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CHAPTER 2. COMPUTERIZED AND MANUAL FINANCIAL ACCOUNTING  
SYSTEMS

2-1. INTRODUCTION

This chapter presents the HUD approach to defining financial accounting systems to track, monitor and report on cooperative housing corporation operations. Whether the system is manual or automated, the system must provide the information necessary to accomplish all the HUD accounting objectives for cooperative corporations.

This approach is comprised of the following steps:

- o Define functional requirements and document the required forms and report formats
- o Define HUD accounting requirements
- o Determine whether a manual or automated system will be implemented
- o Identify conversion requirements
- o Identify system implementation plan
- o Define internal controls

2-2. DEFINE FUNCTIONAL REQUIREMENTS

The purpose of this step is to produce a list of prioritized requirements that accurately describes the needs of the system users. In this case, the users are the cooperative board of directors, management staff and other employees who will prepare the monthly and annual reports to HUD for multifamily housing programs. The first step is to identify the processes that will be supported by the system and define the information requirements of each process. This involves reviewing the forms and reports required by HUD. The functional requirements of a typical cooperative corporation financial accounting system include:

- o Provide the board of directors, management staff and other employees with a system to record financial transactions related to daily cooperative corporation operations
- o Provide status information related to the current financial position of the corporation

- o Support the board of director's and HUD's specific reporting requirements using HUD reporting guidelines

- o Maintain an accurate and complete audit trail of the financial transactions entered into the system
- o Provide checks and balances to ensure data integrity and accuracy
- o Provide a means to produce annual reports to HUD including: Annual Operating Budget (Form HUD-92547), Statement of Position, Statement of Income (Form HUD-92410), Statement of Retained Earnings, and Statement of Cash Flows
- o Provide system controls that will protect cooperative housing corporation assets by notifying users of data discrepancies such as accounts out of balance or excessive increase in expenses

2-3. HUD ACCOUNTING REQUIREMENTS

A. BOOKS OF ORIGINAL ENTRY

Regardless of the type of financial accounting system used, books of original entry must be maintained. They may be maintained in manual logs or automated files. The books must be designed to conform with the Uniform System of Accounts and must be kept current at all times. The manual journals or automated files that need to be maintained include:

1. The Journal of Monthly Charges establishes the revenue to be expected, and the Cash Receipts Journal indicates whether it has been received. When posted to the General Ledger, this will produce the Accounts Receivable listing. Income which was not anticipated in making up the Journal of Monthly Charges will be shown on the Cash Receipts Journal.
2. The Accounts Payable Journal provides the data for the budgeted and actual expense analysis to determine whether the cooperative is running over or under its budget on specific items.

3. The Cash Disbursements Journal and the Cash Receipts Journal are used for recording all cash transactions, including checks. The journals are also used to record the changes in the Certificates of Initial Capital Value and Surplus Accounts when a membership is repurchased by the cooperative and resold.
4. The Journal of Standard Monthly Entries is used to record monthly recurring expenses. An example is the recording of

a 36-month insurance premium. The initial purchase is charged to its respective prepaid insurance account. Each month, 1/36th of the total amount is brought into the books by way of the Journal of Standard Monthly Entries, charging the corresponding expense account which will reflect the monthly cost and crediting the prepaid account which will reduce the balance and reflect the amount that has expired. A proportionate amount should be funded each month and charged to the prepaid account so the cash will be available when the next policy premium comes due.

5. Other Books of Original Entry The cooperative may also maintain other books of original entry such as the Payroll Ledger or Member Receivable Ledger to facilitate record keeping and the preparation of the financial statements and other reports required by HUD. Each cooperative should maintain adequate books to support its operational needs.

- B. THE GENERAL LEDGER (i.e., the collection of all the asset, liability, owner's equity, revenue and expense accounts) and SUBSIDIARY LEDGERS (i.e., ledgers that relate to a specific general ledger account) must be updated on a regular basis and a trial balance taken as soon as possible after the close of each month's business.

Also, the books of account and cash reconciliations must be available at all times to the board of directors, the mortgagee, and the Department of Housing and Urban Development.

- C. MONTHLY PRORATING

Although income is budgeted and assessed on an annual basis, it is received on a monthly basis. Many of the expenses will be sustained

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on a monthly basis, but others, such as utilities, may vary with the season. To make financial statements realistic, an accrual system should be used to prorate the deferred and prepaid expenses to their respective months.

- D. FORMS

All HUD forms used to report financial activity for cooperative corporations are coded to the Chart of Accounts. The following HUD forms are used by cooperative corporations,

- o Form HUD-92547A is the annual operating budget with comparative data for the preceding year. It contains the revenue and expense projections for the current fiscal

year. This form is used by all cooperative projects when submitting their annual budgets. See Appendix 1 for a sample of Form HUD-92547A.

- o The former Form HUD-93211 was the Monthly Report of Cooperative Housing Corporations. Its purpose was to compare the actual revenue and expense of month to month operations with those projected in the current annual budget. Although no longer required to be used by HUD, cooperatives that have copies of the form on hand may find the information it presented to be useful and may use it or a similar format at their sole option.

E. FINANCIAL STATEMENTS AND ACCESS TO BOOKS

This Handbook contains the sample format for formal financial statements which are required to be submitted to HUD at the end of each fiscal year.

Cooperative housing corporation financial statements and supporting information must be made available at all times to the cooperative's board of directors and to the HUD staff and HUD designees when necessary.

2-4. MANUAL VS. AUTOMATED SYSTEMS

After the list of accounting requirements has been documented and agreed upon, an assessment of the feasibility of implementing an automated system

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will be made by the cooperative board of directors. A manual financial accounting system may satisfy the needs of small cooperatives that have simple accounting functions. Transactions may be recorded in manual accounting ledgers and reports can be completed using HUD provided forms and report guidelines.

However, large cooperative corporations with complex recordkeeping requirements may want to consider an automated financial accounting system. The system may be a commercial software package or simply a PC-based spreadsheet. An analysis of the alternatives will be conducted and the board of directors will determine the most appropriate method of maintaining the accounts.

2-5. CASH VS. ACCRUAL BASIS ACCOUNTING

A. CASH BASIS

A cash basis accounting system identifies receivables and payables at the time cash is received or when cash is paid out.

An accrual basis accounting system recognizes the entire amount of a receivable or payable when the financial transaction takes place rather than when the cash is received or paid out. A cash basis system is not acceptable for HUD's purposes.

B. ACCRUAL BASIS

The accrual basis accounting method presents a more accurate picture of the financial state of a cooperative corporation and is the recommended method for bookkeeping for cooperatives. Accrual basis accounting takes into consideration amounts payable for a future accounting period and, similarly, recognizes amounts expected to be received before the amounts are actually collected. When cash is received or paid out, adjustments to the accrual accounts are made to reflect the change in the revenue or expense accounts. Accrual basis accounting is in conformity with generally accepted accounting principles (GAAP).

C. CONVERSION FROM CASH BASIS TO ACCRUAL BASIS

Accrual based accounting measures revenues and expenses more accurately and is required by GAAP. Consequently, HUD requires all cooperatives to use this basis of accounting.

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In making the conversion from a cash based system to an accrual based system, a minimum of the following steps will be necessary:

1. Prepare a journal entry to record the ending balances of all asset and liability accounts on the Statement of Financial Position. These figures will be posted on the new year's general ledger.
2. Prepare a list of recurring journal entries to be booked each month. This will include:
  - o Capital contributions
  - o Amortization of prepaid expenses
  - o Depreciation of fixed assets
  - o Expense accruals
  - o Allowance for doubtful accounts
3. Examine period of operations after fiscal year-end to determine which expenditures should be recorded as liabilities (i.e., accounts payable) for accrual accounting purposes and which accounts already have an amount accrued.

4. Record any current accounts payable liabilities.
5. Examine the status of Resident Occupancy Charges to record the arrearage amounts and the current monthly charges to their respective income accounts, with offsetting entries to accounts receivable,
6. Prepare a trial balance to ensure that entries balance to zero.

2-6. IMPLEMENTATION OF AUTOMATED ACCOUNTING SYSTEM

A. OVERVIEW OF AUTOMATED DATA PROCESSING (ADP) SYSTEMS

The decision to automate the accounting functions for cooperative housing corporations must be made after completing an analysis of the current system capabilities. The analysis may include Data Flow Diagrams (DFDs) showing the flow of information within the current system.

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B. PROJECT INITIATION PHASE

Once it has been determined that using an automated system is feasible and cost effective, a system abstract will be developed to provide a high-level description of the features that will need to be incorporated into the new system. The system abstract presents the critical business functions, performance measurements, a processing abstract and a technology abstract.

For a cooperative housing corporation system, the system abstract may consist of the list of HUD-required reports, the required chart of accounts for cooperatives, the reporting and data entry requirements, a possible program menu, and a potential technical platform for the system.

C. PROJECT DEFINITION AND DESIGN PHASE

Once the general system design has been agreed upon by the board of directors and any other staff, the system details will be documented in the system design. This includes defining the screen layouts, the data files needed to support the system, and the report layouts.

D. PROJECT DEVELOPMENT PHASE

The system design document is used as input for the system development phase. For a new system development project, the system design document will be used for the development of

program specifications. The programmer uses the specifications for the development of the application programs.

If a package software solution is recommended, the system design document will be used to verify that the software package supports the requirements of the system design.

During this phase, the programs are developed and tested. In addition, user procedures are defined. The procedures will define how transactions are posted to the chart of accounts, how the different ledgers relate to each other, and how financial reports are generated.

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E. PROJECT IMPLEMENTATION PHASE

Installation of the application software must be coordinated, parallel operations must be scheduled and system implementation dates must be defined.

Parallel operations of the manual system and the automated system will be necessary for several reasons. Systems testing will be performed on the automated system during the parallel conversion to verify the same results are derived from both systems. Parallel operations are also necessary so that the cooperative corporation system users can gradually become familiar with the automated system before the final cutover is made.

After the system is operational, users will be trained on use of the system to generate reports and to enter cooperative financial information into the system.

F. COMPUTER GENERATED REPORTS

It is important to complete an acceptance test to verify that the forms and reports generated from the automated system are similar to the forms and reports previously used in the manual system. Additional worksheets and reports may be available through the new system however, at a minimum, the automated system should generate the same set of reports produced by the manual system.

G. ADP CONTROLS

The ADP environment presents special challenges for ensuring adequate internal controls and audit trails because of the limited opportunities for the segregation of duties. However, ADP controls can be established to address organizational and operational issues. System controls for automated financial accounting software are designed to prevent, detect, and correct errors that could adversely impact cooperative housing corporation business

activities. Some examples of system controls for verifying the input, processing and output of cooperative housing accounting systems include:

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1. Establish password access to the financial accounting system to ensure only designated board members have access to the system.
2. Limit data update capabilities to a controlled set of system users. Access to financial data should be limited as should access to report generation capabilities.
3. Place field edits on data entry fields to ensure the complete and accurate recording of general ledger account transactions.
4. Generate exception reports when discrepancies in account balances exist or when transactions are suspended.
5. Generate exception reports when records are deleted, or when financial amounts are changed.
6. Generate monthly audit reports to ensure that a complete and accurate audit trail exists. The audit reports need to be available for review as necessary.

2-7. CONVERSION TO AUTOMATED FINANCIAL ACCOUNTING SYSTEMS

The most appropriate time to convert cooperatives from a manual to an automated accounting system is at the beginning of the fiscal year. At the end of the prior fiscal year the accounts are closed out and the account balances are reconciled. The financial statements are reviewed allowing for a clear baseline from which to initiate the automated system activity.

2-8. INTERNAL CONTROLS FOR FINANCIAL ACCOUNTING SYSTEMS

In establishing a financial accounting system for a cooperative corporation, a system of internal controls needs to be defined. The system of internal controls can be thought of as a filtering device that prevents actions or events from leading to organizational problems. The following is a list of general, receipt, and disbursement controls to be used as a guidelines for establishing internal controls.

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A. GENERAL

1. All cash receipts (including those collected by management agents) must be deposited in the name of the project in a bank whose deposits are federally insured. Such funds shall be withdrawn only under the provisions for project expenses. Any owner receiving funds from the project, shall immediately deposit such funds in the project bank account.
2. As insurance against loss, the board of directors or their designated agent must submit to the Field Office proof of a fidelity bond in an amount at least equal to potential collections for two months if requested to do so by the Field Office. Blanket coverage should extend to all employees handling cash.
3. Numbered receipts for carrying charges shall be used and reconciled to actual collections.
4. The person making up deposits shall not handle the accounts receivable or the general ledger.
5. Disbursement checks shall be identified with all relevant account numbers and amounts applicable to each account when one check is for more than one invoice/bill.
6. The person preparing the payroll shall not handle the related pay checks.
7. Unissued checks should be locked up and access to checks should be restricted to a limited number of authorized personnel.
8. The number of bank accounts and inter-bank transfers should be kept to a minimum.

B. RECEIPT CONTROLS

1. Collections and all other funds held within an office, whether pending regular deposit or in imprest funds, shall be completely controlled under proper safeguards, preferably in a fire-resistant combination safe or safe-cabinet.

2. A sequential numbering system shall be used to track all

checks received and deposited.

3. Insofar as is possible, all collections shall be promptly deposited on the day received.
4. Bank statements shall be reconciled by persons other than those recording or handling cash, or preparing and signing checks.

C. DISBURSEMENT CONTROLS

1. A request for a check must have supporting documentation (i.e., invoice itemizing amount requested with an authorized signature) in order for approval to be obtained to make the disbursement.
2. Checks must be approved by an individual authorized to approve checks.
3. The authorized check signer shall review supporting documentation before signing checks.
4. A monthly reconciliation shall be performed to ensure that all checks disbursed are accounted for (i.e., cashed, outstanding, or void).
5. The monthly reconciliation shall be performed by someone other than the person who authorizes the checks.
6. Invoices should be marked "paid" and the check number and date should be posted to the invoice. Supporting vouchers shall also be marked "paid" to prevent resubmission.
7. An adequate recording system shall be used to note all checks issued and cash disbursed.