within the Corporation, and other users of its services such as schools who now have devolved budgets and the ability to source some of the services provided by the Estates Section from alternative suppliers if they so wish.

The Corporation has met with considerable success in promoting economic development. One of the most successful initiatives has been the Bilding Technology Park, comprising mainly incubator units for new businesses. Rents for these premises are based on a “partnership” arrangement, under the terms of which much of the rent is determined as a proportion of the tenant’s gross profit. At the end of a five-year lease tenants are deemed to be established businesses and are required to vacate their incubator unit. It was envisaged that these tenants would move to other premises in Bilding on a commercial basis. However, many of these tenants are relocating outside Bilding, attracted by incentives offered by neighbouring local authorities. The largest tenant on the Technology Park is keen to remain in its existing premises as it nears the end of the lease. The Estates Section refuses to renew the lease and also the tenant considers that the terms of its current lease are now inappropriate. The new Chief Executive wishes to take a more commercial approach to the property management of the Technology Park and reach agreement with the large tenant to renew the lease on appropriate terms.

The first afternoon question concerns the Estates Section. There is considerable criticism of the Section because it is unresponsive to users’ needs, bureaucratic and slow to make decisions. Users have experienced difficulty in securing decisions and action from the Section. Staff are concerned about a lack of training, excessive overtime and uncertain career development. There is also some evidence that the Head of Section is not performing his management role in a satisfactory manner. Matters have reached the point where the problems are sufficiently serious to have attracted the attention of the Chief Executive. There are particular concerns over the Maintenance Management Team: its costs appear high, large amounts of time are spent unproductively and some primary schools are openly talking of not renewing their service level agreements next year, due to concerns over the policy for charging for its services. Related to this is some evidence that the management of the Section is unduly favourable to this Team and the other Teams resent this. At the same time, a private company has submitted a proposal to take over the work of the Section, in whole or in part. As a result the Corporate Management Team is to consider the future of the Section.

The candidate is required to prepare a report for the Director of Corporate Services that analyses and addresses these issues, beginning with an appraisal of the proposals from the private company, which initially seem attractive, but when costed on an activity basis are less advantageous. The candidate is then given an opportunity to discuss management issues relating to the Section, including the identification of any practices that lead to high costs for the Section. The remainder of the question requires an analysis of issues relating to the Maintenance Management Team: excessive unproductive time and questionable bases for recharges to primary schools and other service users.

The second afternoon question concerns a project to build a new primary school, required because of the rising population in the Livingstone district of Bilding. The school is needed by September 2004 to address criticisms of overcrowding in an inspection report by a government agency. However, there have been a number of unexpected difficulties with the site that will cause delay and increase costs. The Education Directorate is concerned that the school will not be ready in time, and will

be over budget. These concerns have been heightened by their experience of serious problems during the construction of a recently completed primary school, which was seriously delayed and 20% over budget. The Directorate argues that ineffective project management by the Property Projects Section was responsible for these problems, and is keen to avoid repetition during the construction of the new school. The candidate is asked to prepare a report assessing the quality of project management, looking at the performance of the Education Directorate as a client as well as the performance of Property Projects as project manager. This advice also includes identification of specific weaknesses in the project management of the recently completed Dampcourse Primary School identified by the chair of its Board of Governors. The candidate must make proposals for improvement to the management of the construction of the new Livingstone Primary School and allocate responsibilities for these.

The candidate is also required to assess the prospects for achieving timely completion of the new school using critical path analysis, and to advise on the optimum trade-off between saving time and incurring extra costs to achieve the deadline. Finally, the candidate must show tact and sensitivity to address proposals by the Education Directorate that the unanticipated extra costs for the new school already identified should not be charged against its budget.

The “quick response” question requires the candidate to draft a briefing note for the Chief Executive, who has to meet with the managing director of a successful business located on the Technology Park unhappy with uncertainty over the renewal of the lease for their premises. Also, the tenant is unhappy with the normal lease terms, and makes counter proposals. These must be assessed, together with the effects of creative accounting to which the tenant has resorted in an attempt to reduce the current level of the rent. The candidate has to recognise that the current arrangement is unfair and open to abuse. Also the candidate has to appraise an opportunistic offer from a commercial property company. Although providing a better financial return for the Corporation, accepting the offer would not be consistent with wider policy objectives and would generate hostile publicity.

The case material affords candidates a full opportunity to demonstrate their understanding of the case and to communicate relevant information clearly and tactfully.

### 3. Question 1

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#### *Aims*

- (a) To test candidates' understanding of the issues raised by the renegotiation of the lease on the Parfit Warehouse and the offer from a commercial developer to lease the property;
- (b) To test candidates' ability under severe time pressure to recognise and analyse the facts and figures relevant to the issues raised;
- (c) To test candidates' skill in presenting this information in a clear, concise and relevant briefing note format for the Chief Executive.

#### *Assessment*

- (a) Brief background on the terms of the Incubator Rent Scheme and whether it is appropriate for the Parfit Warehouse to be included in the scheme. (15%)
  - A brief history of the Parfit Warehouse and why it is in the scheme; (iii),12
  - A discussion of the Incubator Rent Scheme's aims to encourage economic development in specific areas and the concept of the incubator lease; (iii),2
  - A note of the rapid growth in Independent Trading's profits; 6,7
  - A recognition that Parfit Warehouse cannot reasonably be regarded as an incubator unit as it is large and suitable for only occupation by an established business; 2,12
  - A comment on the high public profile of the tenant and the likelihood that appearing to penalise the tenant is likely to be very damaging to the Corporation; 3
  - A note of the differences between the Parfit Warehouse and other units. 2,12
- (b) An identification of the options for Parfit Warehouse rental payments and the calculation of the rents payable under each option. (25%)
  - Computation of current rental payable for 2002/2003 using gross profit for 2001 originally reported by Independent Trading App A
  - Computation of rental payable for 2002/2003 on the current basis using restated gross profit for 2001 as reported by Independent Trading; App A
  - Comparison of these rentals and identification of the effect of the restatement of gross profit; App A
  - Computation of rental payable for 2003/2004 using tenant's projected gross profit for 2002 under existing rental terms; App A
  - Computation of rental payable for 2003/2004 on partnership basis proposed by Independent Trading; App A
  - Comparison of these estimated rentals for 2003/2004 with the fixed rental proposed by Independent Trading. App A
  - Computation of rental payable for 2004/2005 using tenant's projected gross profit for 2003 under existing rental terms; App A
  - Computation of rental payable for 2004/2005 on the partnership basis proposed by Independent Trading; App A
  - A comparison of these estimated rentals for 2004/2005 with the fixed rental proposed by Independent Trading. App A

**NOTE** For suggested calculations see Appendix A, but note comments in 1(e) above.

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(c) Assessment of the letting options for the Parfit Warehouse. (25%)	
• A note that the current rental payment for 2002/2003 is above the estimated commercial rent for the Parfit Warehouse and is thus too high and inconsistent with the objective to provide cheap commercial properties to promote economic growth;	2,12
• A comment that the tenant's restated gross profit has been unfairly depressed by the inclusion of expenses within cost of sales more properly classifiable as overheads;	7
• A comment that this probably reflects an attempt by the tenant to manipulate the rental calculation to reduce the currently excessive level of rent;	7, App A
• A discussion of the risk that Independent Trading may follow other tenants and relocate away from Bilding at the end of the current lease;	6
• A note that economic development also involves retaining tenants;	2
• Calculation of the annual value to the Corporation of transferring the property to Ratchett and Fleecem;	Q1, App A
• A comment that Ratchett and Fleecem are likely to seek to charge tenants high rents to recover the cost of the high rental offered to the Corporation, their other operating costs and their profit margin;	
• A note that this is likely to affect economic development and would result in adverse publicity for the Corporation given the high media profile of Independent Trading;	3
• An explanation that although the Ratchett and Fleecem option provides the best financial return it should therefore be rejected on wider policy grounds;	
• A comment that the Parfit Warehouse is too large to be classified as an incubator unit;	12
• A comment that the most sensible option is to allow Independent Trading to retain occupation of the Parfit Warehouse;	
• A statement that the Independent Trading proposals result in a rent below commercial levels which fails to recognise the depreciation element of the Corporation's costs;	12, App A
• A note that the new lease should be based on a current commercial rental of £70,000;	2, 12
• A conclusion that alternative partnership bases result either in an unrealistically low or high rental and involve subjectivity and administrative complexity;	App A
• A comment that a rebate of rent for 2002/2003 based on apparently unsound accounting data would not be appropriate and should be resisted, as there is no obligation to give a retrospective rebate.	12

**NOTE** For suggested calculations see Appendix A, but note comments in 1(e) above.

(d) Evaluation of the "partnership" basis of the Incubator Rents Scheme, discussion of wider policy implications and determination of recommended basis for the Scheme. (20%)	
• A note that the current practice of basing rent on gross profit can be abused as there is no definition of cost of sales so tenants can define this as they wish;	12
• A comment that there is no attempt to reconcile gross profit notified by tenants from their management accounts with reported audited results;	12
• A note that most tenants no longer have audited accounts anyway, making it impossible to verify reported gross profit;	12
• A discussion of wider policy issues, recognising that economic development also involves retaining tenants;	2,12
• A statement that occupancy levels of incubator units are dropping and that whilst there is a surplus of incubator units it would be sensible to allow existing tenants to renew their leases to avoid them moving away from Bilding;	2
• A conclusion that the current Incubator Rent Scheme is subjective and open to abuse and that specifying a discount against an equivalent market rent for incubator units is fairer, more transparent and less administratively complex.	
(e) Presentation, format, tact and general readability. (15%)	

## 4. Question 2

### *Aims*

Page

- (a) To test candidates' ability to locate, analyse and process financial and related data in the context of a report covering several areas of concern regarding the operation of a service function in a large local authority;
- (b) To test their ability to establish the financial effects of outsourcing options, taking account of costs that will remain with the authority;
- (c) To test their ability to identify poor management practices resulting in unnecessarily high costs;
- (d) To test the candidates' ability to analyse costs and relate these to activities, and to formulate recommendations for improvements to the charging bases used by the Maintenance Management Team;
- (e) To test the candidates' ability to analyse time spent on different types of primary school and to formulate recommendations for improvements to the basis of charging primary schools;
- (f) To test candidates' competence in drafting and presenting a report for the Director of Corporate Services.

### *Assessment*

- (a) Introduction and background to the outsourcing proposal. (25%)
  - Background information about PSI and the agenda of the Corporation reflected in the appointment of the new Chief Executive, noting:
    - background information about the Estates Section; (i)
    - the proposal from Ken Tract Limited offering to take over the services; (iv)
    - identification of options; 10
    - that all costings are at current price levels and the proposal by Ken Tract for future increases in contract price; 10
    - a summary of the main terms of the proposal. 10
  - An analysis of the net cost/saving to the Corporation from the proposal to outsource the whole Section, taking account of the costs that will continue to be incurred by the Corporation; App B1
  - An analysis of the net cost/savings from the outsourcing of individual Teams, taking account of the costs that will continue to be incurred by the Corporation; App B2
  - A summary of the analysis with a comment that a decision on the future of the Section will not be made solely on financial grounds. 16

**NOTE** For suggested calculations see Appendix B, but note comments in 1(e) above.

- (b) Identification of poor management practices and practices that result in costs being unnecessarily high. (25%)
  - A comment that the culture of the Section is bureaucratic and that this has affected morale adversely; (iv)
  - A note that management communication is poor; 5
  - A note that excessive overtime has led to high levels of stress; (iv)
  - A comment that staff requests to be paid overtime instead of taking time in lieu are being refused, indicating a lack of appreciation of staff motivation and contributing to low morale; (iv),5
  - A note that decisions are not being made in time to meet the needs of users; (iv)
  - A comment that the Section is not responding to changing circumstances; (iv)

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<ul style="list-style-type: none"> <li>• A note that little training is taking place, apparently because of inaction by the Head of Section and this is leading to reduced operational effectiveness and lower morale;</li> </ul>	5,8
<ul style="list-style-type: none"> <li>• A comment that the Section's performance endangers retention of PPIP status for the whole Division;</li> </ul>	(iv),8
<ul style="list-style-type: none"> <li>• A note that gradings appear to be out of step with the nature of the work undertaken, leading to discontent amongst staff whose job opportunities are restricted;</li> </ul>	(v),5
<ul style="list-style-type: none"> <li>• A comment that Teams appear to be treated inequitably by the Head of Section, who appears to favour the Maintenance Management Team;</li> </ul>	5
<ul style="list-style-type: none"> <li>• A note of possible abuse of 'training' by Maintenance Management Team in respect of 'away-days' playing golf;</li> </ul>	5,8,26
<ul style="list-style-type: none"> <li>• An analysis of the time records for the Maintenance Management Team, pointing out any areas where their utilisation of time may be a cause for concern: <ul style="list-style-type: none"> <li>◦ average productive time achieved is only <math>\frac{3}{4}</math> of what is possible;</li> </ul> </li> </ul>	App B3
<ul style="list-style-type: none"> <li> <ul style="list-style-type: none"> <li>◦ sickness is well above average, over <math>2\frac{1}{2}</math> times average for Corporation and over 3 times as high as target;</li> </ul> </li> </ul>	(v),App B3
<ul style="list-style-type: none"> <li> <ul style="list-style-type: none"> <li>◦ all staff have had two weeks training, which apparently consists of playing golf;</li> </ul> </li> </ul>	5,8,26
<ul style="list-style-type: none"> <li> <ul style="list-style-type: none"> <li>◦ the large amount of time allocated to 'other' (over four weeks per team member) is not explained and in total is equivalent to over one third of a full time member of staff;</li> </ul> </li> </ul>	26,AppB3
<ul style="list-style-type: none"> <li> <ul style="list-style-type: none"> <li>◦ the Maintenance Management Team (MMT) appears to have no overtime and it might be possible to reduce the overtime for other Teams by redeploying non-productive MMT time to activities carried out by other Teams.</li> </ul> </li> </ul>	5,26
<b>NOTE</b>	For suggested calculations see Appendix B, but note comments in 1(e) above.
(c) An analysis of the rates used for recharging the costs of the Maintenance Management Team to users of their services and a recommendation as to whether the rates should be changed (20%)	
<ul style="list-style-type: none"> <li>• A note that concern has been expressed over charges for Social Services' residential homes, difference in cost between the Corporation's homes and those in the private sector and the pressure to close Corporation homes;</li> </ul>	15
<ul style="list-style-type: none"> <li>• A comment that recharges need to be accurate to allow the Corporation to make decisions on the future provision of services;</li> </ul>	25
<ul style="list-style-type: none"> <li>• An explanation of the current basis of recharges;</li> </ul>	App B4
<ul style="list-style-type: none"> <li>• Analysis of recharges to different types of building, commenting on differences between costs and recharges;</li> </ul>	App B4
<ul style="list-style-type: none"> <li>• A note of the effect on Social Services;</li> </ul>	App B4
<ul style="list-style-type: none"> <li>• A comment that these findings suggest that the recharges should be reviewed, but that further analysis in the following section of the report is also relevant and will have a bearing on any recommendations.</li> </ul>	
<b>NOTE</b>	For suggested calculations see Appendix B, but note comments in 1(e) above.
(d) An analysis of the costs of maintenance management of primary schools, consideration of charging policy and a recommendation as to any changes that should be made. (15%)	
<ul style="list-style-type: none"> <li>• A comment on the background to school service level agreement and issues surrounding amounts delegated compared to amounts charged, noting the growing competition from the private sector;</li> </ul>	(iii),(iv),20
<ul style="list-style-type: none"> <li>• A note that all primary schools are charged the same and a comment that the Corporation has discretion to choose the most suitable method of calculating charges;</li> </ul>	(iii),20,25

- An analysis of time spent on primary schools, noting that the sample is too small for a statistical analysis, but that the amount of time spent seems to vary primarily according to the age of the school;
  - An illustration of the potential differences in costs;
  - A comment about how this analysis links with the previous section, noting that the primary school evidence suggests wide variations between different properties of the same type;
  - A recommendation that the basis of charging for the costs of the Maintenance Management Team should be subjected to a more detailed review;
  - A recommendation that the review should consider factors other than just the use made of property, including size, age and method of construction;
  - A note that charges could be based on actual hours spent on each property, but that this might not be appropriate, particularly for school SLA's and for other users needing some certainty about what their costs will be at the start of the financial year;
  - A comment that a phased transition to a new charging basis may be more acceptable to some users, but that this needs to be balanced against the effect of delaying revised charges for those types of property that are currently overcharged:
- primary schools might go to a private sector provider;
  - Social Services residential homes might be closed, although the amounts involved are relatively small and unlikely to have a material effect on any decision of the future of these establishments.

App B5

App B5

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**NOTE** For suggested calculations see Appendix B, but note comments in 1(e) above.

(e) Presentation, approach, structure and report format. (15%)



## 5. Question 3

### *Aims*

### **Page**

- (a) To test candidates' ability to plan and cost a significant capital investment project;
- (b) To test their ability to apply appropriate project management techniques to optimise the trade-off between time and cost and accommodate the effects of unexpected difficulties;
- (c) To test their ability to identify deficiencies in project management procedures and provide advice on how to overcome them;
- (d) To test their ability to communicate sensitively with the Corporate Management Team to secure commitment to improved procedures and corrective action needed on the Livingstone Primary School project, gain acceptance of the need for change in the practices of both Property Projects and the Education Directorate and maintain the integrity of financial reporting.

### *Assessment*

- (a) Brief background to the Livingstone Primary School project and updating of construction costs in the light of new information. (15%)
  - Brief introduction to the need for the new school and explanation of the constraints in terms of time and budget that apply to the project; (ii),22,28
  - Recognition of the unexpected and unusual problems that have arisen and inclusion of the impact of extra site preparation costs due to the unusual and environmentally sensitive nature of the site of the new school; 11,19,22
  - Modification of the cost elements for construction elements of the project in the light of recommendations from the CLIPS Board; 4, App C1
  - Inclusion of contingencies and project management costs previously omitted. 22,23

**NOTE** For suggested calculations see Appendix C, but note comments in 1(e) above.

- (b) Preparation of a Critical Path Analysis for all activities within the construction of the new school and ascertainment of the total cost of the school construction project and the projected completion date. (25%)
  - Prepare the Critical Path Analysis network diagram; App C1
  - Show the activities and their durations; App C1
  - Analyse the network to show the Earliest Start and Latest Finish Times; App C1
  - Highlight the activities on the critical path; App C1
  - Calculate the overall cost and timescale using normal methods. App C1

**NOTE** For suggested calculations see Appendix C, but note comments in 1(e) above.

- (c) Use the network analysis to identify the cheapest way to complete the project within the required deadline with selective use of accelerated methods. (15%)
  - Compare for each activity the difference in duration and cost using accelerated (crash) methods; App C2
  - Rank activities in terms of the cost per week of time saving; App C2
  - Update the network analysis to reflect the time saved and cost incurred by using crash methods to expedite critical activities with the lowest cost per week saved; App C2
  - Recognise that the critical path changes and that different activities become critical; App C2
  - Iterate until the overall project timescale falls within the constraining deadline; App C2
  - Calculate the revised overall cost for the project. App C2

**NOTE** For suggested calculations see Appendix C, but note comments in 1(e) above.

	Page
(d) Identification of the key elements of effective project management, discussion of the deficiencies evident on the Dampcourse and Livingstone Primary School construction projects, recommendations to overcome these and consideration of proposals by the Directorate of Education to overcome a funding shortfall. (30%)	
<ul style="list-style-type: none"> <li>• An identification of the key elements of effective project management and the detailed steps required within each element;</li> </ul>	App C3
<ul style="list-style-type: none"> <li>• An analysis of weaknesses encountered in the project management of Dampcourse Primary School at each stage of project management;</li> </ul>	13,14,App C3
<ul style="list-style-type: none"> <li>• A statement of practical recommendations to overcome these weaknesses on the Livingstone Primary School project;</li> </ul>	App C3
<ul style="list-style-type: none"> <li>• An identification of responsibility for these weaknesses;</li> </ul>	App C3
<ul style="list-style-type: none"> <li>• A recognition that rectification of the Livingstone Primary School specification and design are required urgently in the light of the deficiencies of the Dampcourse Primary School before the project progresses further;</li> </ul>	
<ul style="list-style-type: none"> <li>• A recognition that the Livingstone School project will cost slightly in excess of the available capital budget;</li> </ul>	App C3
<ul style="list-style-type: none"> <li>• A statement that all costs of the project must be attributed to it to maintain the integrity of financial reporting by objective;</li> </ul>	
<ul style="list-style-type: none"> <li>• A comment that the contingency cannot be reduced because some unexpected problems have already been encountered and indeed the contingency must be applied to all the activities on the project, especially as there may be currently unquantifiable cost implications as a result of rectifying deficiencies in the new school's design;</li> </ul>	22,30
<ul style="list-style-type: none"> <li>• A comment that good project management is likely to minimise costs;</li> </ul>	
<ul style="list-style-type: none"> <li>• A note that it may be possible to vire unused capital budget from elsewhere, but that such virement cannot extend to ring-fenced funding that must be used for specified objectives;</li> </ul>	
<ul style="list-style-type: none"> <li>• A comment that it is not ethical to understate the cost of constructing Livingstone Primary School in the interests of funding rectification work at Dampcourse Primary School.</li> </ul>	30

**NOTE** For suggested calculations see Appendix C, but note comments in 1(e) above.

(e) Presentation, format, approach, report style and general readability. (15%)