CA Final SPOM Set B – Strategic Cost & Performance Management
ICAI Module Questions Compilation

Chapter 10 - STRATEGIC PERFORMANCE MEASURES IN THE NOT-FOR PROFIT ORGANIZATION

TEST YOUR KNOWLEDGE

Question 1

West Coast community operates Homelessness Services (HS) on a not-for-profit basis as a local solution to local housing needs. The primary objective is to meet the accommodation needs of persons within its locality targeting those living in the low/middle income groups and senior citizens. Accommodation is basically furnished; it consists of a small house, with kitchen, bathroom, bedroom/(s), and a sitting room. HS manages 450 such houses across various localities. Exclusive Services (ES) is a profit-seeking organisation which provides rented accommodation to the public. ES manages 200 such houses across localities similar to HS' operations.

Income and Expenditure accounts for the year ended 31st March 2021 were as follows:

	HS (₹)	ES (₹)
Rent Received	1,02,98,600	1,09,98,000
Less:		
Employee Costs	24,00,000	38,00,000
Planned Maintenance and Substantial Repairs	34,19,500	10,41,000
Running Repairs	23,91,600	6,38,000
Miscellaneous Operating Costs	15,27,500	11,75,000
Insurance, Property Taxes, and Interest etc.	13,15,500	18,75,000
Operating (Deficit)/ Surplus	(7,55,500)	24,69,000

Operating Information in respect of the year ended 31st March 2021 was as follows: House and rental information:

Size of House	Number of Houses		Rent per Week (₹)	
	HS	ES	HS	ES
1 Bedroom +	40	20	400	750
2 Bedrooms +	80	40	450	800
3 Bedrooms +	250	140	500	1,175
4 Bedrooms +	80	Nil	700	N.A.

HS had certain houses that were unoccupied during part of the year. The rents lost as a consequence of unoccupied properties amounted to ₹18,17,400. ES did not have any unoccupied houses at any time during the year.

Employees were paid as follows:

Number of Staff	Salary per Staff Member (₹) per annum

HS	ES	HS	ES
1	2	3,00,000	5,00,000
2	2	2,50,000	3,00,000
4	11	2,00,000	2,00,000
8	-	1,00,000	-

Planned maintenance and substantial repairs undertaken:

Nature of Work	Number of Houses		Cost per House (₹)	
	HS	ES	HS	ES
Miscellaneous Building Work	10	-	12,500	-
Sanitary Fittings (Kitchen+Bathroom) [all are same size]	45	5	26,100	52,200
AC Upgrades/ Replacements	8	-	15,000	-
Replacement of Wooden Structure for 3-Bedroomed Houses	50	13	40,000	60,000

Running Repairs Information:

Classification of Repair	Number of Repair Undertaken		Total Cost (₹)
	HS	ES	HS
Emergency	480	160	6,72,000
Urgent	990	376	11,28,000
Non-urgent	560	102	5,91,600

Required

(i) Critically Evaluate how the management of Homelessness Services could measure the 'Value for Money' of its service provision during the year ended 31 March 2021.

(ii) Identify, 2 performance measures in relation to Flexibility and Service Quality (dimensions of performance measurement).

(iii) Analyse, 3 performance measures relating to 'Cost and Efficiency' that could be utilised by the management of Homelessness Services when comparing its operating performance against that achieved by Exclusive Services.

Solution

(i) For commercial enterprises, generating profits is a very important objective. Likewise, not-for-profit enterprises have certain cultural, social or educational objectives for which they are created. Regardless of the type of organization, it is important to know whether the internal operations meet certain performance benchmarks, that will ensure that the organization achieves its objectives in a better manner. Moreover, even if the organization does not operate for profits, it is important for it to be "cost effective". Resources (including money) should be used optimally to achieve intended outcomes. For example, HS can use this benchmarking tool to look into the following questions:

(a) Does the organization function in an efficient and cost-effective manner?

(b) Does the estate management make best use of the buildings to achieve the objectives of the organization?

(c) Does the estate management function manage upkeep of buildings in terms of repairs and improvements in an effective manner?

(d) Are the tenants satisfied with the service provided by the estate management and the suitability of the accommodation for their needs?

"Value for Money (VFM)" is an assessment made based on the criteria of economy, efficiency and effectiveness.

Economy involves minimising resource consumption while meeting specified requirements of quality and quantity. Minimize the cost of resources / required inputs (implies to spend less) while ensuring that the desired quality of service is achieved. For HS, inputs could be purchases made for maintenance and repair work like sanitary fittings, AC, wooden structure for the houses etc., while resources could be the labour employed to carry out these services. HS should aim at purchasing required quality of inputs at the least possible price. Skilled labour needed for this job should be procured at the lowest pay scale possible. Procuring these at lower cost leads to savings for HS. At the same time, HS should ensure that cost cutting / saving does not come at the cost of quality. Lower quality implies inferior service levels, which ultimately will compromise HS' social commitment to provide quality housing to needy members of its community.

Efficiency involves maximising the ratio between resources (input) and the output of goods, services or other results.
The focus of efficiency is on the process of rendering service. The objective of efficient operations is to maximize output using minimum resources. Improved productivity means that resources procured are used in an optimal way (implies spending well).
In the case of HS, one of the resources is the labour employed for repair and maintenance work. Efficiency (productivity) measured would be the relationship between the employees available and the repair work performed by them. If the pool of employees does more repair work than the benchmark set, productivity is higher. This also closely ties up with economy (cost) of operations. If the given pool of employees (resources), who are paid optimum salary (cost), cater to more repair and maintenance work, economy of operations is achieved due to higher productivity of operations. In case these activities are outsourced, efficiency and economy can be achieved by calling for tenders. Select the tender that provides maximum work for least cost.
In addition, HS may explore options for efficiencies from business process improvements, shared services as well as further efficiencies within assets management.

Effectiveness involves ensuring that the outcome achieves the desired policy aims and objectives. Have the objectives been achieved, how does the impact of the actual output / service compare with its intended impact? (Implies to spend money wisely to achieve desired objectives). In the case of HS, effectiveness could be assessed based on the following questions.

(a) Are the housing needs of the targeted community members met?
(b) Are the tenants satisfied with the accommodation?
(c) Given its social cause, are the staff friendly, courteous and hospitable to the customers?
(d) Do the housing accommodations comply with safety standards and other legal requirements?

Each measure is inter linked with the other. For example, HS has replaced sanitary fittings in the kitchen and bathroom in 45 houses for ₹26,100 each, costing a total of ₹11,74,500. Compared to ES that has spent ₹52,200 on each house for sanitary fitting replacement. For the cost of ₹11,74,500 ES could have replaced fittings in only 22 houses (₹11,74,500 / 52,000) as compared to HS' ability to replace fittings in 45 houses. Therefore, HS' decision has been economical, getting more work done for same cost. At the same time, this does not indicate whether the fittings replaced by HS are of similar or better quality as compared to ES. ES could have used better quality fittings that last longer, enhance customer experience, safety etc. The spending by ES could have been more effective than HS because it helps

achieve the desired objective of customer satisfaction, safety and less running cost for maintenance. Therefore, to achieve economy, HS may have compromised on effectiveness.

Benchmarking is a good method of measuring performance it enables a comparison of the process, costs etc. with those of a close competitor. Services will be expected to use benchmarking information to learn from best practice, change procedures and processes to achieve enhanced methods of working, and reduce unnecessary expenditure.

However, benchmarking of performance against ES is not ideal. The performance of HS can be better measured by adopting benchmarking against similar charities whose primary objective is the provision of accommodation to the communities in which they operate.

Thus, HS must have permanent membership of the House Benchmarking Organisations, which helps social housing property-owners to compare the costs of service delivery, resources, and key performance indicators across all areas of the business. For example, the management of HS can enquire about a norm in respect of the repair charges, sanitary charges or wood structure replacement charges etc. of similar non-profit seeking organisations.

Further, benchmarking should be conducted annually to analyse all areas of the business and is used to identify high performing, low-cost services. Using the annual benchmarking exercise results, the HS can plan to target those areas that are low performing and high cost.

Overall, HS should have strong commitment to value for money, which needs to be reflected in the business plan and in service-delivery plans. By applying these principles HS would be able to achieve the optimum utilisation of resources, which will in turn lead to extra capacity and allow HS to provide better services.

(ii) The Building Block Model proposed by Fitzgerald and Moon, gives six dimensions of performance measurement including service quality and flexibility.

Service Quality- Service quality is the measurement of how well a delivered service conforms to the customer's expectations. As a not for profit organization, HS provides housing services to cater to the needs of lower and middle income groups as well as senior citizens in the local community. Although service is provided at a concessional rate compared to its commercial peer ES, quality of HS' service needs to be judged based on certain parameters that were promised by the organization to its tenants. These could be used as parameters to assess service quality. Some of them could be:

- Behaviour, attitude, proactivity of staff employed by HS.
- Quality of basic amenities provided.
- Availability of on-site service for the residents
- Safety within and around the residential unit

Data for assessment of quality can be collected from feedback of tenants, analysing the number and nature of complaints made by tenants, tenant retention rate/loyalty etc. Feedback form tenants can be taken on specific issues or could be general in nature.

Flexibility- Flexibility is the ability of the organization to adapt to customers' requirements. This can be measured through service delivery time, promptness in responding to customer requests, ability of employees to perform different kinds of work etc. In the case of HS, the following performance measures can be used to assess the flexibility:

- The average waiting time for a tenant for a house to become available. Lower the wait time better the flexibility as it indicates that there are sufficient housing units available for rental accommodation.
- Following change in requirements, ability to meet the tenant's request for another house of a different size. This indicates whether the range of housing units offered is sufficient (flexible) to cater to the tenants' changing demand.
- Waiting time for undertaking repairs of an emergency nature, once notified by a tenant. Lower the waiting time during emergencies indicates the availability of appropriate personnel to carry of the repairs on short notice.s

(iii) The management of HS could use the following performance measures –

An organization should aim at achieving results with maximum efficiency at the least possible cost. Efficiency measures the relationship between the input resources utilized and the output service achieved. Few of the measures that HS could use to compare performance with ES are:

The Average Employee Cost per week per house

Here, the resource (input) are the employees, which is 15 in case of both HS and ES.
The employees at HS cater to 450 houses as compared to 200 houses catered by ES. Therefore, HS is more efficient as compared to ES.

Likewise, cost of resources to HS is the employee cost, for which the pay structure and remuneration policies are different in both the organizations. HS has the ability to hire most of its resources at an annual salary of ₹1,00,000, which is the least level in the pay structure. Comparatively, ES also hires cheaper labour but at a slightly higher pay level of ₹2,00,000 annual salary. Therefore, the total cost of labour is higher by ₹14,00,000 (58%) for ES as compared to HS.
To compare the figures on a common factor, the employee cost can be calculated per week per house.

	HS	ES
The Average Employee Cost per week per house [₹24,00,000^/ (450@ × 52)] and [₹38,00,000^/ (200@ × 52)] ^ Employee cost from the income and expenditure table @ Number of houses (given): HS = 450; ES = 200	₹102.56	₹365.38

The average employee cost per week per house of ES is ₹365.38 (2.46 times) more than of HS. It can be concluded that HS is both efficient, in terms of being able to cater more houses with same number of employees, as well as cost effective due to the use of cheaper labour.

The Average Day to Day Repair Cost per week per house

Here, the resource (input) is measured in terms of the cost spent on repairs to maintain the rental houses. Running repairs are generally do not add much value to the rental houses. Therefore, lesser the repairs, higher the efficiency. From the income and expenditure table, it can be seen that HS has spent ₹23,91,600 as running repair cost for 450 houses versus ES that has spent ₹6,38,000 for 200 houses. To compare them on a common factor, the average repair cost per week per house has been calculated.

	HS	ES
The Average Day-to-Day Repair Cost per week per house [₹23,91,600^/ (450@ × 52)] and [₹6,38,000^/ (200@ × 52)] ^ Running repair cost from the income and expenditure table @ Number of houses (given): HS = 450; ES = 200	₹102.21	₹61.35

The average day to day repair cost per week per house for ES is ₹40.86 less than that of HS (-40%). This may be due to the fewer repairs required and the fact that there is no extra cost required for emergency and urgent repairs. The cost of repairs whether emergency, urgent or non-urgent to ES is the same, ₹1,000 [₹6,38,000/ (160 + 376 + 102)] whereas the cost of emergency repairs to HS is ₹1,400 (₹6,72,000/480), urgent ₹1,139 (₹11,28,000/990) and for non-urgent repairs it is ₹1,056 (₹5,91,600/560).

ES's low cost of repairs (which is identical for all types of repairs – emergency, urgent and non-urgent) may have been achieved through entering into a contractual agreement for repairs. HS should also think of entering into such contracts in order to save money.

Percentage of Rent Lost

Occupancy of rental houses indicate whether the capacity (in terms of houses rented) is being optimally utilized. Lesser the vacancy better the efficiency in terms of capacity utilization. This represents opportunity cost of not letting out the property.

	HS	ES
Percentage of Rent Lost (= Rent Lost / Gross Rent) [(₹18,17,400/ ₹1,21,16,000] Gross Rent = Rent Earned + Rent Lost = ₹1,02,98,600 + ₹ 18,17,400 = ₹1,21,16,000	15%	---

ES did not have any unoccupied properties at any time during the year; it has 100% occupancy. This shows that ES's properties are in high demand. On the other hand, HS has lost rent worth ₹18,17,400 through unoccupied properties; this is about 15% of the gross rent receivable.

The management of HS should identify the reasons why the houses remained unoccupied when the occupancy rate is 100% for an organisation like ES, a peer organisation should be used to benchmark the performance.