

FINANCIAL REPORTING IN FURTHER AND HIGHER EDUCATION

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 balances have been extracted from the ledgers of Outwood College at 31 July 2000:

A. College	£000
Income and expenditure account (Cr) (at 1 August 1999)	1,360
Land (at valuation 31 July 1999)	14,750
Buildings (at valuation 31 July 1999)	36,250
Equipment and machinery (at cost)	6,400
Buildings depreciation (at 1 August 1999)	21,450
Equipment and machinery depreciation (at 1 August 1999)	2,975
Staff costs	12,800
Operating costs	4,839
Income from fees and grants	18,368
Investment income	108
Other income	3,617
Interest (Dr)	845
Investments (long term)	2,175
Stock (at 1 August 1999)	1,237
Debtors	4,735
Creditors (all payable during 2000/01)	5,137
Revaluation reserve	16,000
Long term loans	14,500
Bank (Cr)	166
Suspense account (Cr)	350
B. OCT Ltd	
Revenue reserve (Cr) (at 1 August 1999)	100
Land (at valuation 31 July 1999)	250
Buildings (at valuation 31 July 1999)	500
Buildings depreciation (at 1 August 1999)	120
Fees and charges	2,300
Staff costs	1,200
Other operating costs	540
Debtors	310
Bank (Dr)	150
Creditors (all payable during 2000/01)	180
Share capital (issued ordinary shares @ 25p each)	100
Revaluation reserve	150

Additional information:

- (i) The college's investments include 400,000 shares in OCT Ltd which were acquired at par when OCT Ltd was established. OCT Ltd (Outwood College Trading Ltd) was set up by the college some years ago to generate profits from a range of trading activities.
- (ii) The suspense account comprises the proceeds of the sale of fixed assets during the year. Land owned by the college and valued at £310,000 was sold to a developer for £342,000; equipment with a net book value of £20,000 (cost £60,000) was sold for £8,000. The only entries recorded in the ledger related to the sale proceeds in the bank and suspense accounts. The land owned by the college was valued at £15,600,000 on 31 July 2000; the buildings owned by the college were revalued on the same date and should be increased by 8%. The land and buildings owned by OCT Ltd are to be revalued by 10% on 31 July 2000.
- (iii) Depreciation in respect of the year ended 31 July 2000 should be provided on a straight line basis for (a) buildings based on most recent valuation over 50 years and (b) equipment and machinery based on cost over 10 years. In all cases residual values are ignored. It is college policy to charge a full year's depreciation in the year of acquisition and none in the year of disposal.
- (iv) College stocks at 31 July 2000 were valued at cost amounting to £1,140,000. However, this amount includes catering and stationery stocks which had been damaged in floods in late July. These stocks which originally cost £47,000 had subsequently sold in August to local farmers for swill and to a recycling firm for a total of £2,000.

- (v) On 1 August 1999 Outwood College entered into a lease agreement with Outwood Finance Ltd in respect of the supply and installation of machinery in the college's Engineering Faculty. The fair value of the machinery was £300,000 and the college made the first of ten annual lease payments of £41,000 on 31 July 2000. The only entries in the ledger have been to record the payment of £41,000 in the bank account and in operating costs. Under the terms of the lease, the college is responsible for maintaining the machinery which is expected to be scrapped at the end of the lease period.
- (vi) In June 2000 the college received a claim from a student for compensation for injuries sustained as a result of a scientific experiment which went tragically wrong. In early August the college received legal advice that it would probably be liable to pay compensation in the region of £50,000.
- (vii) At the beginning of August 2000 pay negotiations were concluded for a pay award which was backdated to 1 May 2000. It was estimated that the full year effect would be to increase staff costs by 3% in a full year.
- (viii) It is estimated that OCT Ltd's corporation tax charge for 1999/2000 will be £12,000.
- (ix) After the college's financial statements for the year ended 31 July 1999 had been approved and published, a material error had been found which meant that the debtors for fee income had been understated by £250,000. No adjustment has yet been made in respect of this error.

- **Requirement for question 1**

Prepare the consolidated income and expenditure account of Outwood College for the year ended 31 July 2000, together with the consolidated balance sheet as at that date.

(25)

2

The following information relates to the financial statements of Godstone University in respect of the year ended 31 July 2000 (together with the previous year's balance sheet).

Consolidated income and expenditure account for the year ended 31 July 2000

	£000
<i>Income:</i>	
Grants from funding bodies	16,700
Tuition fees	8,300
Other operating income	4,200
Investment income	100
	<u>29,300</u>
<i>Expenditure:</i>	
Staff costs	(17,900)
Other expenses	(9,250)
	<u>(27,150)</u>
Surplus before tax	2,150
Taxation	(250)
Surplus for year after tax	<u><u>1,900</u></u>

Balance sheet as at 31 July

	2000	1999
	£000	£000
Fixed assets	25,650	23,700
Investments	2,000	1,500
Net current assets	3,200	2,250
Creditors: amounts falling due after more than one year	(8,500)	(7,250)
Net assets	<u>22,350</u>	<u>20,200</u>
Represented by:		
Revaluation reserve	5,150	4,900
Income and expenditure account	17,200	15,300
	<u>22,350</u>	<u>20,200</u>

Additional information:

- (i) Fixed assets comprise:

	Land & buildings	Plant & equip't	Motor vehicles
	£000	£000	£000
Net book value at 1 August 1999	14,900	7,200	1,600
Acquisitions	600	2,650	1,250
Revaluation	250	-	-
Disposals	(500)	(400)	(200)
Depreciation	(150)	(800)	(750)
NBV at 31 July 2000	<u>15,100</u>	<u>8,650</u>	<u>1,900</u>

- (ii) Current assets comprise:

	2000	1999
	£000	£000
Stocks	1,200	1,400
Debtors and prepayments	4,700	3,300
Bank	650	(100)
Creditors and accruals	(2,600)	(1,550)
14% loan repayable on 31 January 2001	(500)	-
14% loan repayable on 31 January 2000	-	(500)

Taxation (250) (300)

Creditors at 31 July 2000 include £100,000 in respect of interest payable (£75,000 at 31 July 1999).

(iii) Creditors falling due after more than one year comprise the following:

	2000	1999
	£000	£000
14% loan	-	500
10% loan	3,250	3,250
9% loan	3,500	3,500
6% loan raised 1 April 2000	1,750	-

(iv) Bank interest paid during 1999/2000 amounted to £20,000.

(v) The sale proceeds of the fixed assets sold during the year were as follows:

	£000
Land & buildings	700
Plant & machinery	300
Motor vehicles	150

• **Requirement for question 2**

(a) Prepare the cash flow statement for Godstone University for the year ended 31 July 2000 in accordance with FRS 1 (Revised), together with the appropriate supporting statements. 20

(b) Comment on the results revealed by this statement. 5

(25)

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

Crowhurst Business School (CBS) generates income from its undergraduate and postgraduate (including MBA) programmes, as well as from the operation of its conference centre facilities. These facilities include residential accommodation, a full restaurant service and a licensed bar as well as the usual rooms for tuition purposes. The Director of CBS has requested that a course costing model be developed which will:

- identify the direct cost.
- identify the full cost of activities.
- allow more informed decisions to be made about which activities to provide.
- allow more realistic pricing.
- allow management to monitor the financial effectiveness of activities.

Budget information relating to activities for 1999/2000 is as follows:

	A	B	C	D	E	F
Teaching staff (£000s)	800	1,250	450			625
Supplies (£000s)	200	420	50	10	40	
Room rentals (£000s)	50	100	20			
Direct income (£000s)		1,980		24	880	1,000
Students (nos.)	180	140	40			
Delegate days				1,250	9,500	
Staff (w.t.e.: 40 weeks p.a.)	29	36	15			12

Key to activities:

- A Undergraduate programmes
 B MBA programme
 C Other postgraduate programmes
 D Day conferences
 E Residential conferences
 F Research

Some work has already begun on overhead apportionment as follows:

	A £000	B £000	C £000	D £000	E £000	F £000
Departmental administration	24	57	14	1	26	60
Conference management				19	127	
Catering	39	49	20	20	395	
Domestic staff					80	
Energy and sundry costs						
teaching areas	1	11	1	4	24	
staff offices	6	7	3			

Day conferences are provided for two clients who make use of a room and have coffee supplied in the morning, a light buffet lunch and tea in the afternoon. Residential clients have full board as well as unlimited coffee and tea during the day. Bar income is planned to be £350,000, much of which comes from the residential delegates; however, no data is available to identify the main users of this facility. Staff are provided with lunch each day at no cost.

Bar staff are generally students working on a casual basis at a cost of £25,000 p.a. Bar purchases are planned to cost £170,000.

University overheads have been centrally charged to CBS and comprise the following:

Principal's office	£25,000
Registrar	£35,000
Finance	£110,000
Personnel	£33,000
Other central departments	£170,000

CBS has traditionally apportioned university overheads to courses and activities based on direct cost.

Funding Council and Research Council income is monitored and controlled centrally. The average funding receivable for 1999/2000 is as follows:

Undergraduate	£6,800 per student (Funding Council) £1,000 per student (tuition fees)
MBA	£12,500 per student (tuition fees)
Postgraduate	£5,500 per student (Funding Council) £1,500 per student (Research Grants)

It is the intention of the course managers to expand activities in 1999/2000 including residential financial management seminars and short courses.

• **Requirement for question 3**

- | | | |
|-----|---|----|
| (a) | Calculate an appropriate unit cost for each of the activities of the Business School. | 6 |
| (b) | Draft a statement which determines the overall surplus/deficit of each activity to CBS and to the university and comment on your results. | 12 |
| (c) | Draft a pro forma that course managers can use to make a case to run additional courses/activities. | 4 |
| (d) | Identify any additional information that should be produced to aid decision making and explain how course managers should use it. | 3 |

(25)

4

There has been a number of well publicised examples of less than acceptable standards of management in a variety of public services, including the further and higher education sector, in the last decade.

In a number of cases millions of pounds of taxpayers' money have been lost. Consequently the issue of corporate governance has become a very significant item on the agenda of senior management and is likely to stay so for the foreseeable future.

You are a newly appointed management accountant, and the Director of Finance is preparing a booklet on an introduction to finance for newly appointed governors, senior managers and other relevant parties. He has asked you to prepare the section on corporate governance.

- **Requirement for question 4**

- (a) Explain the term 'corporate governance'. 5
 - (b) Describe how the further and higher education sector has addressed the issue of corporate governance in the last decade. 10
 - (c) Comment on the effectiveness of the measures introduced to date and suggest any areas of potential further developments. 10
- (25)

5

- **Requirement for question 5**

- (a) Identify and explain the main stages in a tendering process. 6
 - (b) Outline **three** pricing bases for tenders and appraise their usefulness. 9
 - (c) Identify the information necessary to evaluate a forthcoming tender for a contract to clean the buildings of a large educational institution. In what format should this information be provided? 10
- (25)