# FINANCIAL REPORTING AND ACCOUNTABILITY REPUBLIC OF IRELAND

**Professional 2 examination**
**10 June 2004**

From 10.00 am to 1.00 pm
plus twenty minutes reading time from 9.40 am to 10.00 am.

***Instructions to candidates***

*Answer **five** questions in total: the compulsory question from **Section A**, **one** question from **Section B, one** question from **Section C,** and **two** questions from **Section D.***

*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 examination room.*

*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.*

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

*Candidates may use the proforma sheets provided in the separate booklet and submit them as part of their answer.*

CIPFA

## SECTION A (Compulsory)

**1** The balance sheets for three individual companies as at 31 December 2003 are as follows:

| | H Ltd €000 | A Ltd €000 | B Ltd €000 |
|---|---|---|---|
| Fixed assets | 7,270 | 3,170 | 1,800 |
| Investment in A Ltd (2,000 50c shares) | 1,800 | - | - |
| Investment in B Ltd (800 €1 shares) | 2,960 | - | - |
| Net current assets | 355 | 1,205 | 1,355 |
| Less: proposed dividend | (125) | (75) | (75) |
| | 12,260 | 4,300 | 3,080 |
| Creditors due in > 1 year | (1,250) | (700) | (830) |
| Debentures | (800) | - | (600) |
| | 10,210 | 3,600 | 1,650 |
| Ordinary share capital | 8,000 | 2,500 | 1,000 |
| General reserve | 500 | - | - |
| Profit and loss account | 1,710 | 1,100 | 650 |
| | 10,210 | 3,600 | 1,650 |

**Additional information:**

(i) H acquired its shares in A Ltd at the beginning of this financial year. Ordinary share capital in A Ltd is unchanged.

(ii) H acquired its shares in B Ltd on 1 January 2000. At this date the retained profits were €1,500,000. The fair value of B Ltd's fixed assets was deemed to be €200,000 above the book value on acquisition, with 10 years of useful life remaining.

The profit and loss accounts for the three companies for the year ended 31 December 2003 are as follows:

| | H Ltd €000 | A Ltd €000 | B Ltd €000 |
|---|---|---|---|
| Turnover | 3,080 | 950 | 1,360 |
| Cost of sales | (1,985) | (560) | (1,155) |
| **Gross profit** | 1,095 | 390 | 205 |
| Distribution | (330) | (90) | (40) |
| Administration | (270) | (60) | (25) |
| **Operating profit** | 495 | 240 | 140 |
| Dividends receivable | 90 | - | - |
| **Profit before tax** | 585 | 240 | 140 |
| Taxation | (150) | (65) | (40) |
| **Profit after tax** | 435 | 175 | 100 |
| Proposed dividend | (125) | (75) | (75) |
| **Retained profit for the year** | 310 | 100 | 25 |

**Additional information:**

(i) H Ltd anticipates receipt of proposed dividends.

(ii) It is the policy of H Ltd to amortise goodwill over a 20 year period.

(iii) During 2003 B Ltd made sales to H Ltd, amounting to €250,000 of which €50,000 remained unsold by H Ltd at 31 December 2003. B Ltd applied a profit margin of 20%.

- **Requirement for question 1**

(a) Prepare the consolidated balance sheet for H Ltd as at 31 December 2003. *16*

(b) Identify the entries that should appear on the consolidated profit and loss account of H Ltd for the year ended 31 December 2003, in respect of the profit of A Ltd. *4*

***(20)***

**SECTION B (Answer one question)**

2

The consolidated balance sheet for SCC Ltd, a state sponsored company at 31 March 2003 is as follows:

| | 1 April 2002 €000 | 31 March 2003 €000 |
|---|---|---|
| **Fixed assets:** | | |
| Operational assets | 635,000 | 727,500 |
| Long term investments | 18,000 | 20,350 |
| **Total long term assets** | 653,000 | 747,850 |
| | | |
| **Current assets:** | | |
| Stock | 10,850 | 11,250 |
| Debtors | 13,500 | 18,750 |
| Cash and bank | 2,750 | 6,450 |
| **Current liabilities:** | | |
| Bank overdraft | (300) | 0 |
| Creditors | (20,750) | (24,500) |
| | | |
| **Total assets less current liabilities** | 659,050 | 759,800 |
| | | |
| Long term borrowing | (223,000) | (248,500) |
| | | |
| **Total assets less liabilities** | 436,050 | 511,300 |
| | | |
| Capitalisation Account | 421,350 | 486,050 |
| General fund Reserve | 14,700 | 25,250 |
| | | |
| **Total balances and reserves** | 436,050 | 511,300 |

(i) The revenue account included asset rentals of €83,500,000, of which depreciation was €17,500,000.

(ii) Cash inflows for 2002/03 were made up as follows:

| | €000 |
|---|---|
| Receipts from Debtors | 203,985 |
| | |
| Operating grant (general) | 258,500 |
| Grants (specific) | 29,250 |
| Other fees and charges | 8,750 |
| Interest received | 1,405 |

(iii) Cash outflows relating to employees totalled €393,115,000, while other operating expenditure included payments to creditors of €73,125,000 and interest paid of €16,650,000.

(iv) Capital expenditure was financed from a mixture of new borrowing plus receipts of €10,000 from sale of old assets which had NBV of €12,000. The increase in capitalisation account reflects revaluation of fixed assets.

- **Requirement for question 2**

(a) Prepare Note 1 (reconciliation from operating activities) to the cash flow statement. *6*

(b) Prepare a cash flow statement for 2002/03 (further notes are not required). *16*

(c) Discuss the appropriateness of cash flow statements in public service organisations. *3*

***(25)***

# 3

The Countryside Protection Agency is an agency of Central Government. The following information has been extracted from its balance sheet for 31 March 2003:

| | 1 April 2002 €000 | 31 March 2003 €000 |
|---|---|---|
| Tangible fixed assets - NBV | 2,750 | 2,925 |
| Stock | 810 | 750 |
| Debtors | 85 | 90 |
| Creditors | (320) | (260) |

**Additional information:**

(i) Land was valued at €1,250,000 at 1 April 2002 and at €1,425,000 at 31 March 2003. There were no acquisitions or disposals of land during the year. Movements on all other tangible fixed assets, in addition to the annual depreciation charge, included:

| | €000 |
|---|---|
| NBV of disposals | 200 |
| Revaluation of assets (excl land) | 170 |
| Acquisitions | 105 |

(ii) Disposal proceeds amounted to €225,000.

(iii) The net grant voted by Dail for the Countryside Protection Agency for 2002/03 was €8,580,000. There was additional miscellaneous income of €100,000.

(iv) Interest on short term investment account for the year was €50,000.

(v) The operating deficit before income (note (iii)) for the year was €8,550,000.

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- **Requirement for question 3**

(a) The issue of notional capital charges for agencies, which have and utilise state assets is under active consideration. In the case of this agency what would be the impact and accounting consequences of implementing a notional capital charge on fixed assets based on the national test discount rate of 5%. *7*

(b) Prepare Note 1 to the Cash Flow Statement for 2002/03. *10*

(c) Prepare a Cash Flow Statement for the year ended 31 March 2003. *8*

***(25)***

**SECTION C (Answer one question)**

4 As part of a pilot initiative, the local authority has established a holding company for housing stock, within the Planning and Development Directorate. The trial balance for the company for the year to 31 March 2004 is as follows:

| | €000 | €000 |
|---|---|---|
| Turnover/rents | | 42,500 |
| Interest receivable | | 420 |
| Operating costs | 31,450 | |
| Interest payable | 7,250 | |
| Land | 100,000 | |
| Housing Property: cost | 228,400 | |
| depreciation (1 April 2003) | | 2,820 |
| Housing property under construction | 31,865 | |
| Office buildings: cost | 4,800 | |
| depreciation (1 April 2003) | | 1,200 |
| Furniture/equipment: cost | 1,750 | |
| depreciation (1 April 2003) | | 700 |
| Cash at bank | 870 | |
| Debtors | 2,150 | |
| Creditors due within one year | | 3,650 |
| Provisions for liabilities and charges | | 300 |
| Central Grant: properties under construction | | 16,000 |
| other housing properties | | 106,400 |
| Loans | | 112,500 |
| Revenue reserves | | 116,400 |
| Disposals account | | 5,930 |
| Other suspense | 285 | |
| | 408,820 | 408,820 |

**Additional information:**

(i) Depreciation has not yet been charged for 2003/04. The policy is to charge depreciation in the year of acquisition and not in year of disposal. None of the existing fixed assets are yet fully depreciated. Asset lives, used to calculate depreciation on a straight line basis, are as follows:

| | |
|---|---|
| Housing property | 50 years |
| Other property | 20 years |
| Other assets | 5 years |

(ii) On 1 April 2003, the company sold a small office building for €730,000. The building had cost €400,000 and had borne depreciation of €160,000 by 31 March 2003. A second disposal took place at the end of the 2003/04 financial year. Housing property was sold for €5.2million, having originally cost €3.3million. €300,000 of this cost related to the land on which the property stood. Depreciation on this property amounted to €440,000 at 31 March 2003. This sale will necessitate the repayment of €1.1million in grants to central government, and it is the policy to transfer the profit on all disposals to the reserves. The only entries completed to date are to record the sales proceeds in the disposals account.

(iii) The suspense account contains repairs and maintenance expenditure, €210,000 of which has enhanced the rental values of the associated properties, which are all currently being let. The remaining €75,000 involved only routine repairs.

(iv) Outstanding rents in respect of March 2004 have been discovered, amounting to €25,000.

(v) On 1 April 2003 the company took up a finance lease, which will last for 5 years. The equipment leased had a fair value of €300,000. The only accounting entry so far made has been to include the first of the five annual lease payments of €75,000 in operating costs for 2003/04.

- **Requirement for question 4**

(a) Prepare the income and expenditure account for 2003/04. *9*

(b) Prepare the balance sheet as at 31 March 2004. *16*

***(25)***

# 5

The following trial balance has been prepared for a registered nursing home for the year ended 31 March 2003:

| | €000 | €000 |
|---|---|---|
| Income from activities | | 68,300 |
| Private patient income | | 4,200 |
| Salaries and wages | 42,750 | |
| Supplies and services | 15,950 | |
| Transport | 485 | |
| Premises | 970 | |
| Administration costs | 2,860 | |
| Interest receivable | | 245 |
| Land | 7,925 | |
| Buildings (NBV) | 48,950 | |
| Equipment – directly funded | 12,200 | |
| Equipment – donated | 1,700 | |
| Accumulated depreciation – directly funded | | 3,300 |
| Accumulated depreciation – donated | | 200 |
| Stock | 240 | |
| Debtors | 1,550 | |
| Cash | 160 | |
| Creditors | | 2,790 |
| Provisions for liabilities and charges | | 300 |
| Capitalisation account | | 49,080 |
| Revaluation reserve | | 5,740 |
| Donation reserve | | 1,500 |
| Retained surplus on I & E account | | 260 |
| Suspense account – capital expenditure | 285 | |
| Disposals | | 110 |
| | 136,025 | 136,025 |

**Additional information:**

(i) Depreciation has also yet to be charged for the year. Buildings have a remaining useful economic life of 40 years, while equipment depreciation is to be calculated using a standard life of 5 years.

(ii) On 1 April 2002 land and buildings were independently re-valued. Buildings were found to have increased by €1,450,000, while land values had been impaired by €125,000. The latter was due to a general market trend in the area. The adjustments are not yet reflected in the accounts.

(iii) Acquisitions financed in the year were limited to the purchase of equipment in February 2003. This has so far been recorded only in the suspense account. In addition, medical equipment valued at €85,000 was donated in March 2003, and this has not been recorded in the trial balance at all.

(iv) Equipment with a gross cost of €300,000 at 31 March 2002 was sold on 1 January 2003 for €110,000. This has so far been recorded only in the disposals account within the trial balance. The equipment had been purchased on 1 February 2002.

(v) The depreciation charges on an historical cost basis for 2002/03 have been calculated as:

| | €000 |
|---|---|
| Buildings | 1,160 |
| | |
| Depreciation policy: | |
| Directly Funded Equipment<br>Donated Equipment | 20% SL |

(vi) Additional private patient income in respect of 2002/03, which has yet to be invoiced, has been identified as €350,000.

- **Requirement for question 5**

(a) Prepare the income and expenditure account for 2002/03. *8*

(b) Prepare the balance sheet as at 31 March 2003. *17*

***(25)***

**SECTION D (Answer two questions)**

6

- **Requirement for question 6**

(a) Name two main sources of finance in each of the four key public sectors, ie central government, local government, health and education sectors. *5*

(b) With reference to accounting standards, compare and contrast the accounting treatment of a government grant in the private sector with that of a public service organisation of your choice. *10*

***(15)***

7

Define **specific** measures of financial performance, stating the method and purpose of each relevant measure, in:

- **Requirement for question 7**

(a) The private sector. *5*

(b) Central or local government. *5*

(c) Health Service. *5*

***(15)***

# 8

Identify, with reference to the degree of compliance with FRS 15, the treatment of appropriate categories of fixed assets on the balance sheet, including the approach taken to depreciation or capital charges, in each of the following sectors:

- **Requirement for question 8**

(a) Central government. *3*

(b) Local Government. *3*

(c) Draft a report to senior management identifying the benefits of asset accounting and how this could impact on cost of service provision, in a sector of your choice. *9*

***(15)***