

FINANCIAL REPORTING IN FURTHER AND HIGHER EDUCATION

Professional 2 examination 7 December 1999

From 10.00 am to 1.00 pm
plus ten minutes reading time from 9.50 am to 10.00 am.

Instructions to candidates

Answer **four** questions in total: **both** questions from Section **A**, and **two** questions from Section **B**. The marks available for each question are shown in italics in the right-hand margin.

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

SECTION A (Answer both questions)**1**

You have recently been appointed as Chief Financial Accountant at Robdown College, a Further Education college. The Director of Finance has shared his concerns with you about the performance of your predecessor. The accounts were rarely produced on time and on occasions they were found to include a number of mistakes which on one occasion proved to be exceedingly embarrassing to the Director of Finance.

The Director of Finance and yourself agree on a strategy for the rapid and accurate production of the Income and Expenditure account and the Balance Sheet, for the year ending 31 July 1999. A trial balance will be extracted to ensure the ledgers balance and there are no glaring omissions. You will then review the ledgers and produce the I & E account and Balance Sheet for the Director of Finance.

Trial Balance	£000
Staff	43,750
Operating Costs	29,750
Interest Charges	875
Fee and Grant income	61,250
Other income	14,000
Land	19,250
Building	31,500
Building depreciation	12,250
Equipment	10,500
Equipment depreciation	8,750
Stock	7,000
Debtors	14,000
Cash	175
Creditors	20,125
Provisions	1,750
Depreciation 1998/99	
Building	1,050
Equipment	700
Long Term Loan	14,000
Revaluation Revenue	2,100
I & E Revenue	24,325

You have investigated the financial ledger accounts and other financial and bank records. You were not surprised to find a number of transactions not yet included in the accounts. A summary of these omissions are detailed below.

- (i) Land surplus to requirements valued at £2.275 million in the books was sold in the last week of the financial year for £3.5 million. The land had originally cost £1.75 million. The transaction had not yet been recorded in the financial ledger. The gain from the sale should be appropriated to a capital reserve.

- (ii) The remaining land had been professionally valued at 31 July 1998 and was found to have increased in value by £1,575,000 (excluding the land sold during the year). The revaluation report was not actioned in the 1997/98 accounts. No formal revaluation had taken place since then, but local land prices are known to have risen by 0.4% since 31 July 1998.
- (iii) Investment income of £962,500 due on the 31 July had not been received.
- (iv) Capital expenditure of £5.25 million on equipment was financed as follows:

Revenue	£0.875 million
Finance Lease	£4.375 million

The Finance Lease is over 4 years at an annual rent of £1,400,000, with the first rental due 1 August 1999.

- (v) A loan had been raised to finance building work totalling £1,400,000. There was a delay, due to a technical computer fault, in receiving the cash from the bank. The treasury manager delayed payment to the contractor until the cash was credited to the college's bank account on the 4 August. The building work was not included in the accounts.

• **Requirement for question 1**

- (a) Prepare the Income and Expenditure account for the year ending 31 July 1999 and the balance sheet as at the same date. 15
- (b) Draft a note for the final accounts file for use by External Auditors, explaining your treatment of the various adjustments, identifying the accounting standard wherever possible 10

(25)

2

The Director of Finance at your institution has developed a good relationship with the members of the Finance Committee. In the last twelve months he has provided a number of training sessions and workshops for the Committee members so that they have a clearer understanding of the financial implications of their decisions.

The next workshop to take place is to focus on the Cash Flow statement included in the Annual Accounts. The Director of Finance discusses his ideas and intentions with you in your role as the Senior Financial Accountant. After a number of discussions it is agreed that you will produce the Cash Flow statement in the required format of the revised FRS1.

However, the next day the Director of Finance is taken ill and has to undergo an emergency operation and will be off work for several months.

It is agreed with the Chairman of the Finance Committee that, in the absence of the Director of Finance, you will both provide all the information promised and lead the workshop. You extract the following information from the financial ledgers and accounts:

Information	£
(i) Operating surplus for year	2,749,000
(ii) Loans - raised in year	5,925,000
- repaid in year	1,687,500
(iii) Capital Expenditure	
- Building	7,896,000
- Equipment	342,000
- Endowment Investment	4,050,000
(iv) Capital Receipts	
- Sale of Endowment assets	3,150,000
- Grants	562,500
- Endowments received	900,000
(v) Depreciation	2,334,000
(vi) Investment income	5,695,500
(vii) Interest payable	216,750
(viii) Working Capital Changes	
Stocks	+ 23,250
Debtors	+3,648,750
Creditors	+ 4,039,500
Investment income due	- 1,035,000

(ix) Deferred Capital grants of £15 million are being written off over a 10 year period.

(x) Taxation paid in relation to a college subsidiary totals £37,500.

(xi) Cash movements in the year with closing balances in brackets amount to:

- Endowment assets	+ £258,750	(£258,750)
- Other	+ £1,527,000	(£20,945,250)
- Overdraft	- £26,250	(£453,000)

(xii) Provisions set aside £1,025,250

• **Requirement for question 2**

- (a) Prepare the Cash Flow statement for the year including a reconciliation of surplus to cash flow from operations and an analysis of changes in net funds. 15
- (b) Draft a brief explanatory note for the Finance Committee members explaining the purpose of each section of the Cash Flow statement. 5
- (c) Comment briefly on the completed Cash Flow Statement. 5
- (25)

SECTION B (Answer two questions)**3**

Your Director of Finance has recently returned from a conference on quality and standards in the Further and Higher Education sector. Many of the speakers prefaced their remarks with comments such as 'I work in a centre of excellence...', 'My College is one of the best...', and other similar phrases. It struck him that many such comments were made with little or no supporting evidence.

On his return to work the Director of Finance discusses his thoughts with you as the Principal Management Accountant. He asks you to draft a report on his behalf for circulation to the senior management team on the concept of performance management. You are happy to do this as it links in well with your concerns with the performance of the catering function. The catering function comprises three separate units operating on a stand alone basis, about which you have recently collected the following information:

(i)

Annual Cost to 31 July 1999	Uptown Campus £	Midtown Campus £	Downtown Campus £
Food	242,640	35,000	647,600
Wages	195,600	45,000	405,200
Management	36,000	15,400	45,600
Crockery	9,360	2,802	20,634
Income from swill	(6,768)	(308)	(1,996)

(ii) **Stocks of Food**

1 August 1998	7,820	2,500	34,480
31 July 1999	7,720	1,960	43,280

(iii) Although managers are free to determine the menus in each unit, in constructing the budget the food budget was set at average of £1.30 per meal.

(iv) The number of meals at each campus for the year ending 31 July 1999 was as listed below:

Uptown Campus	193,004
Midtown Campus	26,068
Downtown Campus	477,190

(v) Overheads of £45,000 are allocated the Catering Department as a whole.

- **Requirement for question 3**

- (a) You are required to draft the report for the Director of Finance on the importance of performance measurement in your organisation. *15*
 - (b)
 - (i) Using the information given, comment on the performance of the catering service on each campus.
 - (ii) What other information would be required so that a more detailed assessment of the performance of the catering services on each campus can be undertaken? *10*
- (25)*

4

You and your business partner have recently retired from the medium-sized accountancy practise which you both established shortly after qualifying as accountants.

Both of you are looking forward to an active retirement and intend to contribute to public life in some form or other.

Your intentions are well known in the local community and you have had a number of offers from a variety of organisations who hope to draw on your significant financial experience. One offer you are excited by is joining the Board of either the local Further Education College or the local Higher Education Institute. There is a vacancy on both boards. This particular offer appeals to you both and you are giving it careful consideration.

As part of their consideration both partners reviewed the financial framework of each institution. They drew up a list of topics for which they required further clarification on the accounting/ financial/ managerial treatment. These are listed below:

Further Education

- Accounting for capital grants	<i>10</i>
- Provisions and contingencies	<i>8</i>
- Contents of Treasurers reports	<i>5</i>
- Accounting for European funds	<i>2</i>
	<i>(25)</i>

Higher Education

- Accounting for capital grants	<i>8</i>
- Inherited liabilities	<i>7</i>
- Corporate Governance	<i>6</i>
- Loans to third parties	<i>4</i>
	<i>(25)</i>

• **Requirement for question 4**

You are a financial expert in Further and Higher Education and have been asked to draw up briefing notes for ONE of these lists i.e **either** Further Education **or** Higher Education. *(25)*

5

You are the Deputy Director of Finance, and the Director of Finance asks you to prepare a paper for the next Management Team meeting on the principles and aims of budgetary control.

There has been considerable discussion in your institution since the announcement of a considerable financial deficit of several million pounds predicted in the coming financial year. The Management Team have been considering ways to address the deficit and it is rumoured the rescue package may include both voluntary and compulsory redundancies.

The deficit has come as a surprise to the vast majority of staff and a number of questions have been raised about the financial framework of the institution, in particular the budgetary control system. Many Heads of Departments have complained that they have been prevented from earning more income for the institution by a lack of resources and of being restrained by the amount of budget their departments have been allocated.

- **Requirement for question 5**

- (a) Critically analyse five main purposes of budgetary control and explain how these purposes can be met by a robust budgetary control system. 10
- (b) What are the principal differences between 'Bottom up' and a 'Top Down' approach to a budget construction and explain in what circumstances each method is more appropriate to use? 10
- (c) Profiling of budgets is not fully developed in many organisations. Explain the purpose and advantages of profiling of budgets. 5

(25)