

FINANCIAL REPORTING IN CENTRAL GOVERNMENT AND AGENCIES

Professional 2 examination 5 June 2001

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**

The following information has been extracted from the accounts of the Information Technology Research and Development Agency for the 2000/2001 financial year. The agency is a trading fund of the Department of Technology and undertakes commercial research work in addition to performing a number of statutory functions on behalf of the parent department.

**The Information Technology Research and Development Agency
Trial Balance as at 31 March 2001**

Category	£000
Fixed assets (at valuation)	117,860
Accumulated depreciation	28,360
Turnover	81,265
Stock at 31 March 2000	4,406
Research funding grants	16,412
Interest payable	1,442
Interest receivable	1,005
Retained profits at 31 March 2000	20,478
Loans from National Loans Fund	24,600
Consumables	12,990
Other operating charges	7,829
Staff costs	49,077
Debtors	14,750
Cash at bank and in hand	8,377
Creditors	8,974
Revaluation reserve	40,262
Deferred development expenditure	4,700
Suspense account (cr)	75

Additional information

The following information has yet to be reflected in the accounts of the Agency:

- (i) Deferred development expenditure relates to three projects:

Project	Original deferred expenditure	Estimated income stream	Remaining deferred expenditure
HAL 2001	£2,760,000	15 years	£920,000
SAL 3001	£4,450,000	10 years	£1,780,000
GAL 4001	£5,000,000	5 years	£2,000,000

It is the agency's policy to write off deferred development expenditure in equal instalments over the length of the estimated income stream relating to that project. In November 2000, the HAL 2001 voice recognition system was superseded by a commercially developed rival. It is unlikely that the Agency will receive any more income from sales of this system.

- (ii) During the year, the agency sold scientific equipment which had a gross book value at 1 April 2000 of £400,000. The equipment had a written down value of £195,000, and sales proceeds amounted to £75,000 which was credited to the suspense account. The original cost of the equipment was £300,000. The Agency's policy on depreciation is to charge a full year's depreciation in the year of acquisition; no depreciation is charged in the year of disposal.

- (iii) Of the amount shown in the trial balance for research grants, £3,400,000 relates to a grant from a private sector company to undertake a long term research programme. The programme is scheduled to commence in September 2001, when a dedicated team will be established for that purpose.
- (iv) After taking account of disposals, the annual indexation of fixed assets has led to an increase in value of £4,475,000. The depreciation charge for the year has been calculated at £6,025,000. Backlog depreciation amounts to £125,000.
- (v) Closing stock at 31 March 2001 was £5,092,000.

• **Requirement for question 1**

Prepare the following from the above information:

- (a) The income and expenditure account for the Information Technology Research and Development Agency for the year ended 31 March 2001. *10*
- (b) The balance sheet for the Information Technology Research and Development Agency for the year ended 31 March 2001. *15*
- NB. All calculations should be rounded to the nearest £000. *(25)*

2

The following information has been extracted from the accounts of the Animal Welfare Agency (an on-Vote Executive Agency of the Ministry of Agriculture, Fisheries and Food) for the year 2000/2001:

- (i) The deficit shown in the operating account for the year amounted to £7,397,000.
- (ii) The operating account included the following transactions:
- depreciation of £470,000;
 - loss on disposal of assets of £127,000;
 - return on capital employed of £592,000;
 - insurance of £150,000; and
 - audit fee of £30,000.
- (iii) Expenditure for the year on new fixed assets totalled £150,000. The sale of fixed assets raised £30,000.
- (iv) The Gross Supply Grant voted by Parliament for the Agency for 2000/2001 was £12,660,000. Appropriations in aid of £7,900,000 were authorised; A-in-A realised amounted to £8,110,000. The surplus on the Vote to be surrendered for the year amounted to £276,000.
- (v) The working capital balances at the beginning and the end of the year were as follows:

	1 April 2000	31 March 2001
	£000	£000
Debtors	3,720	2,981
Creditors	1,704	1,811
Cash	1,619	591

• **Requirement for question 2**

Using the above information in respect of the Animal Welfare Agency:

- (a) Prepare the note to determine the net cash flow from activities and the movement in cash and equivalents for the year ended 31 March 2001; 6
- (b) Prepare the note to show the net Parliamentary grant received reconciled to the Appropriation Account for the Vote; 6
- (c) Prepare the cash flow statement for the year; and 8
- (d) Briefly explain the main categories of cash flows included in a cash flow statement. 5

(25)

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

The following information relates to the Department for Rural Regeneration.

- (i) The Department's ambit is to provide support to economically deprived rural areas and their inhabitants. This is achieved primarily through the secondment of government advisors to local regeneration projects and also by the granting of financial awards in support of the running costs of approved schemes. The Department's 2000/2001 estimate details for expenditure are:

	£
Running costs	5,789,000
Other current costs	2,391,000
Capital spending	892,000
Awards	4,780,000
	<u>13,852,000</u>

- (ii) For 2000/2001 the Department received a gross vote of £13,852,000 (net vote £13,040,000). Its vote on account was £4,900,000. In December 2000 the Department was given a reduced cash-limit of £12,900,000 for the year.
- (iii) Opening balances on 1 April 2000:
- debit of £375,000 in the paymaster's account;
 - debit of £62,000 in the sub-accountants' account;
 - debit of £376,000 in the consolidated fund;
 - the above offset by a credit balance in the Parliamentary Grant Account for a 1999/2000 underspend.

Treasury have instructed the Department that the surplus to be surrendered on the 1999/2000 account is to be dealt with by writing off the undrawn balance on the Consolidated Fund. The remainder is to be written off from the 2000/2001 supply grant.

- (iv) Paymaster statements show that of the £13,665,000 worth of payable orders issued during the year, £13,215,000 had been encashed by 31 March 2001. The orders issued were:

	£
Running costs	5,397,000
Other current costs	2,033,000
Capital spending	890,000
Awards	4,491,000
Sub accountants	854,000
	<u>13,665,000</u>

Paymaster statements show that two payable orders issued during 2000/2001 have expired without being presented – one for an award of £71,000 and one for current costs of £49,000.

- (v) Recent audit work by the NAO, in preparation for the certification of the 2000/2001 accounts, has identified a payable order for £66,000 that was recorded as awards but should have been recorded as running costs.
- (vi) During the year the Department collected cash authorised for use as appropriations in aid of £972,000. No other cash was collected.
- (vii) Grant drawn down during the year was £12,328,000. No money had been surrendered to the Consolidated Fund at 31 March 2001.
- (viii) Sub-account expenditure during the year was:

	£
Running costs	634,000

Awards 268,000

• **Requirement for question 3**

- (a) Prepare the ledger account entries for these transactions; 10
- (b) Prepare the statement of liabilities and assets as at 31 March 2001 and explain briefly what each balance means; 4
- (c) Prepare the appropriation account for the Department for the year ended 31 March 2001; 6
- (d) What are the main changes to the format of central government accounts which will be brought about as a result of the move to Resource Accounting? 5

(25)

4

You have recently been appointed to the finance department of a comparatively new central government Department. The Head of Finance also took up post recently. She is particularly interested in establishing a sound system of internal financial reporting and has asked you to take the lead in drafting a series of strategy papers on this subject. She has sent you a memo setting out the requirements for the first of these.

From: Head of Finance
To: Financial Accountant
Subject: Systems of Internal Financial Reporting

I appreciate that neither of us has been in post for very long but I hope you agree with me that there is an urgent need to review our internal reporting systems. As far as I can see they have not been reviewed since the Department was created some 5 years ago. We need to make sure that they are still capable of delivering what is required.

What with periodic spending reviews and such, we need to make sure that not only does everyone understand the need to control costs and stick to budgets, but that we also have the systems in place to enable our people to achieve this. Our recent performance in this regard has not been good and problems seem to have a habit of creeping up on us unawares.

Perhaps you can put your mind to addressing these two issues – understanding the need for control and the design of appropriate systems – and come up with a paper which sets out the issues involved.

Requirement for question 4

Prepare a briefing note for the Head of Finance which can, if needed, be circulated to heads of divisions within the Department. Marks will be awarded for the following:

- | | | |
|-----|---|------|
| (a) | Format, introductory and concluding remarks; | 3 |
| (b) | Identifying factors which have made the monitoring of financial information more important in Central Government and outlining the implications of each for internal reporting systems; | 8 |
| (c) | Listing the uses to which financial information is put within Central Government; | 3 |
| (d) | Identifying the characteristics of good information in general; and | 3 |
| (e) | Identifying particular types of internal financial monitoring techniques which may be used to produce effective budgetary control, explaining briefly the use of each. | 8 |
| | | (25) |

5 You are a part-qualified accountant seconded to the office of the Chief Executive of an off-Vote government trading fund. A recently appointed non-executive director has written to the Chief Executive requesting information on various aspects of the Agency's financial accounting and reporting regime. Your Chief Executive has asked you to draft a reply to the following memo.

MEMORANDUM

To: Steven Quirel, Chief Executive
From: Graham Branch, Non-Executive Director
Date: 5 June 2001

Subject: Funding and Accountability Issues

At our last board meeting, funding and accountability issues relating to the Agency were briefly discussed. I gained the impression that our main source of funding was our parent department and that the Annual Report was our main means of being held accountable for how we spend our money.

However, I am sure the story is more complicated than this and would greatly appreciate some further guidance. Specifically, would you be able to elaborate on the following:

On the funds flow issue, what are our main sources of *revenue* funds? Do we get some sort of running costs grant from the department like the NDPB I used to be a member of?

Does capital funding come by the same route as revenue funding? If not, could you explain how the Agency obtains buildings and equipment and the like?

I notice from the annual report and accounts that we have something called Public Dividend Capital. Does this mean we have to pay dividends to shareholders? Is that what the six per cent rate of return I keep hearing about is?

Concerning accountability, could you explain exactly what should be included within the Agency's annual accounts? (I understand that there are a number of sources of guidance on this matter.) Who decides what form our accounts should be in?

I am also sure that there are ways, other than the Annual Report, in which we are held accountable for the use of public resources. Could you explain all the ways in which we, as a Trading Fund, are held accountable for the funds we control?

I'm not an accountant of any sort so if you could keep your answers in plain English I would be grateful. Many thanks for your help in this matter.

- **Requirement for question 5**

Draft a response to the above memo which addresses the above queries as clearly as possible. Specifically:

- (a) Describe how revenue funds are obtained by the Trading Fund. 3
- (b) Explain the different ways in which capital assets may be financed by the Agency. 4
- (c) Explain the status of public dividend capital and the rate of return referred to in the Agency's annual report and accounts. 8
- (d) Identify the main items which should be present within the annual financial statements. State the sources of guidance on format, including relevant legislation and directions, and who is responsible for stipulating the format of accounts. 6
- (e) Explain how the agency is monitored in year, and describe ways other than the Annual Report in which they are held accountable. 4

(25)