FINANCIAL AND PERFORMANCE REPORTING
REPUBLIC OF IRELAND

Diploma Stage Examination

6 June 2006

MARKING SCHEME

AT THE HEART OF
YOUR CAREER

Question 1

(a) Income and Expenditure account

	€000	
Income		
Grants and subsidies	40,750	
Goods and services	91,509	
Local government fund – general purpose grant	40,383	
Rates	107,431	
Total Income	**280,073**	
Expenditure		
Payroll expenses	100,298	
Operational expenses 119,635 + 35 - 3375	116,295	*2*
Administration expenses	17,515	
Establishment expenses 13,127 + 40	13,167	*1*
Financial expenses 11,375 - 56	11,319	*1*
Miscellaneous Expenses	4,506	
Total expenditure	**263,100**	
Surplus/(deficit) for the year before transfers	**16,973**	
Transfer (to)/from reserves	**(56)**	*1*
Overall surplus	**16,917**	
General reserve 1/1/05	**32,523**	
General reserves 31/12/05	**49,440**	

Balance Sheet At 31 December 2005

	€000	€000	
Fixed assets			
Land		348,212	1/2
Buildings		290,467	1
Housing		1,006,049	1
Plant & machinery		8,821	2
		1,653,549	
Work in progress and preliminary expenses			
Long term debtors		219,711	
Current assets			
Stocks	94,067		1/2
Trade debtors & prepayments 28,298 – 35 + 1,640 - 581	29,322		2
Bank investments	0		
Cash at bank	0		
Cash on hand	2,516		1/2
	125,905		
Current liabilities (amounts falling due within one year)			
Bank overdraft	(962)		1/2
Creditors & accruals	(36,917)		1/2
Finance leases	(56)		1
	(37,935)		
Net current assets/(liabilities)		**87,970**	
Provisions for liabilities and charges		0	1
Creditors (amounts falling due after more than one year)			
Loans payable	(407,885)		
Finance leases	(728)		1
Other	0	(408,613)	
Net assets		**1,552,617**	
Financed by			
Capitalisation account		(1,653,549)	1
Income WIP		0	
Specific revenue reserve		(40)	1
General revenue reserve		(49,440)	
Other balances 150,468 - 56		150,412	1 ½
Total reserves		**1,552,617**	

(20)

Workings

1. Finance lease:

	DR	CR
Financial Expenses		60,000
Finance Lease	56,000	
Financial Expenses	4,000	
I+E Transfer to Other balances	56,000	
Lease repayment reserve		56,000

In terns of presentation, the balance on the Financial Lease needs to be broken down between current and long-term liabilities.

Opening Balance (per TB)	840,000
Less capital payment this year	(56,000)
Capital remaining	784,000

Current liabilities:	56,000
Long-term liabilities	728,000

2. Disposal of plant:

	DR	CR
Receipt:		
Establishment expenses	40,000	
Usable Capital Receipts (under specific rev. reserve		40,000
Disposal:		
Plant Fixed Asset		35,000
Capitalisation account	35,000	

3. Depreciation:

Land	Nil		348,212
Buildings	297,915 * 2.5%	7,448	290,467
Housing	1,047,968 * 4%	41,919	1,006,049
Plant	(10,059 - 35) * 12%	1,203	8,821
		50,570	1,653,549

	DR	**CR**
Individual Asset Account	X	
Capitalisation account		X

4. Bad debts:

Provision for Doubtful Debts as per Trial Balance		3,956
Provision for this year: Commercial Debtors	(14,563 – 35) * 4% =	581
Adjustment to I&E		3,375

Bad debt write-off: Note 6 is classed as an adjusting post balance sheet event.

5. Legal action:

As this is deemed to be a contingent asset and only probable, no provision is made but a note would be included in the accounts.

Question 2

DETAIL	DR	CR	
Note 1:			
Fixed Assets	500,000		
Capitalisation Account		500,000	
The capitalisation of the pathology lab			
Capital Income and Expenditure Account	500,000		
Bank		400,000	
Creditors		100,000	
The recording of bills paid and due			
Department of Health and Children grant account	500,000		
Capital Income and Expenditure Account		500,000	
The recording of HPO grant from DoHC			
Bank	350,000		
Department of Health and Children grant account		350,000	
Cash received from the DoHC in respect of the grant			
			4
Note 2:			
Fixed Assets	200,000		
Capitalisation Account		200,000	
The capitalisation of the scanner			
Capital Income and Expenditure Account	200,000		
Obligations under Finance Leases		200,000	
Deferred Finance Charges	50,000		
Obligations under Finance Leases		50,000	
The financing of the scanner			
Obligations under Finance Leases	50,000		
Capital I&E account – Income: Charge on Non-capital I&E account		40,000	
Deferred Finance Charges		10,000	
Non-capital I&E account	50,000		
Bank Account		50,000	
Recording of payment made to the leasing company			
Capitalisation account	40,000		
Fixed Assets		40,000	
Recording of the depreciation charge for the year			
			7
Note 3:			
Capitalisation Account	850,000		
Fixed Assets		850,000	
Recording the sale of the asset at book value			
Cash/Debtors	1,500,000		
Proceeds of Disposals Account		1,500,000	
Recording of the proceeds of the sale			

Proceeds of Disposals Account	19,820		
Cash/Debtors		19,820	
Recording of the expenses of the sale			
			3
Note 4:			
Fixed Assets	1,300,000		
Capitalisation Account		1,300,000	
The capitalisation of the asset purchased by trade-in			
Capital I&E account	1,300,000		
Cash		1,100,000	
Creditors		200,000	
Recording the purchase of the fixed assets			
Proceeds of Disposals Account	650,000		
Capital I&E Account under the heading Income: Proceeds of Disposals Account		650,000	
Recording the transfer of the funds from previous disposals to purchase the new asset			
			4

Note 5:
As per the code of practice, contingencies are not included in the AFS but are included as a note to the accounts. In the instance where litigation is involved the note will not contain data on the materiality or amount of the contingencies. In non-litigation contingencies, the nature, related uncertainties and the amount are disclosed.

2

(20)

Question 3

Working 1: Operating Profit

Retained earnings 2005-2004 = 7,746 – 8,000 =	(254)	
Add back tax due	770	
Add back interest due	350	
Operating profit	***866***	
		3

Working 2: Net flow from operating activities

Operating profit	866	
Add back depreciation	1,640	
Subtract profit on disposal	(50)	
Add back goodwill amortised	300	
Subtract government grants amortised	(500)	
Add decrease in stock	1,290	
Add decrease in debtors	174	
Add increase in creditors	720	
Net flow from operating activities	***4,440***	
		7

Working 3: Fixed Assets

Opening balance	9,760	
Additions	**3,580**	
Disposals	(500)	
Depreciation	(1,640)	
Revaluation	400	
Closing balance	11,600	
		6

Net cash inflow from operating activities		**4,440**	
Returns on investments and servicing of finance			
Interest paid		(350)	
Taxation		(800)	
Capital Expenditure			
Additions	(3,580)		
Disposal	550	(3,030)	
Financing			
Loan		(500)	
Net decrease in cash		**(240)**	
			4
			(20)

Question 4

Answer to be written in a report format 1

(a) Analysis of financial performance

Performance against the two set targets

Net margin:

	2004		2005
(250 / 9,400) x 100	3%	(-1,730 / 8,505) x 100	-20%

The target was met in 2004 but was missed significantly in 2005.

Income has decreased significantly and operating costs have increased significantly. (10% decrease in income, 11% increase in costs). Primarily grant income has drastically reduced.

1 mark for calculation of both year's ratios. Up to 1 ½ marks for comments on the performance. Both up to a maximum of 2 ½

Return on capital

	2004		2005
(250 / 11,390 X 100)	2%	(-1,730 / 9,115 X 100)	-19%

The target was missed in both years. The low levels of surpluses generated have resulted in the targets being missed.

Adjusting for the capital additions incurred, net assets have rapidly decreased and would therefore result in an even worse return on capital. (-1,730 / 7,115 x 100 = -24%) but the high deficit returned indicates that the intended additional income has not arisen from this investment yet.

1 mark for calculation of both year's ratios. Up to 1 ½ marks for comments on the performance. Both up to a maximum of 2 ½.

Use of other ratios

Liquidity is a clear problem for Funtime Leisure Management and creditors in particular have caused a significant problem:

		2004		2005
Current ratio	(690 / 2,390)	0.29:1	(395 / 3,710)	0.11:1
Quick ratio	(620 / 2,390)	0.26:1	(330 / 3,710)	0.09:1
Creditor days	(440 / 8,080 x 365)	20	(3,110 / 8,955 x 365)	127
Debtor days	(70 / 6,000 x 365)	4	(75 / 5,000 x 365)	5
Stock turnover	(75 / 8,080 x 365)	3	(65 / 8,955 x 365)	3

Creditor days have significantly increased compared with last year because of the payment of capital creditors. Not enough income (cash) may have been generated from the new capital expenditure to have financed this investment.

In this section students may answer using other appropriate financial ratios. Marks to be awarded on the basis of 1 mark for calculation of a ratio for both years, 1 mark for comments. Maximum of 5 marks for looking at other ratios

(10)

(b) Recommendations

Can further steps to secure more grant income be taken? (Although be aware that this may lead to additional costs as well).

Either costs need to be saved or more income needs to be generated to help improve performance against the targets set and to generate more cash.

More work is needed to understand the extent to which income generation is successful – e.g. by separately identifying costs related to the catering income received.

Can we promote greater take up of annual passes to ensure that cash can be received in advance?

Can more loans be taken out as a temporary measure to pay off suppliers? (Although debt: equity ratios suggest that this may not be possible as there is already a high level of debt compared with equity. (56% for 2005, up from 50%.)

Other valid recommendations should attract credit. Recommendations to be marked on the basis of 1 mark per recommendation explained to a maximum of 5.

(c) Recommendation for awarding management of 2 new leisure centres.

Based on the financial standing of Funtime Leisure Management it would seem unwise to award the management of the two new leisure centres. (Although note comments on limitations below).

Student recommendations should be based on their analysis Recommendations That are based on their findings should be awarded credit as appropriate. Up to a maximum of 2.

(d) Limitations of the review

We do not have complete financial statements for Funtime Management. Having a full cash flow statement or more detailed financial statements (ie a breakdown of costs) would provide better information.

The review only considers financial performance – information on non-financial performance is essential in gaining a more holistic view of Funtime's performance. Reference could be made here to LA suite of performance indicators.

We only have two year's data on which to assess financial performance. Performance in the early stages of any organisation, public or private, is often inconsistent and it may be more beneficial to assess the company on 4 years data before making a conclusive decision.

Other appropriate comments to attract credit.
1 mark per point explained to a maximum of 3.

(20)

Question 5

(a) Users of private and public sector financial statements

Users of private sector statements

The ASB sets out seven groups of users of private sector financial statements:

Users	Information they may be interested in
Investors'	Extent to which shareholder wealth has increased, earnings per share / growth in profit attributable to shareholders
Lenders	The long term solvency and short term liquidity of the organisation in assessing if borrowings will be repaid
Suppliers	The short term liquidity of the organisation. Creditor days. Assessing if supplies made will be paid.
Customers	The viability/ stability of the organisation determined through liquidity measures and profitability measures. Profit margins could be used to indicate the value/ quality of a product.
The Public	Will depend on their relationship with the organisation as often the public fall into one of the other categories too.
Government and other agencies	Profitability and financial solvency may be used to assess the general health of the company as a way of assessing the general economy. May also use the financial statements in a regulatory role e.g. through assessing if profit figures relate to tax paid

1 mark per private sector user + information requirements to a maximum of 6

Users of public sector financial statements

Users of public sector financial statements will follow the same broad categories of those in the private sector too except that investors' will be stakeholders, customers will be service users.

Typically public sector financial statements have a greater number of users interested in them. For example users could include partners, funders (ie for grants), the media and other public interest/ pressure groups and regulators.

In addition to the information that the users of private sector financial statements are interested in, the users of public sector financial statements will also be interested in whether public money has been spent wisely (i.e. can the organisation demonstrate accountability and stewardship for the funding it has received) and if value for money has been offered. Profit or notions of increasing shareholder wealth are not relevant.

1 mark per valid comment on public sector users+ information requirements to a maximum of 4

(10)

(b) Government Department Versus Private Sector Companies

Governing legislation requires that both types of entity produce completely different reports. Companies' financial statements focus on reporting profit and increases to shareholder wealth. These objectives are not relevant to the public sector whereas demonstrating financial stewardship and value for money are relevant. *2*

Companies produce Financial Statements as per the requirements of the Companies Acts and in line with regulations as per GAAP. Government departments produce Appropriation Accounts in line with the Public Financial Procedures and circulars issued by the Department of Finance. *2*

Financial information is prepared on the accruals basis for Companies. Because GAAP is based on the accruals concept, companies can easily apply GAAP regulations to their reporting procedures. However, because Government Departments still account on a cash basis it is not possible to apply GAAP to the production of their appropriation accounts. This makes the statements produced by both companies and government departments incomparable. *2*

Government departments operate on a cash basis, as have all public sector organisations in the past. The Appropriation accounts are cash based but there are accompanying notes that include some information prepared on the accruals basis. The appropriation accounts consist of a statement of expenditure under sub headings, highlighting estimates, outturn and closing accruals. As a note there is also an operating statement, a statement of assets and liabilities and a statement of Capital Assets. *2*

Limited companies produce a Profit and Loss, a Balance Sheet, a Cashflow and a Statement of Total Recognised Gains and Losses. Many notes providing extra information to the shareholder to assist in making investment decisions accompany these. *2*

Other valid points attract credit.
(10)

(20)

Question 6

(a) Key stages of reform

This question is of essay style and the topic under question is very broad. This solution is a guide to the key points that are involved but students will be awarded marks for all relevant and well-supported points addressed

Modernisation programme:
Strategic Management Initiative
Delivering Better Government
Evaluation of the Progress of the SMI/DBG in the Civil Service – Capita Consulting Report

3

Local Government
Better Local Government
Modernising Local Government
Delivering Value for People: Service Indicators for LA's

3

Health Service
Health Amendment Act 1996
Value for Money Audit: Deloitte and Touche
The Health Service Reform Programme
The Brennan Report: Commission on Financial Management and Control Systems in the Health Service *4*

Other valid points attract credit.
(10)

(b) The International Experience

The UK: Candidates should address the Resource Accounting and Budgeting programme (RAB) leading to the Whole of Government Accounts initiative.

New Zealand: The New Zealand experience of Financial and Performance Reporting reform is the main international model as the reform programme began in the late 80's and much evidence is now available on the outcomes of the reform programme.

Other countries that may be discussed are Chilli, France, the US

Other valid points attract credit.
(5)

(c) The future of Financial and Performance Reporting in the Irish public services

<u>Central Government:</u> The key issue is the rollout of full accrual accounting. The pilot project in the Department of Public Enterprise and the Capita Consulting report on same are evidence of how this can be successful and possible. The implementation of MIF systems also support this future change. The change in reporting focus from cash spent to service delivered will also have a significant impact on the format of reports produced.

Local Government: The key challenges for Local Government involve the development of their code of practice more in line with GAAP. The potential issue of the introduction of IFRS' or IPSASB may need to be addressed although this is very much dependent on both EU regulations and Government Legislation. Currently much of the focus is on the presentation on management information e.g. Performance Indicators.

Health Services: The future of Health Sector Financial and Performance Reporting will depend on how the structure of the HSE develops. Current reporting procedures are based on the Health Board structures and policies as prescribed by the Department of Health although the HSE have been passed the responsibility for the development of these procedures. As with the Local Authorities, accrual accounting is being used in the Health Service but the adoption of GAAP is very limited and some key issues need to be addressed such as the treatment of contingencies and fixed assets.

Other valid points attract credit.
(5)

(20)