

FINANCIAL REPORTING IN CENTRAL GOVERNMENT AND AGENCIES

Professional 2
December 1999

MARKING SCHEME

The logo for CIPFA (Chartered Institute of Public Finance and Accountancy) features the letters 'CIPFA' in a serif font. The letter 'P' is stylized with a large, elegant flourish that loops over the top of the 'I' and extends to the right.

Question 1

(a) Income and Expenditure Account

Working 1 - Depreciation

1,887	+	$((12 \times 5) / 5)$	=	1,899	
Trial Balance		vehicles			1/2

Income and Expenditure Account for the Specialised Construction Agency for year ended 31 March 1999

	£000	£000	
Turnover	244,287		
Changes in stocks (£27,216-£29,823 - 1 mark)	<u>(2,607)</u>		
		241,680	2
Consumables (£24,783+£138 - 1 mark)	(24,921)		
Staff Costs	(33,816)		
Depreciation (W1) -1 mark)	(1,899)		
Other Charges	(179,014)	<u>(239,650)</u>	2
Operating Profit		2,030	2
Interest Receivable		737	
Interest Payable		<u>(2,134)</u>	
Profit for Year		633	2
Retained Profit B/f		<u>10,553</u>	
Retained Profit C/f		<u>11,166</u>	2

*2 marks for presentation
(15)*

Balance Sheet of the Specialised Construction Agency as at 31 March 1999

FRS 12 – Provisions and Contingent Liabilities is effective ?? financial statements ending on of after 23 March 1999. This question and marking scheme does not address the FRS 12.

	£000	£000	
Fixed Assets		38,082	
(note 2&5 £38,098+60-76) - 1 mark			
<u>Current Assets</u>			
Stock	27,216		
Debtors	40,638		
Cash	<u>1,866</u>		
	69,720		1
<u>Current Liabilities</u>			
Creditors (amounts falling due within one year)	(49,013)		
Contract charges paid in advance (note 3 £24x0.75)	<u>(18)</u>		1
Net Current Assets		<u>20,689</u>	1
		<u>58,771</u>	½
Financed By:			
<u>Provision for Liabilities and Charges</u>			
Insurance Provision		4,554	
Contingent Liability – 1 mark (note 4)		74	
Long Term Loan		26,678	
Revaluation (£16,375-76) – 1 mark (note 5)		16,299	
Income & Expenditure Account		<u>11,166</u>	1
		<u>58,771</u>	½

2 marks for presentation

(10)

Question 2

(a)

Calculation of the net cash outflow from activities

	£000	
Operating deficit	(7,976)	
<i>plus</i>		
Charges not involving cash movements		
Add: depreciation	2,070	<i>1/2</i>
Add: notional charges (2,898+172)	3,070	<i>1/2</i>
Less: reduction in bad debt provision	(48)	<i>1/2</i>
Less: gain on disposal of assets	(186)	<i>1/2</i>
<i>plus/less</i>		
Movements in revenue accruals adjustments		
decrease in stock (3,795-3,558)	237	<i>1/2</i>
increase in debtors (5,658-6,831)	(1,173)	<i>1/2</i>
increase in creditors (4,554-2,898)	(1,656)	<i>1/2</i>
Net cash outflow from revenue activities	(5,662)	

Movement in cash and equivalents

	1 April 1998	31 March 1999	Movement	
	£000	£000	£000	
Cash	2,745	3,120	375	<i>1/2</i>

1 mark for presentation
(5)

(b)

Parliamentary grant received reconciled to the Appropriation Account for the Vote

Reconciliation	£000	£000	
Gross Parliamentary grant		51,060	
Appropriations in aid		(43,470)	
Net Parliamentary grant voted		7,590	<i>1</i>
Excess of Parliamentary grant over actual expenditure	(1,070)		<i>1</i>
Excess of Appropriations in aid (43,470-42,435)	1,035		<i>1</i>
		(35)	
Net Parliamentary grant received		7,555	<i>1/2</i>
The grant was utilised to finance			
- net cash outflow from operating activities		5,662	<i>1/2</i>
- net capital expenditure (1,863-345)		1,518	<i>1/2</i>
Increase in cash		375	<i>1/2</i>
			<i>(5)</i>

(c)

**Urban Regeneration Agency Cash Flow Statement
for the Year Ending 31 March 1999**

Cash Flows	£000	£000	
Net cash outflow from operating activities		(5,662)	1
Investing activities			
Purchase of fixed assets	(1,863)		1/2
<i>less</i>			
receipts from sale of fixed assets	345		1/2
Net cash outflow from investing activities		(1,518)	1/2
Net cash outflow before financing		(7,180)	1/2
Financing			
Net vote expenditure appropriated in the year		7,555	1/2
Increase in cash and equivalents		375	1/2
			<i>I mark for presentation</i>
			(5)

(d)

- essential element of the information required for accounts to give a true and fair view; 2
 - provides information that assists in the assessment of liquidity, solvency and financial adaptability; 2
 - greater visibility in the analysis of the reporting entity's inflows and outflows of cash; 2
 - facilitates comparison of the cash flow performances of different organisations. 1
 - the classification of cash flow in accordance with the substance of the transaction or event giving rise to it, provides consistent treatment across all the primary statements; 1
 - distinguishes cash flows for investing to maintain the business from cash flows for investing to expand the business; 1
 - allows users to understand the effect on cash flows of items shown as exceptional or extraordinary in the profit and loss account; 1
- (10)
- (25)

This question does not include reporting changes arising due to FRS 12.

Question 3

(a) **A Labour**

- high number of hours worked by Central and South suggests that overtime has been worked – need to consider the impact of overtime on costs and output – efficiency issue; 1

- absenteeism levels in Central and South are significant. The underlying causes must be investigated – the small staff numbers mean that one employee on long term sick leave could skew the figures - is the higher number of hours worked at Central and South a factor in the level of absenteeism – stress, fatigue, malingering?; 1

B Other Costs

- running costs are generally quite low in relation to total costs. However total costs are significantly impacted by any overtime costs; 1/2

C Output

- output of licenses good in relation to North, but lower than South – in relation to the level of hours worked, labour costs have proved less cost-effective for Central than South – need to examine overtime policy and output targets; 1/2

- output per person is worrying, with Central achieving 68% of the output per person of South in relation to licenses, and 85% of the output of vehicle registrations; 1

D Income

- South generating more license income despite smaller staff numbers and lower staff costs. Central's income matches North, who operate with 67% of Central's staffing level and having worked 70% of Central's hours - North, despite smallest staff and working hours, achieves the best ratio of operating surplus to income – 85%; 1/2

- More income is generated from vehicle registrations, so staff resources should be targeted in this direction, increasing the volume of registration applications per hour, and so to generate a greater return per staff hour; 1/2

Central generates substantially higher levels of income per member of staff, but this is offset by higher staff costs. Staff costs are 23% higher than South and 60% higher than North. Efficiency/VFM balance must be struck between number (and cost) of hours worked and additional revenue generated; 1

E Unit Costs

- cost per license/registration processed is consistently higher at Central - £0.78 return, or 6.5%, achieved per £12 license processed in comparison with a 34/35% return made by the other two divisions; *1*
- the contrast is greater with the return on cost of vehicle registration processed, with Central's costs being £4 higher than the processing cost at North; *1*

F Admin

- payment of invoices is poor in all divisions, particularly South. Tardy payment risks interest charges from suppliers and higher costs; *1*
- Central's response to written complaints is very poor, with only 77% being responded to within target compared to 97% being within target in North; *1*
- This information is worrying when compared to the high error rate in Central, double that of South and seven times greater than North. Again raises questions regarding the cost effectiveness of the additional hours worked and staff costs; *1*
- The error rate may be due to the high staff turnover of 40% per annum, with average tenure in post of three years; *1*
- need to investigate the underlying causes of absenteeism, turnover and errors – is ten days training per person per year enough, are there other management/morale problems; *1*
- it would be useful to compare this year's performance with previous years' data, to determine if any decline in performance is apparent, and the nature of overall trends; *1*
- computer down time is too high across all divisions. Is this due to inadequate training/experience, or is it purely a system problem; *1/2*
- do the low running costs suggest inadequate maintenance is being carried out, and does the system need replaced/upgraded with the associated cost. *1/2*

(15)

(b)

- the OPA is a published statement which accompanies the annual report and resource accounts of the parent department of the agency; 2
- b
- the OPA summarises the department's aim, key objectives, agreed outputs and performance targets for the year; 2
- the statement reports on the outputs produced and value for money achieved in the utilisation of the resources allocated to the department during the financial year, and progress made toward the achievement of the department's longer term objectives and aim; 2
- the OPA represents the summary or highest level in the performance measurement and reporting structure of the department and its agencies while the agency's performance indicators report is a more detailed management information report for operational and short term planning purposes, and is focused on the operational requirements of the agency; 2
- there should be a clear relationship between the detailed information produced in the operational performance indicator report and the strategic published OPA. 2

(10)

(25)

Question 4

Response to Mr B Bottomline

Capital Charges – Cost of capital

- recognises opportunity cost of investing capital in assets; *1*
- recognises true cost of borrowing, removing concept of “free good” capital within Government; *1½*
- illustrates full cost of operations; *1*
- facilitates comparison with other bodies, including the private sector. *1*

Rate of Return

- rates specified by HM Treasury, as Government does not borrow commercially or is required to make a return for shareholders/investors; *1*
- charged at Treasury rate of return of 6% for non-commercial operations, or 8% for trading operations. *1*

Accountability and Stewardship

- private sector companies are accountable to the shareholders and Board of Directors; *1*
- stewardship relates to the capital and assets of the enterprise, and the rate of return achieved; *1*
- public sector organisations are accountable to a wide range of interested groups, including the public, elected members and Parliament; *1*
- stewardship relates to the use of public funds. *1*

Drivers for Efficiency and Effectiveness

- wide range of Government initiatives promoting the three Es and VFM, from FMI, Next Steps, Competing for Quality, Citizens’ Charter to Resource Accounting and Budgeting (RAB); *1½*
- the New Fiscal Rules (and RAB) link departmental funding to the achievement of pre-agreed outputs and targets, and articulated through documents such as the Public Service Agreement and the Departmental Investment Strategy; *1½*
- agency business plans and reports set out and report on performance targets to be achieved. *1*

Standards, Guidelines, Accounting Methodology, Competition

- RAB introduced commercial accounting techniques, such as accruals accounting and capital accounting concepts, which agencies currently operate; *1*
- the reporting emphasis is now on resources consumed, outputs produced, and the achievement of objectives; *1½*

- Central Government follows UK GAAP, which includes SSAPs, FRSs, SORPs, etc; *1*
- Allows greater comparison with private sector, providing greater transparency in assessment of efficiency and the competition for delivery of services. *1*

Short-term attitude to use of funds

- New Fiscal Rules sets three year Departmental Expenditure Limit (DEL); *1½*
- DEL is linked to the delivery of agreed outputs and achievement of performance targets; *1½*
- RAB (and OPA) focuses on outputs achieved rather than resources consumed; *1½*
- Golden Rules limits borrowing for investment in infrastructure. *1½*

(25)

Question 5

- (a)
- comes into force for accounting periods ending on or after 23 March 2000; *1½*
 - supersedes SSAP 12, Accounting for Depreciation; *1½*
 - sets out the principles of accounting for the initial measurement, valuation and depreciation of tangible fixed assets, with the exception of investment properties which continue to be accounted for in accordance with SSAP 19; *1½*
 - aims to prevent “cherry picking” in the choice of assets to be revalued and the frequency of the revaluation. *1½*

Objectives of the FRS:

- ensure consistent principles are applied to the initial measurement of tangible fixed assets; *2*
- ensure that the revaluation of fixed assets is performed on a consistent basis and kept up to date, and that gains and losses on revaluation are recognised on a consistent basis; *2*
- ensure that depreciation of tangible fixed assets is calculated in a consistent manner and recognised as the economic benefits are consumed over the assets’ useful economic lives; *2*
- ensure that sufficient information is disclosed in the financial statements to enable users to understand the impact of the entity’s accounting policies regarding initial measurement, valuation and depreciation of tangible fixed assets on the financial position and performance of the entity. *2*

- (b)
- cash accounting records capital only when spent, and no account is taken of asset while in use or sold; *1*
 - RAB allocates cost of providing capital over its expected useful life, with the opportunity to charge directly on this basis; *1*
 - RAB and capital charging improves the quality of decision making on new capital investment and the use of existing capital assets; *1½*
 - Focus on the desirable balance between capital and current expenditure. *1½*

- (c)
- decisions on investments and assets taken on the basis of what delivers the public interest; *1½*
 - sets out in detail how the resources allocated to finance public or privately financed investment in the Comprehensive Spending Review will be managed to deliver the department’s objectives, provide VFM and ensure positive social returns; *1½*
 - DIS used to support future bids and allocations; *1½*
 - Departmental appraisal, management and evaluation systems must support capital investment decision making process. *1½*

(25)