Appropriateness of Double-Entry Accounting Method for Service Charge Returns

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Abstract:
Service charge administration is one of the most difficult aspects of facility management of serviced apartments. Estimates upon which occupants make advance payment into account may be wrong or bastardised by inflation while some difficult occupants may not pay promptly. Then follows the issue of rendering returns at the end of accounting period. Most managers do not have adequate accounting knowledge and refuse to employ accountants for such services. A problem is therefore created when returns are not rendered rightly and through acceptable accounting method. The research examined this problem through a descriptive survey method. Out of 200 estate surveyors/valuers and chartered accountants administered with questionnaire, 126 completed theirs successfully and returned them for analysis. Data were summarised through frequency distribution and analysis was made through Chi-square tool. Major findings indicated that combination of incomplete records and double entry accounting methods could be used for rendering service charge accounts but the services of a chartered accountant should be employed to render proper accounts through double entry methods; and it was so recommended.

Key words: service charge, single entry, incomplete records, double entry, estimates.

Introduction.

These researchers would like to look at service charge as amount of money paid for provision of amenities, facilities and other services available to the property for which rent had been charged. It is an additional payment, different from the rent payment for the use of the property. It is applicable to other areas like restaurants and lodging accommodation whereby a customer makes extra payments, in addition to payment for food eaten and accommodation used.

In case of apartments that are serviced, managers compute service charge based on estimated costs of different expenditures necessary to make the accommodation serviceable. These heads may include clearing of common areas, janitorial services, security, power generating sets and diesel, lifts and provision for central air conditioning for heating. Estimates made on projected expenses for the services are totalled and divided among all occupants based on lettable spaces or units occupied.

Problem occurs when the property manager collects the service charge deposits from the occupants based on his estimates and fails to render returns correctly or appropriately to occupants after expending their funds within the accounting period, through an acceptable accounting method.

Statement of the problem.

It is required that the property manager should render appropriate and comprehensive returns at the end of each accounting year to all occupants who contributed to the service charge account. This account should be well understood by all occupants. Most times it is not so. The problem this research seeks to address therefore is to establish the appropriateness of double-entry accounting method in rendering proper and comprehensive returns at the end of each accounting year to the occupants.

Aim and objectives

The aim of this research is to establish the appropriateness of double-entry method for computation of service charge returns in management of serviced property.

Objectives

In the process of achieving this aim, the following objectives were necessary:

(i) To identify various accounting methods in used for computation of service charge returns;
(ii) To compare the various accounting methods used in recording service charge returns;
(iii) To analyse the data from respondents in regard to use of double-entry as appropriate method in computation of service charge returns;
(iv) To see if combination of various methods is suitable for computation of service charge returns.

The research also addressed the following questions:

(i) What are the various accounting methods in use for computation of service charge returns?
(ii) Which of the accounting methods used in computing service charge returns is the most appropriate?
(iii) What is the appropriateness of double-entry method in computing service charge returns?
(iv) Is combination of various methods suitable for use in calculation of service charge returns?

Literature review.

Service charge as seen by estate surveyors.

Akomolede (2006), defines service charge as a payment made by occupiers of a building or an estate for maintenance of common services. He further states that in block of offices, flats or shopping plazas, some services would have to be provided jointly for the benefit of all occupiers. Such services, according to him, include but not limited to the following: servicing of generator, servicing of lift, servicing of central air conditioners, servicing of borehole and water pumps, payment of electricity for common lighting, dislodgement of septic tanks, water disposal, gardening, cleaning of common areas, security, maintenance of swimming pool and other recreational activities, if any. Though the above author sounded a caveat, “not limited to the following”, diesel is a very important factor in service charge that once servicing of generating set is mentioned, regular purchase of diesel should also be mentioned.

Merriam-Webster (2015), defines service charge as an amount of money that is charged for a particular service in addition to a basic fee; an amount of money paid to owner of an apartment building for services (such as garbage collection).

Realestatedefined (2013), sees service charge as a periodic charge or expense incurred in running a building, especially cost or expense that benefits more than one party (whether a tenant or owner-occupier) in a multi-occupied building in particular, such costs as are regularly recharged by a landlord to a tenant in accordance with the terms of a lease and which vary from time to time according to the actual expenditure incurred on running of the building, but not rent payable.

According to Ebi (2017), service charge account is used to record every transaction that transpires in provision of services on any tenement. To him landlord’s responsibility must be differentiated from service charge expenses, for example repairs to roof of a property.

These researchers wish to add that it covers all occupiers, not necessarily tenants, as they could be a mixture of tenants and landlord in same tenement.

Accountants’ view of service charge.

Since accounting has been called the language of business (Bloomfield, 2008), it plays a crucial role in providing needed information for the stakeholders in the property industry to make informed decisions regarding the lease and the management of the property. In both residential and commercial properties, the accounting information is needed by the

owner of the property as well as the tenant. The tenant also needs the accounting information to know how much service charge he needs to pay as well as how the previous one he paid had been spent (Gluszek & Zieba, 2014). This type of information would help the tenant to plan his budget as service charge is a hidden cost that varies with certain internal and external factors.

As Gluszek and Zieba (2014) indicate, both the landlord and the tenant are highly interested in the service charges and the rental amount. The rental amount is clearly stated in the lease contract and it is not tied to the variability of certain factors during the period of the lease contract. Unlike the rental amount, the service charge is a hidden cost that is not easy or very difficult to determine upfront when the landlord or the company managing the property is presenting the budget to the tenant. The actual amount spent on maintaining the property for the accounting period under consideration would be known at the end of the accounting year (Pargma, 2004; Barrass, 2015). But accounting for the service charges in both commercial and residential properties has been causing uncomfortable and sometimes tense relationship between the landlord and the tenant. Holt (2016), indicates that the Service Charge Operating Report (SCOR) for offices published annually in United Kingdom (UK) has identified deficiencies in the service charge accounting statements for the past six years. The deficiencies include inconsistency, incomparability, and lack of transparency in the accounting information presented to the tenants in these properties. He calls on the accountants to improve the quality of service charge financial reporting as they are the ones with the right skills and expertise to make it happen. He calls for the application of double entry system in preparing service charge accounting statements.

Barras (2015), indicates that the issue of accounting for service charge has been a public debate in the property industry for a long time. He argues that accounting for service charge is carried out by preparing and presenting the budgeted service charge to the tenants at the beginning of the accounting year. The actual service charge expenditure will then be reconciled with the budgeted service charge at the end of the year to determine the difference or variance between the actual service charge expenditure and the budgeted service charge. He indicates that as simple as this process looks like, it is causing unpleasant relationship between the facility manager and the tenants.

According to Uwaegbulam (2015), the 1004 Residents' Association in Victoria Island, Lagos, Nigeria accused the property managing company of charging high service charge, mismanagement, lack of transparency, accountability, and fairness. The issue surrounding service charge accounts is similar globally. Gluszek and Zieba (2014), indicate that "Accounting for service charges and service charge accounts in the property industry is a specialist area that requires expertise and understanding of the sector".

Common methods used for retirement of service charge

(i) **Single entry and incomplete records**

According to Bala (2016), a form of financial recording transactions that are incomplete can be regarded as incomplete recording. In other words, it is a recording that derives from incomplete records and fails to detail the two aspects of accounting. It is a form of double entry recording but in an incomplete form.

Sharma (2017), says while it is not strictly based on double entry rules, it is based on ordinary memory and incomplete records. Sharma (2017), also describes single entry as a mixture of double entry, single entry and no entry. According to him, it is suitable for small businesses and personal accounts which ignore real and nominal accounts. It may show profit and loss account but its layout may not be seen. In order to see the profit or loss of the business, capital

at the beginning is compared with capital at the end of the accounting period.

Some of the advantages presented by use of incomplete records or single entry system include, but not limited to: simplicity and inexpensiveness of the method. It also saves time. Some of the disadvantages also include: inability of the method to be used for preparation of regular profit and loss accounts and trial balance that checks arithmetical accuracy. It also lacks uniformity and may present difficulty in detecting fraud.

(ii) **Double entry**

Leiwy (2015), says this system of accounts is known as double entry because, for each transaction, there are two entries, a debit (Dr) and a credit (Cr). Even when several debits and credits are recorded in different 'T' accounts, all the credits in different accounts must eventually be equal to the debits in the other accounts. This is understable, in that, a debit on cash book will also produce a credit on sales book. Taking this further to our service charge account, a credit received by an occupant through payment of service charge will always produce a debit on service charge returns book. A purchase or payment for an item made from the service charge account will debit the purchase (or contractor's) account while the service charge is credited for releasing the amount. The rule states that whatever transaction made should have entries on left side of an account or accounts and same should be extended on right side of another account or accounts. This forms the accounting equation.

Service charge preparation and returns

(i) It starts from estimates of all captured expenses to be incurred within the period, usually one year; this shall include the management firms' fees for the period.

(ii) All occupants are grouped either in units (say flats) or office space (square metres) and totalled, say six flats or 500 square metres.

(iii) The total service charge for the period is divided by the total units or space in the tenement and the result is multiplied by the number of units or space occupied by each occupant; that forms the amount of service charge to be paid by each occupant.

Assuming that the estimated total expenditure for the year is ₦2, 553,613.48 (including management fees), and there are six flats, then each flat will pay ₦2, 553,613.48 ÷ 6, i.e. ₦425, 602.25.

Certain rules should be kept in order to produce a good service charge returns. Depending on magnitude of transactions and the accounting systems used, the rules apply.

Littlejohn (2017), agrees that:

i. it should be prepared periodically at equal intervals, e.g. quarterly, 6 monthly or yearly;
ii. there should be client's account where monies paid in but not used should be kept in a "ring-fenced" system that bars the manager from mixing with their normal incomes;
iii. a normal income and expenditure statement with explanatory notes and where applicable, balance sheet must be prepared.

Table 1.0: Example of Income and expenditure statement of service charge account.

EBI, SOETAN & PARTNERS
Income and Expenditure Statement

S/N	Date	Description	Income (₦)	Expenditure (₦)	Balance (₦)
1.	05/01/2016	Amount b/d	-	-	360,760.43
2.	09/01/2016	Surveyor's transport to and fro Ikeja GRA	-	250	360,510.43
3.	15/01/2016	Service charge paid by Kukundi & Co. (for diesel)	248,000	-	608,510.43
4.	15/01/2016	Fee to Ebi, Soetan & Partners	-	24,800	583,710.43
5.	16/01/2016	Diesel supplied 2,000 litres at ₦124 per litre	-	248,000	335,710.43
6.	16/01/2016	Surveyor's transport to and fro Ikeja GRA	-	250	335,460.43
7.	12/02/2016	Service charge paid by Danae & Sons	88,000	-	423,460.43
8.	12/02/2016	Jan. salary to security men	-	88,000	335,460.43
9.	12/02/2016	Fee to Ebi, Soetan & Partners	-	8,800	326,660.43
10.	12/02/2016	Jan. salary to cleaner	-	16,000	310,660.43
11.	12/02/2016	Surveyor's transport to and fro Ikeja GRA	-	250	310,410.43
12.	29/02/2016	Balance c/d	-	-	310,410.43

Table 2.0: Example of double-entry method in service charge returns.

EBI, SOETAN & PARTNERS
Service Charge Account

₦	₦
Bank (contributions from occupants) 4,000,000 Interest earned 400,000	General repairs 100,000 Maintenance (front space) 100.000 Lift repairs 200,000 Lift maintenance 140,000 Cleaning 150,000 External decoration 160,000 Electricity 150,000 Generator and diesel 2,000,000 Water 80,000 Accountancy cost 190,000 External auditor fees 100,000
4,400,000	
Balance b/d 300,000	

	Building insurance 180,000 Fire insurance 150,000 Managing agent fees 400,000 Balance c/d 300,000 **4,400,000**

Research Methodology

The research method used was descriptive. Relevant data was collected through the use of questionnaire. Out of the sample size of 100 estate surveyors and valuers and 100 chartered accountants administered with questionnaires, 126 were successfully completed and used for final analysis. Data were first summarised in frequency distribution form after which the researchers analysed the research questions through Chi-square tool.

Data presentation and analysis.

Looking at our research questions one, two and three, the following data and analysis are presented:

Table 3.0: What are the various accounting methods most commonly used in computing service charge returns?

	Frequency	**Percentage (%)**	**Valid Percentage (%)**	**Cumulative Percentage (%)**
Incomplete records	36	28.6	28.6	28.6
Single entry	27	21.4	21.4	50
Double entry	63	50	50	100
Total	**126**	**100**	**100**	

Source: Field survey, 2017.

The method most commonly used for computing service charge returns is the double entry as 63 respondents (50%) ticked. This is followed by incomplete records method ticked by 36 (28.6%) of the respondents. Only 27 (21.4%) of the respondents use single entry. Double entry method, from the above, is the most commonly used.

Table 4.0: What are the less commonly used accounting methods in computing service charge returns?

	Frequency	**Percentage (%)**	**Valid Percentage (%)**	**Cumulative Percentage (%)**
Receipts and Payments Cash Book	54 72	42.9 57.1	42.9 57.1	42.9 100
Total	**126**	**100**	**100**	

72 respondents (57.1%) agree that use of Cash Book is less commonly applied in computing service charge returns. Also 54 respondents representing 42.9% agree that Receipts and Payments are less commonly used in computation of service charge. From the above, accountants and valuers agree that Receipts and Payments and Cash Book are less commonly used for computation of service charge returns.

Table 5.0: Which of the accounting methods used in computing service charge returns is most appropriate?

	Frequency	Percentage (%)	Valid Percentage (%)	Cumulative Percentage (%)
Incomplete records	9	7.1	7.1	7.1
Single entry	9	7.1	7.1	14.2
Double entry	108	85.8	85.8	100
Total	**126**	**100**	**100**	

Double entry method was ticked as the most appropriate for computing service charge returns by 108 (85.8%) of the respondents while 9 respondents (7.1%) each ticked incomplete records and single entry. By use of frequency distribution, double entry method is the most appropriate accounting method to be used for computing service charge returns.

Table 6.0: Do you agree that combination of incomplete records and double entry methods can be employed in computation of service charge returns?

	Frequency	Percentage (%)	Valid Percentage (%)	Cumulative Percentage (%)
Strongly disagree	18	14.3	14.3	14.3
Disagree	9	7.1	7.1	21.4
Do not know	9	7.1	7.1	28.6
Agree	63	50	50	78.6
Strongly agree	27	21.4	21.4	100
Total	**126**	**100**	**100**	

Respondents that agree that combination of incomplete records and double entry methods can be used are 63 (50%), while 9 (7.1%) each disagree or do not know. 18 (14.3%) strongly disagree while 27 (21.4%) strongly agree. It seems tenable, therefore, that a combination of incomplete records and double entry methods can be used.

Statistical significance

Further analysis through Chi-square reveals statistical significance. The tables, though not shown for want of space, reveal that all tables analysed from the above frequency distribution tables, have expected counts less than 5. These are in each case more than minimum expected count range from 0.07 to 1.29.

Findings and conclusions

(i) The accounting methods mostly used for computing service charge returns in order of usage are double entry method, incomplete records and single entry system.

(ii) The less commonly used accounting methods used in computing service charge returns in the order of usage are cash book and receipt and payments.

(iii) The most appropriate methods used in computing service charge returns

in order of usage are double entry method and single entry/incomplete records. Majority of computations are done with double entry methods.

(iv) Majority of managers agree that combination of incomplete records and double entry methods can be employed.

Recommendations and summary

Recommendations

(i) Managers of serviced apartments should use double entry method of accounting to render returns to occupants.

(ii) Where combination of incomplete records and double entry methods are used, the end result should still be harmonised returns through double entry.

(iii) Managers of serviced tenements can do their day-to-day recordings through incomplete records and employ the services of chartered accountant who will convert such entries to double entry account.

Summary

Service charge administration is one of the most difficult aspects of facility management. Starting from the estimates at the beginning of the accounting period, to non-payment by some tenants and inflation which renders estimates useless, to computation of returns, there are bound to be conflicts among managers and occupants. The managers should do all they can to be transparent and knowledgeable in their day-to-day schedules, as the first step. Then they should engage a professional accountant to be able to compute their service charge return to occupants through double entry method of accounting.

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