CIPFA

FINANCIAL AND PERFORMANCE REPORTING

Diploma stage examination

4 December 2007

From 2.00pm to 5.00pm
plus ten minutes reading time from 1.50pm to 2.00pm

Instructions to candidates
*There are **six** questions on this question paper*
*Answer **five** questions in total*
Two compulsory** questions from **Section A ***Three** of the four questions from **Section B***
*The questions in Section A carry, in total, **40** marks* *The questions in Section B each carry a total of **20** marks*

All workings should be shown. Where calculations are required using formulae, calculators may be used but steps in the workings must be shown. Calculations with no evidence of this (for example, using the scientific functions of calculators) will receive no credit. Programmable calculators are not permitted in the examinations room.

Formula sheets, Proforma booklets, tables, graph paper and cash analysis paper are available from the invigilator, where applicable.

Where a question asks for a specific format or style, such as a letter, report or layout of accounts, marks will be awarded for presentation and written communication.

AT THE HEART OF
YOUR CAREER

SECTION A (Compulsory – answer both questions)

1

The following trial balance has been extracted from the financial ledgers of Altonborough Unitary Authority for the 2003/04 financial year:

	£'000	£'000
Net operational assets	991,640	
General Fund balance		29,658
Sale of assets		9,062
Loans received		235,204
Loans repaid	196,020	
Stock	14,480	
Short-term debtors	15,196	
Short-term investments	5,188	
Cash and bank	174	
Creditors		8,858
Finance lease		600
Long term borrowing		452,326
Fixed asset restatement account		397,960
Capital financing account		25,802
Usable capital receipts reserve		23,166
Central services (net)	55,580	
Education (net)	890,352	
Cultural, environmental and planning (net)	115,068	
Social Services (net)	180,378	
Highways, roads & transport (net)	46,470	
Interest paid	43,984	
Interest received		1,002
Revenue support grant		424,924
NNDR		185,134
Council tax		756,974
Suspense *(notes (i) & (ii))*		3,860
	2,554,530	**2,554,530**

Additional Information

(i) A capital grant amounting to £4,000,000 has been received to help fund a new day centre for vulnerable young people costing £4,500,000. The centre is expected to have a life of 40 years. The new asset is reflected in the net operational asset figure in the trial balance and the grant received has been credited to the suspense account.

(ii) Capital expenditure for the year, all of which is included within net operational assets, has mainly been financed through the use of loans from the Public Works Loans Board. These loans have been included in the loan transactions above.

The finance lease of £600,000 was taken out with a lease term of 5 years. The annual payment for 2003/04 has been debited to the suspense account.

The remaining financing of capital expenditure that has yet to be reflected in the trial balance is as follows:

	£000
Use of capital receipts	6,000
Direct Revenue Finance	1,980

(iii) Education assets with a net book value of £8,850,000 as at 31 March 2003 were sold in the year. The proceeds of sale have been recorded as "sale of assets" in the ledgers, but no other entries have been made.

(iv) Altonborough's policy is to charge a full year's depreciation in the year of acquisition, none in the year of disposal, and to calculate notional interest based on closing net book values. However, the trainee accountant has calculated asset rentals for the year as follows, based on the net operational assets balance included in the trial balance above, before adjustments for disposals were made.

	£000
Depreciation	18,803
Notional interest	31,232
	50,035

The asset rentals should be allocated as follows:

	£000
Central Services	895
Education	30,784
Cultural, environmental & planning	13,567
Social Services	2,000
Highways, roads & transport	2,789
	50,035

The depreciation charge calculated by the trainee accountant includes £471,000 relating to the assets disposed of.

(v) The Minimum Revenue Provision for the year has been calculated as £19,765,000.

(vi) During the year, the environmental department performed £123,000 of grounds maintenance work in schools, which it invoiced to the education department and recorded in the ledgers of both departments, but it remained unpaid as at the year-end.

- **Requirement for question 1**

Prepare Altonborough's consolidated revenue account for the year ending 31 March 2004, and the consolidated balance sheet as at this date.

(20)

2

The Rural Regeneration Agency is a supply-financed central government agency. Its Balance Sheets for the past 2 years were as follows:

	31 March 2007 £'000	31 March 2006 £'000
Fixed assets - NBV	30,816	28,700
Current assets		
Stock	78	40
Debtors	1,710	1,580
Cash	1,019	400
	2,807	2,020
Creditors due within 1 year	(4,823)	(2,960)
Provisions	(70)	(70)
Total net assets	28,730	27,690
Taxpayers' equity		
General fund	21,195	21,500
Revaluation reserve	5,948	4,690
Donation reserve	1,587	1,500
	28,730	27,690

Additional information for the year ending 31 March 2007:

1. Net indexation/ revaluation of £1,446,000 has been charged on all fixed assets.

2. The donation reserve relates to the Agency's administrative building, Oakwood Mansion, which was donated to the Agency by Sir William Oakwood in the early 20th century. Net indexation of £127,000 was charged on the building for the year, which is included in the net indexation/revaluation balance in note 1 above. £40,000 was transferred from the donation reserve to income in relation to depreciation on the building. No new assets were donated in 2006/07.

3. Purchased land with a book value of £80,000 and a historic cost of £19,000 was disposed of in the year. A profit of £15,000 was recorded in the operating cost statement for this sale.

4. The total depreciation charged to the operating cost statement totalled £2,230,000.

5. The agency's net supply voted for the year was £6,994,000 and it had a surplus to surrender on its gross vote of £780,000. The agency raised £4,890,000 in Appropriations in Aid in the year, compared with £4,678,000 voted for the year.

6. Creditors listed in the balance sheet as at 31 March 2007 include £73,000 in respect of capital creditors.

7. The cost of capital has been included in the Agency's operating cost statement at a rate of 3.5%. The audit fee for the year was £34,000. All cash is held in PAYMASTER.

- **Requirement for question 2**

Prepare the cash flow statement for the Rural Regeneration Agency for the year ended 31 March 2007, including all supporting notes.

(20)

SECTION B (Answer three from four questions)

3 You are a trainee accountant employed by Wryley City Council, a large unitary authority. Your boss, the Director of Corporate Affairs, has received the following letter from a newly elected councillor and she has asked you to draft a reply.

The Old Vicarage
Upper Wryley
Mapleshire M12 4FT

Ms Louise Doyle
Director of Corporate Affairs
Wryley City Council

Dear Ms Doyle

I have recently been elected as a councillor, and was wondering if you could be of assistance to me. As a retired solicitor, I have no experience of local government but I have been reading about various issues currently facing local government finance that I was hoping you could clarify for me.

a) The business pages seem to be full of stories regarding corporate governance failings in private sector companies, and I gather that the private sector has now taken many steps to put improved corporate governance procedures in place. Please can you explain to me what steps are being taken in the public sector to improve corporate governance, and the specific corporate governance developments affecting local authorities.

b) One of my fellow councillors told me that the council is a member of something called a benchmarking club, as she was looking at a report comparing the performance of our leisure services to some other local authorities in this area. Please can you explain what benchmarking is, how the process works and what its advantages are?

c) I was browsing through Wryley's recent financial statements, and I noticed that as well as the consolidated accounts, there is a separate revenue account dealing only with housing activities. Why is this? Wouldn't it be easier just to include the housing amounts in the main consolidated accounts?

d) One of my neighbours used to be a Wryley councillor until a few years ago, and he told me that the council's spending on new capital projects is limited by the amount of money that can be borrowed to finance these projects, which is in turn limited by something called Credit Approvals. Please explain what Credit Approvals are, and whether they are still used, or have they been replaced by this new Prudential Code thing that I've heard about? What is this? I don't really understand why we would need to borrow money anyway, as we can surely just increase council tax whenever we need more money for a capital project?

I would appreciate clarification of the above points as soon as possible.

Yours sincerely,
George Edalji LLB

Councillor

- **Requirement for question 3**

Draft a letter from Ms Doyle to Mr. Edalji, ensuring that you address all of the points raised in Mr. Edalji's letter. Marks will be awarded as follows:

(a)	Corporate Governance developments	*7*
(b)	Benchmarking	*7*
(c)	Housing Revenue Account	*2*
(d)	Credit Approvals and the Prudential Code	*4*
		(20)

4

You are a financial accountant with West Hope NHS Trust. The Chief Executive has commissioned a review of the Trust's fixed assets and has asked the Finance Director to provide information on assets held at 31 March 2007. She wishes to use this information to discuss the issue with the Trust Board, and so she wants the information to be presented in a user-friendly manner.

The Finance Director has emailed you as follows:

'You are probably aware that we are involved in a major review of the Trust's fixed assets. I would like you to produce a schedule showing the movement in the value of fixed assets between 1 April 2006 and 31 March 2007. This should be detailed enough for Board members to discuss each class of asset separately. All movements, such as disposals, indexation, impairments, etc should be clearly identified. In addition, I'd like you to include a *brief* explanation of what each adjustment is for and how it has been calculated. See Attachment 1 for data and our fixed asset policies'.

Attachment 1:

Tangible fixed asset information

1. Balances held at 1 April 2006

	£000
Land	85,500
Buildings	72,000
Equipment	48,000
Equipment depreciation	14,000
Assets under construction	2,500

None of the assets held at 1 April 2006 had been donated.

2. During the year, the following transactions took place:

   - On 10 October 2006, equipment (estimated 10 year life) was bought for £24,000.
   - On 5 May 2006, a building (estimated life 45 years) was bought for £347,000.
   - On 12 February 2007, equipment (estimated 5 year life) was donated to the Trust. The value of the asset was £33,000.
   - On 5 March 2007, equipment (7 year life) was purchased for £52,000.
   - On 24 December 2006, equipment (7 year life) was sold for £12,000. The asset was bought on 1 May 2004. Its current cost at 1 April 2006 was £48,000.

3. Buildings are depreciated over their remaining useful life, which was estimated to be 45 years from 31 March 2006. Equipment is depreciated on current cost over the estimated life of the asset.

4. A piece of land was revalued on 1 April 2006 from £75,000 to £120,000.

5. At 1/4/2006 the current cost and accumulated depreciation of the equipment was split over the various lives as follows:

	Cost	Dep'n
	£'000	£'000
5 years	£12,500	£3,750
7 years	£25,000	£7,500
10 years	£10,500	£2,750

6. Indices for the year were:

	Opening	Closing
Land *	1.08	1.06
Buildings	1.06	1.07
Equipment	1.05	1.07
Assets under construction	1.06	1.06

* There was a balance in the revaluation reserve of £500,000 for land.

- **Requirement for question 4**

(a) Prepare a Tangible Fixed Assets schedule as requested by the Finance Director, suitable for using in a report and presentation to the Trust Board. *11*

(b) Prepare brief notes explaining each of the adjustments in the Tangible Fixed Assets schedule, including the financial standards and other regulations that must be followed. *9*

(20)

5

You are the financial controller of Porterhouse University. The University was established in 1853 in part from a gift from Lady Mary Evans, the widow of a famous Egyptologist. On her death in 1874 she bequeathed the University a considerable investment and property portfolio. The income from this was to be used solely for the purposes of establishing a faculty of Egyptology and supporting students who wished to study the subject. These assets comprise about half of all the endowment assets held by the University. The remainder of the endowments is of an unrestricted nature.

Over time the University has expanded its faculties and it now offers a range of courses, mostly of degree level. However, in recent years the management board of the University has become increasingly concerned about the future of Porterhouse as a centre of higher education.

A principal concern is the fact that student enrolments have fallen for the last five years including a 10 per cent fall in the last year. The main problem with enrolments seems to lie in the University's over-reliance on courses which are no longer perceived as relevant by prospective students.

The board has recently appointed a new Vice-Chancellor, Sir Ronnie Godber-Evans, former Managing Director of United Porridge Oats Ltd and distant relative of Lady Mary. His remit is to re-establish the University as a centre of excellence in the field of catering and dietary science, building on the success of the Scullion School of Catering, a faculty of the University. The proposed plan calls for considerable investment (something in the region of £10 million over the next three years) in order to achieve this.

Sir Ronnie has asked you to put together some information for the next meeting of the University's board of management focusing on recent financial performance and the key factors lying behind that performance. He also wants you to put forward some suggestions on how financial performance might be improved and ways in which the expansion of the catering faculty might be financed.

You have several items of information to hand including the following taken from the last two years' financial statements:

Porterhouse University: Group Income and expenditure account for the year ending 31 July

	2007 £000	2006 £000
Income:		
Funding council grants	19,157	20,133
Tuition fees and education contracts	8,119	8,572
Research grants and contracts	6,044	6,224
Other income	3,403	2,611
Endowment and investment income	4,239	3,338
Total income	40,962	40,878
Expenditure:		
Staff costs	(27,061)	(29,806)
Other operating expenses	(7,815)	(5,406)
Depreciation	(2,252)	(2,351)
Interest payable	(20)	(4)
Total expenditure	(37,148)	(37,567)
Surplus on continuing operations before tax	3,814	3,311
Taxation	(230)	(191)
Surplus on continuing operations after tax	3,584	3,120
Transfer to accumulated income within specific endowments	(2,829)	(2,031)
Retained Surplus for the financial year	755	1,089

- Income from research grants and contracts has been stable over the last few years;
- Other income consists primarily of receipts from catering and conferences (£1,411,000 in 2006; £1,635,000 in 2007) and rents from University owned student accommodation;
- Last year, in a bid to raise income, the University increased rents by 25 per cent. Student opposition to this rise led to a rent strike by approximately half the students in University owned accommodation;
- The increase in other operating expenses was due almost entirely to expenditure on a backlog of repairs to buildings and student accommodation;
- For both years the entire income earned from restricted endowments has been transferred to reserves.

Porterhouse University: Group Balance sheet as at 31 July

	2007	**2006**
	£000	**£000**
Fixed assets (at valuation)		
Tangible fixed assets	52,850	54,417
Investment properties	14,224	14,218
Total fixed assets	67,074	68,635
Endowment assets (at valuation)	53,636	50,507
Current assets		
Stock	15	16
Debtors	1,598	732
Current asset investments	2,079	-
Cash in hand	1	2
Creditors due within one year		
Trade creditors	(672)	(598)
Bank overdraft	(405)	(90)
Net current assets	2,614	62
Total assets less current liabilities	123,324	119,204
Provisions for liabilities and charges	(20)	(20)
Net assets	123,304	119,184
Financed by:		
Endowments		
Specific	27,032	26,063
General	26,604	24,444
Revaluation Reserve	19,227	18,991
General reserve	50,441	49,686
Total	123,304	119,184

- Investment properties in the balance sheet relate exclusively to University owned student accommodation.

The University has three internally set financial targets which are:

- Retained surplus for the year to equal at least 2.5 per cent of total income;
- Staff costs not to exceed 80 per cent of total costs (excluding depreciation);
- Endowment income to equal at least 5.5 per cent of the total value of endowment assets.

- **Requirement for question 5**

You are required to prepare a report to the management board of the University which covers the following points:

(a) Whether or not the University has achieved its targets for the two financial years and factors which may have affected this year's performance. *10*

(b) Any other matters emerging from the information above relating to the financial performance of the University which you consider should be mentioned. *3*

(c) Recommendations for improving the University's financial performance. *4*

(d) Suggestions for ways in which the additional funds needed for the proposed expansion might be raised. *3*

(20)

6

(a) Gerritson Housing Association (GHA) was set up 20 years ago to provide affordable housing in deprived areas of Gerritsonshire.

5 years ago, GHA could no longer afford the fees charged by local tradespeople to perform work on its housing stock, and so it set up a company called Maintenance Services Ltd (MSL). MSL was set up in order to provide electrical, plumbing and other maintenance services both to GHA's own housing stock and to private house owners in the local area. GHA owns 90% of MSL's share capital, with the remaining 10% being owned by MSL's employees.

During the 2006/07 year, MSL's total invoiced sales of work performed was £369,000, of which £207,000 relates to work performed on behalf of GHA. As at 31 March 2007, £84,000 of the invoices to GHA remain unpaid.

GHA also owns 50% of the share capital in Good As New Ltd, a company set up two years ago with a local private sector partner to sell affordable good quality secondhand furniture to its tenants.

- **Requirement for question 6 (a)**

(i) Explain how MSL should be treated in the GHA group consolidated accounts, with reference to applicable accounting standards. *3*

(ii) Explain how the work performed by MSL for GHA must be treated in the GHA group consolidated accounts, with reference to relevant accounting standards. Include any journal entries required to adjust the consolidated accounts, and explain the effect of these journal entries on the group's surplus and net assets for the year. *3*

(iii) Explain what type of relationship exists between GHA and Good As New Ltd with reference to relevant accounting standards. How should Good As New Ltd be treated in GHA's consolidated accounts, and how does this differ from the treatment of MSL? *3*

(iv) Explain one other adjustment that groups may need to consider making when preparing consolidated accounts. *1*

(b) GHA's housing stock is 25% funded by Social Housing Grants from the Housing Corporation. As at 1 April 2006, the gross cost of its housing stock is £3.2m and it has accumulated depreciation of £1.9m. Its policy is to charge straight-line depreciation over 30 years and there were no additions or disposals to housing stock during the year.

- **Requirement for question 6 (b)**

(i) Explain how GHA should account for its Social Housing Grant, with reference to relevant accounting standards and other guidance. *3*

(ii) Calculate GHA's depreciation charge for the 2006/07 financial year, and the net book value of its fixed assets as at 31 March 2007. *2*

(c) Consolidation is becoming more widespread across the public sector, including the Whole of Government Accounts Initiative.

- **Requirement for question 6 (c)**

What are the advantages of having Whole of Government Accounts? Can you think of any potential disadvantages? *5*

(20)