



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 1: PUBLIC SECTOR ACCOUNTING

MONDAY 13 DECEMBER 2021

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question. You will be told when to start writing.
2. This paper is divided into TWO sections:
Section A: One (1) Compulsory questions.
Section B: There are four (4) questions. Attempt any three (3) questions.
3. Enter your student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.
4. Do **NOT** write in pencil (except for graphs and diagrams).
5. **Cell Phones** are **NOT** allowed in the Examination Room.
6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.
7. All workings must be done in the answer booklet.
8. Present legible and tidy work.
9. Graph paper (if required) is provided at the end of the answer booklet.

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SECTION A

This question is compulsory and must be attempted.

QUESTION ONE

In the last decade adoption of IPSAS accrual across the world has gained momentum. Governments and public sector entities are increasingly adopting IPSAS in order to improve transparency and accountability of public funds. Despite this political appetite to go IPSAS, there has been a slow pace with which IPSAS is being adopted in Africa and globally. In 2013 - 2018, the Zambian government has been making pronouncements that as part of its public financial management reform program, International Public Sector Accounting Standards (IPSAS) would be adopted as its reporting framework by 2022.

Required:

In view of the above:

- (a) State and explain five (5) implications of adopting IPSAS for public sector organization. (10 marks)
- (b) State five (5) major benefits of IPSAS for Zambia's public sector accounting. (5 marks)
- (c) Identify five (5) key considerations to make while adopting IPSAS in Zambia. (5 marks)
- (d) Identify five (5) key challenges that have contributed to the slow pace with which IPSAS is being adopted in Zambia. (5 marks)
- (e) Briefly explain Five (5) ways in which the challenges identified in part (d) can be addressed. (5 marks)
- (f) With the aid of relevant examples, briefly distinguish between public sector cash basis reporting and accruals basis reporting. (10 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section

Attempt any THREE (3) questions.

QUESTION TWO

Accountants occupy positions of public trust and should be seen to be ethical in their professional conduct. Adherence to a code of ethics such as those formulated by the international accounting education standards board (IAESB) can go a long way in minimizing ethical dilemmas for a professional accountant.

Required:

- (a) List and explain the seven (7) ethical principles of public life. (14 marks)
- (b) List and explain three (3) threats to the objectivity of a public accountant. (6 marks)

[Total: 20 Marks]

QUESTION THREE

A chart of accounts can greatly assist public financial officers to efficiently respond to the informational needs of decision makers.

Required:

- (a) Discuss five (5) purposes of a chart of accounts in the context of public sector accounting. (10 marks)
- (b) The international accounting standards board (IASB) has mission of promoting uniformity in financial reporting in order to make accounting information more comparable.

Required:

Discuss five (5) advantages of global accounting standards. (10 marks)

[Total: 20 Marks]

QUESTION FOUR

Year in year out, cases of mismanagement and maladministration of public resources are on the rise in Zambia. An overview of the 2017 auditor general's report highlighted the increase in irregular payments, misappropriation of funds, unaccounted for funds and wasteful expenditure largely due to general weak internal controls in public offices. A classical case in point is the Ministry of General Education as identified by the 2017 auditor general's report. Below is an extract of the report.

Unsupported Payments: Contrary to Financial Regulation Nos. 45(2) and No. 52(1), payments in amounts totaling K11,319,784 paid to cashiers involving two hundred and nineteen (219) transactions processed during the period under review were not supported with documents such as letters of transfer and acquittal sheets. Included in the amount of

K11,496,050 was an amount of K9,172,773 involving one hundred and ninety-seven (197) transactions that was paid to cashiers that were not identified.

Over Payment of Subsistence Allowances: Public Service Management Division Circular No. B21 of 2016 specifies the rates for payment of subsistence allowance. During the period under review various officers were paid amounts totaling K1,659,900 in respect of subsistence allowance resulting from the use of incorrect rates instead of K1,428,350 which should have been paid had the correct rates been used resulting in an overpayment of K231,550. As at 31 August 2018, no recoveries had been made from the affected officers.

Irregularities in the Payment of Fuel Imprest: Cabinet Office Circular No. B7 of 2012 and No. B23 of 2012 stipulate that fuel for Government transport which is required to take officers for official business outside the district boundary be paid using the prescribed formula. However, payments for fuel imprest in amounts totaling K96,817 involving five (5) transactions were made without using the prescribed fuel formula and it was difficult to ascertain the distances covered in that the actual places visited were not disclosed.

Misapplication of Funds: Contrary to the Appropriation Act of 2016, amounts totalling K31,853,941 meant for Curriculum and materials development, Secondary School Infrastructure Development, Early Childhood Education Grants and School requisites for free Primary Education were spent on activities such as marking and monitoring of examinations, accounts activities, refunds to NIF and Keep Girls in School (KGS), training, events, foreign travel, internal audit activities, OBB workshops among others not related to the purpose for which the funds were appropriated for by Parliament.

Unaccounted for Stores: Contrary to Public Stores Regulation No. 16, stores items costing K150,157 (General stores – K20,007 and Fuel - K130,150) procured during the period under review were unaccounted for in that they did not have receipt and disposal details.

Missing Payment Vouchers: Contrary to Financial Regulation No. 65 (1), ninety-eight (98) payment vouchers in amounts totaling K639,557 processed during the period under review were not availed for audit.

Audit Committee: During the period under review, the Audit Committee met only once instead of meeting at least four (4) times as stated in their terms of reference. Further, internal audit reports were not reviewed by the Audit Committee thereby making it not possible to ascertain how their oversight role was accomplished.

Failure to Respond to Internal Audit Reports: During the period under review, the Internal Audit unit produced three (3) audit reports. However, as at 31 August 2018, Management had not responded to the reports.

Required:

- (a) Define internal controls and describe the objectives of internal controls. (5 marks)
- (b) With reference to the case as appropriate, identify and elaborate the weaknesses in internal controls at the Ministry of General Education. (10 marks)

- (c) Based on part (b), recommend measures that could be put in place in order to address the internal control deficiencies. (5 marks)

[Total: 20 Marks]

QUESTION FIVE

- (a) List and explain any four (4) core functions of treasury management. (10 marks)
- (b) The Classification of the Functions of Government (COFOG) is a detailed classification of the government functions. The aim of the classification is to ensure that all government expenditure is reported accordingly. Identify the functional areas reported as Government expenditure according to COFOG classification. (5 marks)
- (c) Distinguish between tax revenue and non-tax revenue and provide relevant examples.

(5 marks)

[Total: 20 Marks]

END OF PAPER

PFM1: PUBLIC SECTOR ACCOUNTING SUGGESTED SOLUTIONS

SOLUTION ONE

(a) What adoption of IPSAS entails

- IPASB provides countries with the option to adopt either cash and or accrual basis depending on the specific needs and systems of financial operation in place for the government or the countries in question.
- The cash basis allowed providers of external assistance, particularly providers of development assistance to follow a variety of accounting practices.
- Many recipients of external assistance therefore maintain their accounts on the cash basis of accounting and the development of a cash basis standard was therefore a step in the right direction.
- Accrual accounting focuses on revenue, cost, assets, liabilities and equity – instead of cash flows only.
- The capitalisation of assets, such as computers and machines, makes it possible to calculate depreciations and account for them in each period during which the machine is used. Most of the IPSAS are based on accrual basis which is in line with IFRS

(b) Five (5) major benefits of IPSAS for Zambia's public sector accounting

Governments and public sector entities are adopting IPSAS due to the following benefits:

- Greater accountability and transparency; Better decision making arising from increased information;
- Improved efficiency in financial reporting and auditing processes; Data consistency and application resulting from standardisation;
- Enhanced accounting professionalism in the public sector;
- Broader economic and social advantages e.g increase in direct investments which translate to more jobs;
- International Comparability between Governments and Public sector entities; Government stability through reforms brought about by IPSAS adoption.

(c) Five (5) key considerations to make while adopting IPSAS in Zambia

- Some of the considerations to make while adopting IPSAS include:
- Stakeholder engagement- to gain buy in; Structural and legal transformation;
- Transformation and change management;
- Skills capacity;
- Cost; Technology and infrastructure; Implementation approach- Phased or big bang; External support- private sector, donors, professional firms; If these considerations are not well factored, they become challenges.

(d) Five (5) key challenges that have contributed to the slow pace with which IPSAS is being adopted in Zambia.

- Capacity;
- Weak internal control environment;
- Change management; Stakeholder support and government buy in;

- Legislation which is inconsistent with accrual basis of accounting;
- Implementation cost and infrastructural challenges.

(e) Five (5) ways in which the challenges identified in part (d) can be addressed

- Build Capacity;
- strengthen weak internal control environment;
- change management;
- stakeholder support and government buy in;
- revise legislation which is inconsistent with accrual basis of accounting;
- improve infrastructural.

(f) Public sector cash basis reporting and accruals basis reporting.

Financial reporting under the cash basis

This accounting system recognizes only cash inflows and cash outflows. The resulting final accounts are summarized cash books. There are no balance sheets under this system because there are no other assets (apart from cash) and liabilities in the books other than cash balances.

- Sales are recognized only when cash is recorded. So, there are no receivables.
- Purchases are only recognized when cash is paid. So, there are no payables.
- There is no inventory adjustment because the accounts are not concerned with recording usage. There is no opening or closing inventory except that cash has been paid for it.
- There are no non-current assets.
- There are no current and non-current liabilities.

Financial reporting under the accrual basis

Revenue and costs are accrued (i.e recognized as they are earned or incurred, and not as money is received or paid), matched with one another so far as their relationship can be established or justifiably assumed, and dealt with in the income statement of the period to which they relate.

- The earning of revenue is generally taken to mean that invoices have been issued.
- Costs are incurred when services are received. Therefore, recognition of income and costs is not when cash is received or paid.

SOLUTION TWO

Part (a)

Seven Principles of public life

	Principle	Explanation
1	Selflessness	The interest of public officers should be subordinate to public interest
2	Integrity	Public officers should be honest and straightforward in their professional and business relationships. They should not use their positions to gain financial or material advantage.
3	Objectivity	The decisions of public officers should not be influenced by third parties. Public officers should act with impartiality fairly and on merit.
4	Accountability	This is a state or quality of being answerable. Public officers are accountable to the public and their representatives.
5	Openness	Holders of public office should be transparent and open in the way they conduct themselves. They should not withhold information from the public unless there is a legal reason for doing so.
6	Honesty	Holders of public office should be dependable and truthful in their everyday work and private life.
7	Leadership	Public officers should walk the principles above. They should be challenge the status quo and inspire others to emulate their professional behaviour.

Part (b)

Three threat to the objectivity of a public Accountant

	Threat	Explain
1	Self-interest	The Public Accountant has beneficial interest in the beneficiaries of his work. He or she may possess financial and other interest in a public or private institution which they have been assigned to audit.
2	Self-review	The Public Accountant finds himself in a position where he may review his own work. This occurs when an accountant performs other duties separate from his core duties. This may occur when a previous judgement needs to be reassessed by the professional accountant responsible.
3	Advocacy	The public accountant promotes a position which favours a client to extent whereby his objectivity is questionable. This may take place when an accountant negotiates business deals on behalf of his clients.
4	Familiarity	This occurs when an accountant is more sympathetic to the needs of his client because of a close relationship or simply failure to maintain a professional relationship.
5	Intimidation	Occurs when actual or perceived threats deters an Accountant from acting in his role.

SOLUTION THREE

Part (a)

Five purposes of a chart of accounts

- To differentiate between revenue, expenditure, assets and liabilities
- To provide a standard framework for the presentation of financial information easy of understanding and analysis
- To facilitate preparation of financial accounting reports
- To facilitates comparisons between different organisations or government institutions
- It serves as an index to locate a given account within the ledger.

Part (b)

Five advantages of global accounting

- Promotes uniform reporting – this is essential for periodic overtime comparisons of information for the same organisation or similar organisations.
- May reduce training costs – if the same standards are taught in different countries the need to send public accountants for training abroad is unlikely to arise and this can reduce training costs.
- Facilitates the transfer of labour between nations – the usage of the same accounting standards across the globe means accountants can work in different nations after appreciating the tax and commercial law of a sovereign state.
- Enhanced accountability – global standards require that a firm complies fully with all applicable standards in the spirit of promoting public accountability.
- Promotes foreign direct investment – Oversea investors would be more willing to invest in a state which adopts and applies global accounting standards.

SOLUTION FOUR

(a) Definition of internal controls

- ✓ Internal control has been defined as the **process designed** and **effected by those charged with governance, management** and other **personnel** to provide **reasonable assurance** about the achievement of an entity's **objectives** with regard to reliability of **financial reporting, effectiveness** and **efficiency** of operations and compliance with applicable **laws** and **regulations** designed and implemented to address identified business risks, financial risks, compliance risks, operational risks and other risks that threaten the achievement of any of the objectives.
- ✓ **Objectives of internal controls**
- ✓ **Achieving orderly conduct of business:** Internal controls should ensure the organisation's operations are conducted **effectively and efficiently**. In particular they should enable the organisation to respond appropriately to **business, operational, financial, compliance** and other **risks** to achieving its objectives.
- ✓ **Adherence to internal policies and laws:** Controls should ensure that the organisation and its staff comply with **applicable laws and regulations**, and that staff **comply with internal policies** with respect to the conduct of the business.
- ✓ **Safeguarding assets:** Controls should ensure that assets are optimally utilised and stop assets being **used inappropriately**. They should prevent the organisation **losing assets** through **theft or poor maintenance**.
- ✓ **Prevention and detection of fraud:** Controls should include measures designed to prevent fraud such as **segregation of duties** and **checking references** when staff are recruited. The information that systems provide should **highlight unusual transactions or trends** that may be signs of fraud.
- ✓ **Accuracy and completeness of accounting records:** Controls should ensure that records and processes are kept that generate a **flow of timely, relevant and reliable information that aids management decision-making**.
- ✓ **Timely preparation of reliable financial information:** They should ensure that published accounts **give a true and fair view**, and other published information is **reliable** and **meets the requirements** of those stakeholders to whom it is addressed.
- ✓ **Public sector general control objectives are meant to achieve:** promoting orderly, economical, efficient, and effective operations and quality products and services consistent with the organization's mission; safeguarding resources against loss due to waste, abuse, mismanagement, errors, and fraud and other irregularities; adhering to

laws, regulations, and management directives; and developing and maintaining reliable financial and management data and fairly disclosing that data in timely reports.

(b) Identified Weaknesses

- ✓ Weak internal controls – Audit committee rarely meets, and audit reports are not reviewed.
- ✓ Failure to follow regulation
- ✓ Lack of enforcement of rules and regulations.
- ✓ Lack of monitoring of internal controls.
- ✓ Weak transaction and procurement controls.
- ✓ Lack of supervision.
- ✓ Lapses in human, authorization, procedural, operational, technological, documentation, segregation and recording controls.

(c) Measures

- ✓ Revise the PPA 2008 and make it punitive for the offenders.
- ✓ Ensure audit committee function as intended and recommendations are followed by ST.
- ✓ Targeted training to accountants, internal auditors, PSs in procurement and PFM law's provisions.
- ✓ Supervise audit committee work by ST.

SOLUTION FIVE

- Cash management.
Cash management involves ensuring that the reporting entity has sufficient funds to meet its short term obligations.
- Financial asset management
Financial asset management ensures that the public sector entity is able to generate adequate returns from its investments.
- Debt management
Debts management reduces credit risk or failure to recover funds which were advanced to third parties for eventual repayment.
- Accounting and reporting
This involves a process of identifying, analyzing, summarizing and presenting accounting information with the view of improving decisions.
- Revenue collection
Revenue collection focuses means and processes of improving the revenue base of a public sector organization.
- Central bank and commercial bank relations
Central bank and commercial bank relations include creating a working relationship with the central bank as well as being in full command of relevant central bank regulations.

b) Functional areas of government (COFOG) expenditure:

- General public service
- Defense
- Public Order & Safety
- Economic Affairs
- Environmental Protection
- Housing and Community amenities
- Health
- Recreation, Culture and Religion
- Education
- Social Protection

c) Tax revenue and Non-Tax revenue

- Tax revenue is a compulsory payment to government instituted through taxation.
Tax: PAYE, VAT, Sales Tax, Corporation Tax, Customs & Excise Duty, Mineral Royalty tax, Corporation tax, Property Tax.
- Non tax revenue refers to revenue earned by government from sources other than tax. **Non – Tax:** Fines, fees, levies, Ground rent, Passport fees, Commissions, dividends, tool fees.

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 3: GOVERNANCE AND MANAGEMENT IN PUBLIC SECTOR

TUESDAY 14 DECEMBER 2021

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

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SECTION A

This question in this Section is Compulsory.

QUESTION ONE (COMPULSORY)

Case study: RESETTLEMENT ACTION PLAN FOR SERENJE TO MPIKA ROAD

The Serenje–Mpika Road forms a part of the Zambian Great North Road (T2) that is a section of international routes: the Trans-Africa Highway and the North-South Corridor (NSC). The NSC is a joint COMESA/EAC/SADC Aid for Trade initiative. Its primary aim is to reduce the time, and cost of transport along this priority Corridor which links the port of Dar-es-Salaam in Tanzania to the Copper-belt (Southern DR Congo and Northern Zambia) and connects to the southern ports of South Africa specifically the port of Durban. The Corridor system, with its spurs, services eight (8) countries - Tanzania, DR Congo, Zambia, Malawi, Botswana, Zimbabwe, Mozambique, and South Africa. The project has been endorsed by the SADC/EAC/COMESA Tripartite that aims to improve the regional transport infrastructure with a view to supporting economic and social development programs along the Trans-Africa Highway/North-South Corridor. The project road was originally constructed as a bitumen surfaced road in 1970s and is now beyond its design life, notwithstanding the emergency and periodic maintenance interventions. It has received a number of rehabilitation and periodic maintenance since its initial construction, commencing with emergency maintenance between 1995 and a World Bank (WB) funded periodic maintenance between 1998 and 2000. This intervention provided a limited design life intervention, with focus on partial reconstruction for severely deteriorated sections and double seal treatment for most sections. Follow up maintenance was not fully undertaken, and consequently in 2011 the Government of the Republic of Zambia (GRZ) commissioned two emergency repair works contracts for the section. The poor condition of the road would be detrimental to the movement of goods and services, and therefore intervention driven by ensuring that the critical route does not present a transit bottleneck for trade in the region. GRZ with the support of COMESA conducted studies in 2013 for the Serenje – Nakonde section of the corridor, in three (3) Lots viz.: Lot 1 – Serenje – Mpika, Lot 2 – Mpika – Chinsali and Lot 3 – Chinsali – Nakonde. The Bank is financing the Chinsali – Nakonde section (approved July 2015) while the appraisal for the Mpika – Chinsali section is advanced with EU/European Investment Bank (EIB) support. The Serenje – Mpika (238 km) section is complementary to these. In response to a funding request submitted to the Bank by Government of the Republic of Zambia (GRZ), the Bank conducted a Preparation Mission in

August/September 2016. The funding request was for the support to the improvements of the Serenje – Mpika section (238 km) of the North – South Corridor in Zambia. The objective of the mission was to review, discuss and confirm possible project components for the Project with GRZ, the Executing Agency and the relevant authorities inclusive of development partners. The mission specific objectives were: (i) to confirm the technical feasibility and economic viability of the project; (ii) to discuss and agree with the Borrower, on project components, categories of expenditures and procurement modes; (iii) to assess and confirm the preparedness and disclosure requirements of the Environmental and Social Impact Assessments (ESIAs) and RAPs locally; and, (iv) to determine, in consultation with the respective Government authorities, the contribution of the Bank in the implementation

Source: Road Development Agency Government/Fairley Road, Report- 2017

Required:

- (a) Contract management requires that the management of contracts takes into account best practices. List down eight (8) best practices required in management of Contracts. (16 marks)
- (b) List four (4) factors to consider when selecting a sub-contractor for a project (4 marks)
- (c) Discuss the terms good governance, accountability and transparency as it relates to the effective management of Government and the Public Sector. (15 marks)
- (d) Explain why Governments form regional groupings like COMESA (5 marks)

[Total: 40 Marks]

SECTION B

Answer Any Three (3) Questions in this section.

QUESTION TWO

Public policy formation is the study, creation and implementation of laws, regulations, funding priorities or other actions on a specific public issue by a local, state or federal government. Public policy strategy can also be the rescinding of an existing policy or the deliberate decision not to act upon an issue as well.

Required:

- (a) Explain five (5) characteristics of a good public policy. (15 marks)
- (b) Give two (2) main approaches instrumental to policy implementation. (5 marks)

[Total: 20 Marks]

QUESTION THREE

Corporate ethics in governance is fundamental as it underpins the structures and systems used to ensure good governance and without it governance will fail. So our first Golden Rule of Corporate Governance is that the business morality or ethic must permeate an organization from top to bottom and embrace all stakeholders.

Required:

- (a) Point out five (5) principles of good governance (10 marks)
- (b) Explain the five (5) governance ethics to be considered at workplaces. (10 marks)

[Total: 20 Marks]

QUESTION FOUR

- (a) State any five (5) advantages of Nationalization? (10 marks)
- (b) Explain Decentralization and Centralization the with two example of each (10 marks)

[Total: 20 Marks]

QUESTION FIVE

Internal communication is the sharing of information within an organization for business purposes. Internal communication is important in all organizations and its flow is multidirectional.

Required

- (a) Describe the following internal flows of communication in the public sector:
- (i) Downward communication (4 marks)
 - (ii) Upward Communication; and (4 marks)
 - (iii) Lateral (horizontal communication) (4 marks)
- (b) Explain two (2) consequences of conflicts (4 marks)
- (c) List four (4) strategies that can be used as techniques for managing conflict. (4 marks)

[Total: 20 Marks]

END OF PAPER

PFM3: GOVERNANCE AND MANAGEMENT IN PUBLIC SECTOR

SUGGESTED SOLUTIONS

SOLUTION ONE

Contract management requires that the management of contracts takes into account best Practices. List down eight (8) best practices required in management of Contracts

- (i) Optimizes delivery of large capital projects
 - (ii) Enhances risk management
 - (iii) Identifies savings and additional revenue opportunities
 - (iv) Customer and supplier dissatisfaction
 - (v) Revenue collection delays
 - (vi) Encourages communication between all parties to contracts
 - (vii) Erroneous payments
 - (viii) Service delivery issues
 - (ix) Missed saving opportunities
- (b) List four factors to consider when selecting a sub-contractor for a project
- i- Look for strong performance and credentials. ...
 - ii- Make sure they are insured. ...
 - iii- Make sure they are licensed. ...
 - iv- Ask for referrals. ...
 - v- Check to see if they have any complaints logged against them. ...
 - vi- Ask them about safety. ...
 - vii- Create a written contract.
- (c) Discuss the terms good governance, accountability and transparency as it relates to the effective management of Government and the Public Sector.
- i. **Good governance**- This is a way of measuring how public institutions conduct public resources in a preferred way.
 - ii. **Transparency**- having an open and clear disclosure of relevant information to shareholders and other stakeholders
 - iii. **Accountability**- corporate accountability means being answerable and account for the actions and consequences.

(d) Explain why Governments form regional groupings like COMESA

Regional groupings help countries in the following ways

- International Trade incentives between among members
- Economic support among members
- Infrastructural development support

SOLUTION TWO

(a) Discuss the five (5) factors that influence Public Policy

- i- Endorsed – The policy has the support of management.
- ii- Relevant - The policy is applicable to the organization.
- iii- Realistic – The policy makes sense.
- iv- Attainable – The policy can be successfully implemented.
- v- Adaptable – The policy can accommodate change.

(b) Give two main approaches instrumental to policy implementation

- (i) *Top-down approach:* policy designers are the central actors and concentrate their attention on factors that can be manipulated at the central level
- (ii) *Bottom-up approach:* emphasis target groups and service deliverers, arguing that policy is made at the local level

SOLUTION THREE

(a) Point out five principles of good governance

- i- Leadership.
- ii- Ethics & Integrity.
- iii- Stewardship.
- iv- Accountability & Transparency.
- v- Effectiveness.
- vi- Roles and Responsibilities.
- vii- Participation.

(b) Explain the five governance ethics to be considered at workplace

- i. **Probity/Honest-** this relates to being principled not to take bribes and not to mislead the shareholders and stakeholders.
- ii. **Fairness-** taking a balance application is the management without prejudice and taking into account minority views in making decisions
- iii. **Responsibility-** management able to accept responsibility for credit or blame over governance decisions.
- iv. **Transparency-** having an open and clear disclosure of relevant information to shareholders and other stakeholders
- v. **Accountability-** corporate accountability means being answerable and account for the actions and consequences.

SOLUTION FOUR

(a) State any advantages of Nationalization?

Nationalization is the process of taking privately-controlled companies, industries, or assets and putting them under the control of the government.

- i- It creates public interest
- ii- It provides workers' rights in those companies
- iii- It creates a natural monopoly
- iv- Helps to regulate market prices
- v- Provides more jobs

(b) Explain Decentralization and Centralization the with two example of each

(i) Decentralization refers to the systematic effort to delegate to the lowest levels all authority except that which can only be exercised by central points.

Examples

- Allowing decisions to be made at branch level
- Allowing departments to make plans and decide how execute them

(ii) Centralization refers to the system were decisions are made at the central point usually top management. Examples are political parties.

SOLUTION FIVE

(a) Describe the following internal flows of communication in the public sector:

- Downward communication
- Upward Communication; and
- Lateral (horizontal communication)

(i) Downward communication occurs when information and messages flow down through an organization's formal chain of command or hierarchical structure. In other words, messages and orders start at the upper levels of the organizational hierarchy and move down toward the bottom levels. Responses to downward communications move up along the same path.

(ii) Upward Communication

Communication is a very important part of working in the business environment. Managers must be able to communicate with employees and employees must be able to communicate with managers in order to have a profitable business. **Upward communication** is the flow of information from front line employees to managers, supervisors, and directors.

(iii) Lateral Communication

Lateral (Horizontal) communication is defined as the exchange, imparting or sharing of information, ideas or feeling between people within a community, peer groups, departments or units of an organization who are at or about the same hierarchical level as each other for the purpose of coordinating activities, efforts or fulfilling a common purpose or goal. Horizontal communication is one of the essential communication skills we need in life. This communication helps to promote teamwork and facilitates coordinated group effort within a group or organization. It usually is less structured and informal compared to vertical communication. This communication may take place as telephone calls, e-mails, memos, letters, informal discussions, gossip, teleconferencing, videoconferencing, and meetings set up by the group.

(b) Discuss **TWO (2)** consequences of conflicts and failed negotiations.

-Conflict is a process in which people disagree over significant issues, thereby creating friction.

-Conflict can be a destructive force. However, it can also be beneficial when used as a source of renewal and creativity.

-Although conflict is inevitable and desirable in organizations, a high level of unresolved conflict can be destructive. Individuals, teams, or departments that are engaged in high conflict may lose sight of the common goals and focus on winning at all costs.

-They could withhold important information from others, or even actively sabotage others' work.

-When conflict leads to winners and loser, losers may be demoralized and become demotivated.

(c) State **Four (4)** strategies that can be used as techniques for managing conflict.

Collaborating or Problem Solving

This is the most preferred method of resolving the conflict, when the team is working like a well-oiled machine. Meaning that the team is already in performing or adjourning stages of team development.

Collaborating or problem solving is the most productive conflict management technique, when the team members trust each other and they know that they need to work together to achieve a common goal.

Compromising

Both parties give up something to resolve the conflict. This conflict resolution is only possible, when both the parties have some mindset to agree and want to keep the relationship alive.

Compromise conflict resolution is a lose-lose situation, because both parties are giving up something in order to resolve the conflict.

Smoothing/Accommodating

Smoothing is when the arguments flare up between the parties, then you play down the problem to make it seem like the problem is not so bad or does exist at all.

Then each of the party step back, cool down and take time to think about what is going on.

Smoothing is a temporary work around and will not resolve the actual issue.

Forcing/Competition

This is where a manager makes a decision in favor of one party. So one party wins and the other party loose. Hence this is called win-lose situation.

There may be negative consequences to this conflict resolution, as the losing party may get demotivated. So this conflict resolution technique need to apply carefully by looking at the impact to the project.

This is definitely not the best option when you have opportunity to use other conflict resolution techniques.

Withdraw OR Avoid

When people are more frustrated, they walk away from the problem or they just skip it for the time being. Here the actual problem still persists. And it may come back in future. It is just that people withdrawn from the situation. Sometimes, the problem may also get resolved by itself.

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT EXAMINATIONS

DIPLOMA LEVEL

PFM4 - PUBLIC SECTOR FINANCIAL MANAGEMENT

FRIDAY 17 DECEMBER 2021

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question. You will be told when to start writing.
2. This paper is divided into TWO (2) sections:
Section A: One (1) Compulsory scenario question.
Section B: Four (4) Optional Questions. Attempt any Three (3) questions.
3. Enter your student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.
4. Do **NOT** write in pencil (except for graphs and diagrams).
5. **Cell Phones** are **NOT** allowed in the Examination Room.
6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.
7. All workings must be done in the answer booklet.
8. Present legible and tidy work.
9. Graph paper (if required) is provided at the end of the answer booklet.
10. Present Value and Annuity tables are attached at the end of this paper.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

SECTION A

This question in this section is compulsory.

QUESTION ONE

Hawk Republic is in the process of preparing its 2022 National Budget. It prepares its national budget using output based budgeting. Output based budget has been rolled out to all Ministries and its national development it had set to allocate and achieve the following in the education sector over the medium term expenditure framework:

Budget Allocation

Programme	2022 K'000	2023 K'000	2024 K'000
Early Childhood Education	87,000	125,000	15,000
Primary Education	8,185,000	9,225,000	10,557,000
Secondary Education	4,137,000	6,292,000	8,235,000
Youth and Adult Literacy	935,000	920,000	1,120,000
Management and Support Services	925,700	942,000	890,300
Total	14,269,700	17,504,000	20,817,300

Programme Outputs

Programme	Output Indicator	2022	2023	2024
Early Childhood Education	Proportion of Grade 1 entrants	26%	30%	35%

Primary Education	Pupil Teacher Ratio	1:30	1:20	1:15
Secondary Education	Grade 9 completion rate	60%	70%	85%
Youth and Adult Literacy	No. of Youth & Adult literacy centers established	1,300	500	400
Management and Support Services	No. of Teaching Posts Created	2,000	6,000	4,000

During the 2022 budget preparation, Hawk Republic was faced with so many challenges which included reduction in revenue collection by 70% due to rising in the debt service and huge wage bill. These two scenarios have slowed down economic growth. Due to reduction of revenues, the ministry received a circular advising that the 2022 projected budget in the Medium Term Expenditure Framework should be revised by 30% in order to align with the resource envelope. The government of Hawk is hoping to raise the shortfall of funds in the budget from co-operating partners in form of grants.

You are Director of Finance in the Ministry of General Education and the Permanent Secretary has requested your office to prepare the following paper for presentation to stakeholders outlining:

- (a) The basic steps in budget preparation in the Public Service. (6 marks)
- (b) Advantages and Disadvantages of Planning. (21 marks)
- (c) Revised Budget figures for 2022 based on the reduction in the revenues as guided by the Ministry of Finance. (3 marks)
- (d) Evaluating the extent to which the programme outputs in the 2022 budget will be achieved given the reduction in revenues. (1 mark)
- (e) What are the pros and cons of the following capital budgeting techniques.
 - (i) Payback Period (4 marks)
 - (ii) Accounting Rate of Return (5 marks)

[Total: 40 marks]

SECTION B

There are FOUR (4) questions in this section.

Attempt any THREE (3) questions.

QUESTION TWO

CTY Hospital is a Government Hospital established 20 years. It has been fully funded by the Government until last year when government decided to reduce its funding to the hospital due to budget constraints. The reduction in funding led to delayed payments of salaries for medical staff at the hospital. The Hospital is now looking for alternative sources of funding to supplement Government funding.

During a recent meeting of the Board of Directors, a decision was made to introduce fee paying services at the hospital. The hospital Directors are proposing that certain hospital wards be upgraded to higher standards in order to turn them into fee paying wards. Patients will now have the option of either being admitted in the upgraded wards at a fee or be admitted in the ordinary wards at no cost. However, this decision is subject to approval from the minister of health.

The Chairperson of the hospital Board of Directors is not optimistic about this proposal because he believes it will face criticism from the media. He is also concerned about the possible reaction of other interest groups such as NGOs and trade unions. However, the medical authority and pharmaceutical authority are already aware as the Directors are also members of these institutions. The Chairpersons of these institutions are in full support of the proposal as they believe it is in public interest and it will raise the standard of medical services offered at the hospital and eliminate the salary arrears.

Required:

Assume that you are the Project Manager appointed by the Board to oversee the Hospital fee paying project.

- (a) Identify the internal and external stakeholders of the Hospital. (4 marks)
- (b) Draw up a stakeholder map of the Hospital, with reference to the scenario and explain the reasons for your mapping. (16 marks)

[Total: 20 marks]

QUESTION THREE

The Government of Delta Republic has been implementing Treasury Reforms for the last five years. Among the components of the treasury Reforms implemented are the Treasury Single Account. However, during recent IMF visit, the mission indicated that the Government of Delta Republic still lagged behind in the implementation of cash flow forecast and debt management reforms. According to the road map that was shared, the Cash flow forecast and Debt Management reforms were supposed to be implemented during 2018 fiscal year. The Authorities of Delta Republic have indicated that there was no need for cash flow forecasting later on best practices in debt management. Currently the Government of Delta Republic focuses on debt contraction, no database of loans contracted and repayments are maintained. This has made it very difficult for the Government to undertake debt restructuring.

Required:

- (a) Explain to the Authorities the advantages of cash flow forecast and how cash flow of an organization can be managed. (10 marks)
- (b) Prepare a presentation to the Authorities on best practice of public debt management. (10 marks)

[Total: 20 marks]

QUESTION FOUR

The Management of Alpha District Council are reviewing the capital investments options for the coming year and are considering four (4) projects.

Project A – Would cost K39,000 now and would earn the following profits:

1 st Year	K18,000
2 nd Year	K22,000
3 rd Year	K20,000
4 th Year	K16,000

The capital equipment purchased at the start of the project will be resold for K15,000 at the start of the sixth year .

Project B – would involve a current outlay of K54,000 on capital investments and K30,000 on working capital. The cash profits of the project would be as follows:

Year	K
1	15,000
2	22,000
3	8,000

At the end of the third year the working capital investment would be recovered and the equipment would be sold K15,000.

Project C – would involve a current outlay of K60,000 on the equipment and K25,000 on working capital. The investment in working capital would be increased by K31,000 at the end of first year. Annual cash profits would be K28,000 for five years. At the end of the project, the working capital would be recovered.

Project D – would involve an outlay of K30,000 now and a further outlay of K30,000 after one year. Cash profits thereafter would be as follows:

2 nd Year	K25,000
3 rd Year	K22,000
Year 4 th to 8 th	K18,000 Per Annum

The District Council has a policy of discounting all projects of 5 years duration or less at a cost of 12% and all other projects at a cost of 15%. All investments are believed to be of similar risks to the District Council's existing capital investment.

Required:

- (a) Calculate the NPV of each project, and determine which should be undertaken by Alpha District Council. (14 marks)
- (b) Explain how uncertainty and risks could be considered in the investment process. (6 marks)

[Total: 20 marks]

QUESTION FIVE

The Ministry of Finance of Country Y is in the process of setting up a Treasury Department. Experts that have been evaluating the current system at the Ministry of Finance for country Y have raised a number of concerns with regard to effectively operating the Department. Some of the issues raised were capacity of Staff to execute the Treasury functions and also the current negative global economic down turn. They have proposed that the operational risk management strategy was critical for the Treasury Department. It was further noted that officials in the Treasury Department did not fully understand their responsibilities. Assuming you are the Chief Accountant in the Treasury Department, the Accountant General has requested that you prepare a memo outlining:

- (a) Three (3) examples of Internal Operational Risks and Seven (7) examples of External Operational Risks. (10 marks)
- (b) Three (3) critical factors to take into account when determining a risk management strategy for a Treasury Department. (6 marks)
- (c) The responsibilities of Treasury Department in operational risk management.

(4 marks)

[Total: 20 marks]

END OF PAPER

Formula Sheet

Economic order quantity

$$= \sqrt{\frac{2C_n D}{C_H}}$$

Miller – Orr Model

Return point = Lower limit + $\left(\frac{1}{3} \times \text{spread}\right)$

$$\text{Spread} = 3 \left[\frac{\frac{3}{4} \times \text{transaction cost} \times \text{variance of cash flows}}{\text{interest rate}} \right]^{\frac{1}{3}}$$

The Capital Asset Pricing Model

$$E(r_i) = R_f + \beta_i (E(r_m) - R_f)$$

The asset beta formula

$$\beta_a = \left[\frac{V_e}{(V_e + V_d(1 - T))} \beta_e \right] + \left[\frac{V_d(1 - T)}{(V_e + V_d(1 - T))} \beta_d \right]$$

The Growth Model

$$P_0 = \frac{D_0(1+g)}{(r_e - g)}$$

Gordon's growth approximation

$$g = b r_e$$

The weighted average cost of capital

$$\text{WACC} = \left[\frac{V_e}{V_e + V_d} \right] k_e + \left[\frac{V_d}{V_e + V_d} \right] k_d (1 - T)$$

The Fisher formula

$$(1 + i) = (1 + r)(1 + h)$$

Purchasing power parity and interest rate parity

$$s_1 = S_0 \times \frac{(1 + h_e)}{(1 + h_b)} \qquad f_0 = S_0 \times \frac{(1 + i_e)}{(1 + i_b)}$$

Present Value Table

Present value of 1 i.e. $(1 + r)^{-n}$

Where r = discount rate
 n = number of periods until payment

Periods (n)	Discount rate (r)										
	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	
1	0.990	0.980	0.971	0.962	0.952	0.943	0.935	0.926	0.917	0.909	1
2	0.980	0.961	0.943	0.925	0.907	0.890	0.873	0.857	0.842	0.826	2
3	0.971	0.942	0.915	0.889	0.864	0.840	0.816	0.794	0.772	0.751	3
4	0.961	0.924	0.888	0.855	0.823	0.792	0.763	0.735	0.708	0.683	4
5	0.951	0.906	0.863	0.822	0.784	0.747	0.713	0.681	0.650	0.621	5
6	0.942	0.888	0.837	0.790	0.746	0.705	0.666	0.630	0.596	0.564	6
7	0.933	0.871	0.813	0.760	0.711	0.665	0.623	0.583	0.547	0.513	7
8	0.923	0.853	0.789	0.731	0.677	0.627	0.582	0.540	0.502	0.467	8
9	0.914	0.837	0.766	0.703	0.645	0.592	0.544	0.500	0.460	0.424	9
10	0.905	0.820	0.744	0.676	0.614	0.558	0.508	0.463	0.422	0.386	10
11	0.896	0.804	0.722	0.650	0.585	0.527	0.475	0.429	0.388	0.350	11
12	0.887	0.788	0.701	0.625	0.557	0.497	0.444	0.397	0.356	0.319	12
13	0.879	0.773	0.681	0.601	0.530	0.469	0.415	0.368	0.326	0.290	13
14	0.870	0.758	0.661	0.577	0.505	0.442	0.388	0.340	0.299	0.263	14
15	0.861	0.743	0.642	0.555	0.481	0.417	0.362	0.315	0.275	0.239	15
(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	
1	0.901	0.893	0.885	0.877	0.870	0.862	0.855	0.847	0.840	0.833	1
2	0.812	0.797	0.783	0.769	0.756	0.743	0.731	0.718	0.706	0.694	2
3	0.731	0.712	0.693	0.675	0.658	0.641	0.624	0.609	0.593	0.579	3
4	0.659	0.636	0.613	0.592	0.572	0.552	0.534	0.516	0.499	0.482	4
5	0.593	0.567	0.543	0.519	0.497	0.476	0.456	0.437	0.419	0.402	5
6	0.535	0.507	0.480	0.456	0.432	0.410	0.390	0.370	0.352	0.335	6
7	0.482	0.452	0.425	0.400	0.376	0.354	0.333	0.314	0.296	0.279	7
8	0.434	0.404	0.376	0.351	0.327	0.305	0.285	0.266	0.249	0.233	8
9	0.391	0.361	0.333	0.308	0.284	0.263	0.243	0.225	0.209	0.194	9
10	0.352	0.322	0.295	0.270	0.247	0.227	0.208	0.191	0.176	0.162	10
11	0.317	0.287	0.261	0.237	0.215	0.195	0.178	0.162	0.148	0.135	11
12	0.286	0.257	0.231	0.208	0.187	0.168	0.152	0.137	0.124	0.112	12
13	0.258	0.229	0.204	0.182	0.163	0.145	0.130	0.116	0.104	0.093	13
14	0.232	0.205	0.181	0.160	0.141	0.125	0.111	0.099	0.088	0.078	14
15	0.209	0.183	0.160	0.140	0.123	0.108	0.095	0.084	0.074	0.065	15

Annuity Table

Present value of an annuity of 1 i.e. $\frac{1 - (1 + r)^{-n}}{r}$

Where r = discount rate
 n = number of periods

Periods (n)	Discount rate (r)										
	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	
1	0.990	0.980	0.971	0.962	0.952	0.943	0.935	0.926	0.917	0.909	1
2	1.970	1.942	1.913	1.886	1.859	1.833	1.808	1.783	1.759	1.736	2
3	2.941	2.884	2.829	2.775	2.723	2.673	2.624	2.577	2.531	2.487	3
4	3.902	3.808	3.717	3.630	3.546	3.465	3.387	3.312	3.240	3.170	4
5	4.853	4.713	4.580	4.452	4.329	4.212	4.100	3.993	3.890	3.791	5
6	5.795	5.601	5.417	5.242	5.076	4.917	4.767	4.623	4.486	4.355	6
7	6.728	6.472	6.230	6.002	5.786	5.582	5.389	5.206	5.033	4.868	7
8	7.652	7.325	7.020	6.733	6.463	6.210	5.971	5.747	5.535	5.335	8
9	8.566	8.162	7.786	7.435	7.108	6.802	6.515	6.247	5.995	5.759	9
10	9.471	8.983	8.530	8.111	7.722	7.360	7.024	6.710	6.418	6.145	10
11	10.37	9.787	9.253	8.760	8.306	7.887	7.499	7.139	6.805	6.495	11
12	11.26	10.58	9.954	9.385	8.863	8.384	7.943	7.536	7.161	6.814	12
13	12.13	11.35	10.63	9.986	9.394	8.853	8.358	7.904	7.487	7.103	13
14	13.00	12.11	11.30	10.56	9.899	9.295	8.745	8.244	7.786	7.367	14
15	13.87	12.85	11.94	11.12	10.38	9.712	9.108	8.559	8.061	7.606	15
(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	
1	0.901	0.893	0.885	0.877	0.870	0.862	0.855	0.847	0.840	0.833	1
2	1.713	1.690	1.668	1.647	1.626	1.605	1.585	1.566	1.547	1.528	2
3	2.444	2.402	2.361	2.322	2.283	2.246	2.210	2.174	2.140	2.106	3
4	3.102	3.037	2.974	2.914	2.855	2.798	2.743	2.690	2.639	2.589	4
5	3.696	3.605	3.517	3.433	3.352	3.274	3.199	3.127	3.058	2.991	5
6	4.231	4.111	3.998	3.889	3.784	3.685	3.589	3.498	3.410	3.326	6
7	4.712	4.564	4.423	4.288	4.160	4.039	3.922	3.812	3.706	3.605	7
8	5.146	4.968	4.799	4.639	4.487	4.344	4.207	4.078	3.954	3.837	8
9	5.537	5.328	5.132	4.946	4.772	4.607	4.451	4.303	4.163	4.031	9
10	5.889	5.650	5.426	5.216	5.019	4.833	4.659	4.494	4.339	4.192	10
11	6.207	5.938	5.687	5.453	5.234	5.029	4.836	4.656	4.486	4.327	11
12	6.492	6.194	5.918	5.660	5.421	5.197	4.988	4.793	4.611	4.439	12
13	6.750	6.424	6.122	5.842	5.583	5.342	5.118	4.910	4.715	4.533	13
14	6.982	6.628	6.302	6.002	5.724	5.468	5.229	5.008	4.802	4.611	14
15	7.191	6.811	6.462	6.142	5.847	5.575	5.324	5.092	4.876	4.675	15

PFM4 - PUBLIC SECTOR FINANCIAL MANAGEMENT SUGGESTED SOLUTIONS

SOLUTION ONE

S/N	a) The basic steps in budget preparation in the Public Service
	<ul style="list-style-type: none"> • The first step in budget preparation should be the determination of a macroeconomic framework for the budget year (and ideally at least the next two years). The macroeconomic projections, prepared by a macroeconomic unit in the Ministry of Finance or elsewhere, should be agreed with the Minister of Finance. This allows the Budget Department within the Ministry of Finance to determine the global level of expenditure that can be afforded without adverse macroeconomic implications, given expected revenues and the level of deficit that can be safely financed. In a few countries, there are fiscal rules in place that may limit total spending or recurrent spending. • The second step should be the allocation of this global total among line ministries, leaving room for reserves (a separate planning and a contingency reserve as explained below) to be managed by the Ministry of Finance. • The next step should be for the Budget Department to prepare a budget circular to give instructions to Line Ministries, with the indicative aggregate spending ceiling for each Ministry, on how to prepare their estimates in a way that will be consistent with macro objectives. This circular will include information on the economic assumptions to be adopted on wage levels, the exchange rate and price levels (and preferably differentiated price levels for different economic categories of goods and services). • Step four is the submission of bids by Line Ministries to the Budget Department. Once received there needs to be an effective "challenge" capacity within the Budget Department to test the costing of existing and any new policy proposals. • The next step comprises the negotiations, usually at official and then bilateral or collective Ministerial level, leading finally to agreement. • Finally, step six is Cabinet endorsement of the proposals for inclusion in the budget that will go to Parliament.
	b) Advantages and Disadvantages of Planning
	Advantages of Planning <ul style="list-style-type: none"> • Planning leads to more effective and faster achievements in any organization. • Since planning foresees the future and also makes a provision for it, it gives an added strength to the organisation for its steady growth and continuous prosperity. • It secure unity of purpose, direction and effort by focusing attention on the objectives. Hence, unnecessary duplication, overlapping and cross-purpose workings are eliminated. • It ensures an even flow of work, minimizes false steps and protects against unwanted deviations. • It enhances the efficiency of other managerial functions.

- It provides an effective basis for control in all organizations whether small or big.
- It facilitates the process of decision-making.
- It enables the management to implement future programmes in a systematic way so that the management may get the maximum benefit out of the programmes framed. It enables all the activities to be conducted in an orderly and coordinated manner in order to achieve the common goals.
- With the rapid growth of technological development, it is essential for a manager to keep abreast of the up-to-date technology. Planning helps in this process.
- Planning encourages the sense of involvement and team spirit. Planned targets provide a basis upon which good performances can be rewarded and poor performances can be improved.
- Planning is the essence of all management activities. Once it is done well, other activities automatically follow.
- It educates people. It orients people. It gives them a sense of direction and the stimulating feeling that their efforts are being put to useful purpose, rather than being wasted. They begin to feel that they are worthy partners in an organization.

Disadvantages of Planning

Planning aims at forecasting and providing a means for examining the future and drawing up a plan of action. The very purpose of planning is to develop creative and innovative policies to guide company's activities in the market place. This is not an easy task. There are many obstacles in the path leading to successful planning. They are:

- Accuracy of facts and information about the future is one of the limitations of planning. "no manager can predict completely and accurately the events of the future". Managerial planning can be made accurately only if the events in future are predicted accurately. Often adequate facts may not be available.
- Time, money and effort are required in the collection and analysis of data and in the formulation and revision of plans. It is a time consuming process. It is an expensive process. Planning is useful only when the expected gains from it exceed its costs. Often it is remarked that the cost of planning is in excess of its actual contribution.
- Planning takes time i.e., adequate time. Sometimes, it may cause delay in taking decisions. A manager may be bogged down by procedures, rules, etc., when quick decision is essential.
- Planning may create a false opinion that all problems will be solved if the plans are implemented. In practice, management has to revise the plans continuously and check on their execution.
- Another major limitation of planning is that there are various alternatives to combat certain problems. Every alternative has its own merits and limitations. Every alternative presents different results also. In this way, diversity of alternatives cause many difficulties in the way of formulating planning.
- The effectiveness of planning may be greatly influenced by external forces, the controllability of which is not in the hands of planners. Government control, natural calamities, etc., may create hurdles in the implementation of managerial plans.
- It makes the entire organizational set up extremely rigid.

	<ul style="list-style-type: none"> • It leads to probable results and not assured goals. • In the planning process, the quality of the output depends upon the quality of input. • It encourages a false sense of security against risk of uncertainty. 																												
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Secondary Education	1,241,100	6,292,000	8,235,0																										
Youth and Adult Literacy	280,500	920,000	1,120,0																										
Management and Support Services	277,710	942,000	890,300																										
Total	4,280,910	17,504,000	20,817																										
	d) Evaluating the extent to which the programme outputs in the 2022 budget will be achieved given the reduction in revenues.																												
	<ul style="list-style-type: none"> • The programme outputs in 2022 will not be achieved as projected due to non-availability of resources. Therefore there is need for Government of Hawks Republic to revise the programme outputs in line with the resources that have been available to the Education Sector. 																												
	e) What are the pros and cons of extra budgetary funds																												
	Pros																												
	<ul style="list-style-type: none"> • Can increase efficiency by simulating private market conditions where levels and standards of service are linked directly to fees or charges. 																												

- Can provide more consistent source of funds for expenditures that yield high benefits yet do not get much recognition (road maintenance expenditures are a primary example).

Cons

- Can result in a loss of aggregate expenditure control; such expenditure may be outside the control of Ministry of Finance.
- Can distort allocation of resources by circumventing the budget process and review of priorities.
- Earmarked revenues can become entrenched so funding is no longer based on priority needs.
- Less transparency may lead to inefficiency and/or misuse of funds.
- Can facilitate rent-seeking and abuse of monopoly power.
- Leads to less flexibility at the margin to reallocate when budget is under stress.
- Is incompatible with good cash management practices.

SOLUTION TWO

(a)

INTERNAL STAKEHOLDERS

Medical staff
Board of directors

EXTERNAL STAKEHOLDERS

Minister of health
The Medical Authority
the media
The public
The Pharmaceutical Authority
Patients
NGO's
Trade Unions

(b)

		Low	High
Influence High	(4) Medical Authority, Pharmaceutical Authority		(1) Minister of health & board of directors
	(3) The General Public & the Media & NGO		(2) Medical Staff & Trade Union & Patients

Quadrant 1.

Key stakeholders placed here have high influence and high importance and therefore need to be fully engaged on the strategy/project.

Quadrant 2

Stakeholders placed here can be highly important but having low influence or direct power, however need to be kept informed through appropriate education and communication.

Quadrant 3

Stakeholders here have low influence and low importance and care should be taken to avoid the dangers of unfavorable lobbying and therefore should be closely monitored and kept on board.

Quadrant 4

Stakeholders placed here can hold potentially high influence but low importance. Should be kept satisfied with appropriate approval and perhaps brought in as patrons or supporters.

SOLUTION THREE

a) Explain to the Authorities the advantages of Cashflow Forecast and how cashflow of an organization can be managed.

Advantages of Cashflow Forecasting

- Predict cash shortages and surpluses
- See and compare business expenses and income for periods
- Estimate effects of change (e.g., hiring an employee)
- Prove to lenders your ability to repay on time
- Determine if you need to make adjustments (e.g., cutting expenses)

How to Manage Cash flow of an Organisation

- **Cash flow analysis** - Cash flow projections do not guarantee the future. But, they do help you accurately estimate impending finances. A cash flow analysis will reveal if you have enough cash on hand to cover upcoming expenses.
- **Stick to your budget**-A budget is a tool that helps you accomplish your goals and make smart spending choices. Use the budget as a road map for your finances. At times, you may need to stray from your budget plan. Adjust your budget as the environment changes and unexpected expenses occur.
- **Cut costs** -To manage cash flow, you should review your costs periodically. By doing so, you might find cheaper alternatives to some of your expenses. Also, make sure you are not paying for unnecessary expenses. Get rid of costs that you do not need. And, negotiate with your vendors to get lower prices or longer payment terms.
- **Don't let late collection of revenue fall to the wayside**-Late-collection of revenue can be devastating to your cash flow. Keep following up to ensure revenues are paid on time.
- **Keep a cash reserve** -The cash reserve serves as an extra cushion for your cash flow. You can keep a cash reserve in a savings account. Only withdraw from the account during an emergency.

b) Prepare a presentation to the authorities on best practice of public debt management.

- An Institutional framework that recognizes the main activities be undertaken for Debt Management should be set up . Major decisions on foreign and domestic borrowing based on approved borrowing plans should be made by the office responsible for resource mobilization.
- Countries should enact legislation that defines the Government's authority to borrow , invest and enter into financial obligations such as guarantees , hedging and derivative transactions and amortize, redeem or repurchase debt.
- A Complete and up to date loan database for external and domestic debt of the public sector should be maintained.
- There should be co-ordination of policy formulation among the agencies and staff responsible for debt management , fiscal , monetary and exchange rate

policies of government while maintaining separate responsibility for each of the activities.

- Public Sector should not borrow more than sustainable levels determined on the basis of agreed ceilings for debt indicators . Borrowing above these levels would make it difficult to absorb external shock of the economy.

SOLUTION FOUR

Project A

Year	Capital Outflows	Inflows	Proceeds	Net	DF 12%	Discounted values
0	(39,000)			(39,000)	1.000	(39,000)
1		18,000		18,000	0.893	16,074
2		22,000		22,000	0.797	17,534
3		20,000		20,000	0.712	14,240
4		16,000		16,000	0.636	10,176
5			15,000	15,000	0.567	8,505

NPV = K27,529

Project B

Year	Initial Cost	Working capital	Inflows	Proceeds	Net	DF 12%	Discounted Values
0	(54,000)	(30,000)			(84,000)	1.000	(84,000)
1			15,000		15,000	0.893	13,395
2			22,000		22,000	0.797	17,534
3		30,000	23,000	15,000	53,000	0.712	37,736

NPV = (K15,335)

Project C

Year	Initial Cost	Working Capital	Annual Inflows	Net	DF 12%	Discounted Values
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0	(60,000)	(25,000)		(85,000)	1.000	(85,000)
1		(31,000)	28,000	(3,000)	0.893	(2,979)
2			28,000	28,000	0.797	22,316
3			28,000	28,000	0.712	19,936
4			28,000	28,000	0.636	17,808
5			28,000	84,000	0.567	47,628

NPV = K(20,009)

Project D

Year	Initial Cost	Inflow	Net	DF 15%	Discounted Values
0	(30,000)		(30,000)	1.000	(30,000)
1	-		-	0.870	-
2	(30,000)	25,000	(5,000)	0.756	(3,780)
3		22,000	22,000	0.658	14,476
4		18,000	18,000	0.572	10,296
5		18,000	18,000	0.497	8,946
6		18,000	18,000	0.432	7,776
7		18,000	18,000	0.376	6,768
8		18,000	18,000	0.327	5,886

NPV = K20,368

Comment:

All the projects, except project B yield positive NPVs and should therefore be undertaken by Alpha District Council.

b) Explain how uncertainty and risks could be considered in the investment process.

- **Adding a risk premium to the discount rate**

A premium may be added to the usual discount rate to provide a safety margin. Marginally profitable projects (perhaps the riskiest) are less likely to have a positive NPV. The premium may vary from project to project to reflect the different levels of risk.

- **Payback period**

Estimates of cash flows several years ahead are quite likely to be inaccurate and unreliable. It may be difficult to control capital projects over a long period of time. Risk may be limited by selecting projects with short payback periods.

- **Sensitivity analysis**

Sensitivity analysis typically involves posing 'what if' questions. For example, what if demand fell by 10%, selling price was decreased by 5%, etc. Alternatively, we may wish to discover the maximum possible change in one of the parameters before the project is no longer viable. This would be calculated for each input individually.

Probability distribution

A probability distribution of expected cash flows may be determined, and hence the expected NPV (EV) may be found together with risk analysis e.g. best possible outcome, worst possible outcome, probability of a negative NPV. A more sophisticated measure of risk is to calculate the standard deviation. This considers the degree of dispersion of the different possible NPVs around the expected NPV. The greater the spread of outcomes around the expected NPV, the higher the potential risk. The coefficient of variation should be calculated to compare projects.

SOLUTION FIVE

S/N	(a) Examples of Internal and External Operational Risks
	<p>Examples of Internal Operational Risks are:</p> <p>Employee Risk – Examples include fraud, data entry errors, lack of knowledge, loss of key employees.</p> <p>Process Risk – One source of process risk is from accounting or financial reporting errors, non-payment for goods and services, errors in the actual settlement and payment process of financial transactions.</p> <p>Technology Risk – Risk of potential failure of vendors acquired hardware , software and or communication devices, Issues involving capacity and compatibility, security breaches.</p> <p>Examples of External Operational Risks are:</p> <p>Financial Institution Risk – Potential operational failure on the part of the financial institution that perform daily transactions processing or communication failure.</p> <p>Legal and Regulatory / Compliance risk – Include potential lawsuit or other legal actions and need to comply with many regulations.</p> <p>Supplier Risk – Provision of substandard products that result in customer dissatisfaction.</p> <p>External Theft / Fraud – Payment process involving false invoices or cheque fraud or availing false bank details.</p> <p>Physical and Electronic Security – Risk may arise as a result of break in which could compromise critical information and safety of staff.</p> <p>Natural Disasters – These events range from power outage, earth quake or floods.</p> <p>Terrorism – Exposure to terrorism can be managed by increasing the physical security on both premises and employees.</p>
	<p>(b) Three critical factors to take into account when determining a risk management strategy for a Treasury Department</p>
	<ul style="list-style-type: none"> • Importance of the Organization Culture – Organization culture plays an important role in managing the overall operation risk. • Importance of Technology – It is important when devising a strategy to manage operational risk, with regards to technology. • Importance of Procedures – Procedure is critical to any organization because of the essential need to monitor and control them in relation to limits placed on authority and risk taking

	(c) The responsibilities of Treasury Department in operational risk management.
	<ul style="list-style-type: none">• Measure and Allocate the cost of each risk element so that risks factors are analysed in management decisions.• Managing exposure caused by accidental losses that arise from activities managed by treasury.

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 5: PUBLIC SECTOR AUDITING

THURSDAY 16 DECEMBER 2021

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question. You will be told when to start writing.
2. This paper is divided into TWO (2) sections:
Section A: One (1) compulsory question.
Section B: There are four (4) questions. Attempt any two (3) questions.
3. Enter your student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.
4. Do **NOT** write in pencil (except for graphs and diagrams).
5. **Cell Phones** are **NOT** allowed in the Examination Room.
6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.
7. All workings must be done in the answer booklet.
8. Present legible and tidy work.
9. Graph paper (if required) is provided at the end of the answer booklet.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.
SECTION A

This question is compulsory and must be attempted.

QUESTION ONE

The Zambian Network Corporation is a public company with a Board of Directors appointed by the Ministry of Commerce and Industry. The Zambian Network Corporation was formed under the Industrial Development Corporation. Its main mandate is to provide reliable and affordable internet communication systems to all the ten provinces of Zambia. Its Head Office is situated in Lusaka. The Chief Executive Officer reports directly to the Minister and his appointment is ratified by parliament.

The accounts department of The Zambian Network Corporation is centralized and managed by 10 full time accounting staff, headed by the Chief Accountant. It uses an Integrated Financial Management Information System known as IFMIS. The financial statements are prepared in accordance with International Public Accounting Standards. (IPAS).

Being in the telecommunications sector, the Zambian Network Corporation is expected to comply with the Zambia Environmental Management Agency (ZEMA) and the Zambia Information Communication Authority (ZICTA) regulations. Among other projects the company undertakes, is the erecting of telecommunication towers which are mostly near the game reserves in the remote rural parts of the country. Its main source of revenue streams comes from charges for internet connectivity and advisory services relating to the telecommunication sector.

Due to the outbreak of Covid-19, there has been an increase in demand for telecommunication services as most people are required to work online from home. Further, the demand for internet services has increased due to the online learning platforms and virtual meetings. This has led to an increase in revenue.

You have been appointed as Audit Supervisor in charge of a forensic investigation at Zambian Network Corporation. The management at Zambian Network Corporation feels a need for a forensic investigation to be conducted at Head Office as a result of an anonymous report to the Anti-corruption Commission concerning embezzlement of K120million which was meant for the upgrading of communication facilities in the lower Zambezi.

One auditor who was seconded to be part of the team to carry out the forensic investigation initially worked for The Zambian Network Corporation for the last one year before getting an audit placement at the Auditor General's Office. In order to gain an understanding of The Zambian Network Corporation (ZNC) and its environment, two of the auditors were tasked to visit the Zambian Network Corporation (ZNC) to obtain documents and make further inquiries. Further, the investigating team wishes to go through the permanent and current audit files for the Zambian Network Corporation where it is felt vital information to help with the investigation may be found.

Required:

- (a) Explain four (4) roles the Auditor General's Office plays in the audit of public institutions such as The Zambia Network Corporation.
(6 marks)
- (b) Evaluate the need for a forensic investigation at The Zambia Network Corporation.
(6 marks)
- (c) Explain four (4) documents that should be kept on the permanent file of The Zambia Network Corporation.
(6 marks)
- (d) Explain four (4) matters that the public sector auditors need to gain an understanding of the Zambia Network Corporation environment.
(8 marks)
- (e) Explain four (4) methods that the public sector auditors can use to gather audit evidence during the audit of Zambia Network Corporation.
(6 marks)
- (f) Briefly explain any four (4) fundamental ethical principles that need to be observed during the audit of The Zambia Network Corporation.
(8 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Attempt any THREE (3) questions.

QUESTION TWO

Southern Farmers Co-operative is one of the Government owned co-operatives under the Ministry of Co-operatives. The co-operative was formed by members from different Districts in the province. The objective of the co-operative is to be the most efficient, effective and economically viable entity among all co-operatives in the country.

Each member of the co-operative is required to contribute 10% of the total cost of the inputs in terms of fertilizers, seeds and chemicals that they receive from the co-operative. Upon harvesting the crop, each member is expected to deposit 80% of the income earned in the account of the Ministry of Agriculture that is maintained at the district. Each farmer is later reimbursed with the 10% they earlier deposited plus 70% of the sales, while 20 % is spent on operational costs of running the co-operative offices.

During the year, some members of the co-operative suggested the need for the co-operative to acquire the latest plant and machinery that is able to grind the grain, pack and load on the trucks. They argued that this was going to make the co-operative realize its main objective of being the best cooperative among all cooperatives in the country.

The auditors from the Auditor General's office are expected to conduct audits of all publicly owned entities including the Southern Farmers Co-operative. Further auditors were required to organize a workshop at which issues to do with quality audits especially *International Standard for Quality Control (ISQC) 1* and *ISSAI 40 Quality control for SAIs* were to be discussed. The workshop was expected to be completed before the audit commenced. This was as a result of complaints of poor quality audit work that was observed by the previous supervisor.

You are supervising the audit of Southern Farmers Co-operative and you have come across the following issues from the working papers that you are reviewing:

Issue number 1

There was a discovery of 25 bags of maize valued at K42, 000 missing. The record was there but the actual quantities were not found. The matter was considered material but not pervasive. The auditor concerned suggested that this could result in an adverse opinion.

Issue number 2

After an audit review of the working papers was conducted, it was found that the audit staff that went to conduct stock taking were prevented from accessing a substantial portion of the storage facilities. The amount of inventory of maize grain not verified was substantial. The matter was considered both material and pervasive. The auditor suggested that the matter should result in the issuance of a qualified opinion.

Required:

- (a) Discuss the appropriateness of the suggested audit opinions relating to issues number 1 and 2 above. (4 marks)
 - (b) Explain three (3) audit procedures for the audit of inventory at Southern Farmers Co-operative during and after the inventory count. (6 marks)
 - (c) Explain three (3) elements that can enhance quality controls as guided by ISQC1 and ISSAI 40 during the audit of Southern Farmers Co-operative. (6 marks)
 - (d) Explain the need for a performance audit on the acquisition of Plant and Machinery and explain its components at Southern Farmers Co-operative. (4 marks)
- [Total: 20 Marks]**

QUESTION THREE

Zambia Titling Agency is a Government entity founded on the premise of giving titles to owners of properties in gazetted townships. This was done in order to give security to the owners of the properties. It was also observed that some of these properties could be used as collateral in case the owners wanted to get loans from the banks. The targeted number of titles to be issued is two-million.

The following is a simplified process that is undertaken by an applicant before a title is issued.

1. A team of volunteers, supervised by a qualified person from the Ministry of Lands, go out to capture the details of the owner of the property. The details captured are National Registration Number (NRC), size of the plot and a sketch map of the plot.
2. Once the details are captured, they are sent to a central processing center where a register of all applicants is compiled.
3. After 3 weeks, the owner of the property is notified via a short messaging service (sms). They then go to the titling center at Heroes Stadium to verify if the details from the computer printout are correct.
4. Once details are confirmed to be correct, the owners are required to pay a sum of K1, 200 into a Ministry of Lands bank account. A Government receipt is issued which is taken to the offices situated at the Heroes stadium. Thereafter, a title is issued after three months.
5. In certain cases, the Ministry of Lands allows the differently abled persons to apply for titles online. The system is integrated with each disabled individual's mobile line. This was argued to be a better way of avoiding inconveniencing certain groups that are considered marginalized. In addition, an allowance of 2% for uncollected fees from those who had initially paid deposit is made. An Initial assessment of internal controls by Auditors indicates that internal controls in relation to titling process are not strong.

At one of the planning meetings, it was discussed that an Information Technology audit be conducted first before Financial; Compliance and Performance audits are conducted. Most of the members on the audit team for Zambia Titling Agency are audit trainees with no prior experience of auditing government agencies. They are also wondering how to audit a 2% allowance for possible uncollected fees. Further owing to the large number of titles to be issued, auditors are considering the use of analytical procedures in accordance with ISAAI 1520/ISA520.

Required:

- (a) Explain the meaning of an Information Technology audit, giving an example of how it can be applied in financial, performance and compliance audits. (5 marks)
- (b) Explain the benefits of planning for an audit in a public sector entity. (6 marks)
- (c) Explain three (3) audit risks under the headings of Control, Inherent and Detection risks in relation to the audit of Zambia Titling Agency. (6 marks)
- (d) Explain three (3) factors that auditors would consider before using analytical procedures. (3 marks)

[Total: 20 Marks]

QUESTION FOUR

Fitwala University of Zambia is a publicly funded institution of higher learning. Recently the University embarked on the following activities:

1. The Fitwala University of Zambia leased part of its land to a property developer to build a shopping mall that will be put on rent. The construction cost is estimated to be K285m. This will be partly funded by the developer and later to be handed over to Fitwala University of Zambia management after a period of 10 years.

The Managing Director and Chief Executive Officer of the property development company, is a former Fitwala University of Zambia Vice Chancellor. He was hand-picked by The Fitwala University of Zambia management alleging that he is a well-known person of integrity and that there was no need to advertise the position.

2. The Fitwala University of Zambia has 10 scholarships that it awards to intelligent students from disadvantaged families. The applicants are scrutinized by officers from the Ministry of Community and Vulnerable groups. Successful candidates are then enrolled on The Fitwala University of Zambia programs. One of the supervisors on the audit of The Fitwala University of Zambia got to know of the scholarship and was given two places by the Vice Chancellor of The Fitwala University of Zambia.
3. The property developer will facilitate the acquisition of shares for University staff in the shopping mall once the mall is listed on the stock exchange.

Mr. Mwenzo a Senior Auditor in the Office of the Auditor General's office previously worked in the accounts department at Fitwala University of Zambia. He was in charge of preparing financial reports as well as internal audit work. He is now leading the audit of Fitwala University of Zambia. During the year, the Fitwala University of

Zambia received bad media publicity from the public due to allegations of mismanagement of funds.

One of the former employees in the accounts department sued Fitwala University of Zambia for wrongful dismissal on allegations of embezzlement of funds. Management approached Mr. Mwenzo to be a witness in court regarding the case.

During the year, a government funded project for training of public accountants in International Standards for Public Auditors commenced. Among other topics to be deliberated at the training workshop is the operations of the International Organisation for Supreme Audit Institutions (INTOSAI). In addition, participants to the training workshop are expected to learn how to apply a conceptual framework for public sector financial statements and to prepare specific and general purpose financial reports.

Required:

- (a) Identify and explain three (3) ethical issues and suggest suitable responses relating to the audit of The Fitwala University of Zambia. (6 marks)
- (b) Explain the relationship that exists between Parliament, the Office of the Auditor General and the Executive. (3 marks)
- (c) Explain the following :
 - (i) Authority of conceptual framework for General Purpose by Public Sector Entities such as The Fitwala University of Zambia. (2 marks)
 - (ii) Specific Purpose Financial Reports (3 marks)
 - (iii) General Purpose Financial Reports (3 marks)
- (d) Explain three (3) factors that will assist auditors in determining whether external confirmations can be used as substantive procedures. (3 marks)

[Total: 20 Marks]

QUESTION FIVE

The Office of the Auditor General is the Supreme Audit Institution (SAI) in Zambia. It was created by an act of Parliament. As an independent institution, it is expected to audit all institutions such as Ministries and Government Agencies.

Despite being a creation of parliament, the Office of the Auditor General, does not report to any Ministry. It is expected to audit government institutions and prepare independent audit reports that it submits to parliament. Reports are handed over to the Public Accounts Committee. Therefore, a special relationship exists between the Government, Parliament and the Office of the Auditor General (OAG) known as the *Triangle of Accountability*.

In order to strengthen internal governance systems in public corporations, it is required that a public sector audit committee should be established as one of the committees on the Boards of Directors of such entities.

The types of audits that require to be undertaken by the Supreme Audit Institution include compliance, financial, Information Technology and performance audits. ISSAI 100 *Principles*

of public sector auditing identifies three elements of all public sector audits that apply to all the different types of public sector audits.

Required:

- (a) Explain the three (3) elements of a public sector audit engagements in accordance with ISSAI 100 *Principles of public sector auditing*. (6 marks)
- (b) Outline the functions of a public audit committee of the Board of Directors. (4 marks)
- (c) Explain how the Office of the Auditor General manages to maintain its independence despite it being a creation of parliament. (6 marks)
- (d) Explain the difference between compliance audit and a financial audit. (4 marks)

[Total: 20 Marks]

END OF PAPER

PFM5: PUBLIC SECTOR AUDITING SUGGESTED SOLUTIONS

SOLUTION ONE

(a) Roles of the Auditor General (AG)

- (i) They audit financial statements such as Profit or Loss and Statements of Financial Positions that are prepared by various Ministries and state controlled corporations.
- (ii) Performance audits-The AG also conducts performance audits in relation to how public institutions are using the funds in terms of Efficiency, Economical and Effectiveness. This is referred to as a Value for Money or VFM audit.
- (iii) They also conduct compliance audits. Compliance audits are performed in order to ascertain whether these public institutions are performing in accordance with the laws and regulations that govern the respective sectors.
- (iv) The AG has a responsibility to express an independent opinion on whether financial statements present a true and fair view.
- (v) The AG performs audit on how the funds allocated to various Government entities are being used. By providing such an oversight, they are safeguarding the interest of the public so that funds for essential services are not misused.

(b) Forensic audit will be required for the following reasons:

- (i) There is information that some funds have been misapplied or there is existence of fraudulent activities being perpetuated by some accounting staff .Therefore in order to establish the extent fraudulent activities and the culprits involved, an independent forensic investigation should be carried out.
- (ii) It is not possible to establish who is involved. Therefore in order to establish the extent fraudulent activities and the culprits involved, an independent forensic investigation should be carried out.
- (iii) The investigation will be carried out in a confidential manner other than that carried out during a routine audit. No single member in the accounts department will have a chance of knowing that a forensic audit is being carried out.
- (iv) The amounts that have been lost will need to be established .Therefore a forensic audit will be needed in order to ascertain the amount of economic loss arising from fraudulent activities.

(c) The following documents will have to be kept in the auditor's permanent files.

- (i) Copies of memorandum and articles of association – this is a document in which information such as name of the institution , its location , required amount of capital or funds ,and the names of the members to be contacted.
- (ii) Chart of accounts – this is a document which will show numerically a list of assets, liabilities, share capital and expense accounts.
- (iii) Organisation chart – this shows the entity's structure in terms of authority , responsibilities and the level of seniority from the Chief Executive Office to the lowest staff in the organisation.
- (iv) Minutes of previous meetings-these will be of containing importance to be referred to in future.
- (v) A copy of the engagement letter with details of the responsibilities of management and the public sector auditor.

(d) The following matters should be considered when gaining an understanding of a public sector organisation.

- (i) Relevant laws and regulations that governs the industry or ministry in which the entity operates.
- (ii) The relevant financial reporting framework such as the IPSAS.
- (iii) Understanding the relevant knowledge of government regulations relating to IT
- (iv) Understanding public policies and how they can impact on risks assessments
- (v) The reporting system within and who the board of directors at ZNC reports to.
- (vi) Understanding the governance structure –this is important as the structure in a government controlled entity is different from that in a private sector entity.

(e) The following are the methods that AG can use to gather audit evidence:

- (i) Observations –auditors need to select procedures that need to conform to the laws and regulations. They should then observe and make judgment whether such procedures are carried out in accordance with the stated laws and regulations.
- (ii) Inspections – external auditors from the Auditor General Office need to inspect documents, books of accounts to confirm whether the details are prepared in accordance with the expected public sector accounting framework.
- (iii) External confirmation-written confirmation from external parties can confirm how funds have been obtained and used as opposed to oral explanations from the same entity/ client.

- (iv) Inquiry of management –external auditors from the Auditor General’s office will seek information by asking relevant personnel from management and accounts department. They then compare such responses with other relevant information.
- (v) Analytical procedures – these can be used to establish a plausible relationship between financial data and non-financial data in order to auditors to gain a full understanding about trends and patterns of certain information.

(f) Fundamental ethical principles:

- (i) Confidentiality –external auditors from the Auditor’s General will mostly like come across information which is confidential. This information should not be divulged to anybody as that will be unethical , unless prior permission is given by the client.
- (ii) Professional skills and due care-external auditors are experts that have been entrusted with the responsibilities due to their special training and skills they possess. They are therefore competent and not to accept any work for which they are not qualified to perform.
- (iii) Professional behavior – while carrying an audit, external auditors are expected to behave in a manner that does not discredit the name of the institution such as ZICA and then bring the name of the profession into disrepute.
- (iv) Objectivity – they should not promote any interest or to be bias towards a particular when coming up with an opinion.

SOLUTION TWO

(a) **Issue number 1**

The discovery of 25 bags valued at K42 000 that were missing. This matter was assessed as material and not pervasive. An adverse opinion can only be expressed if the matter was both material and pervasive. The appropriate opinion would be a qualified opinion.

Issue number 2

Auditors were not given access to a large number warehouse for them to verify existence and condition of the grain. The matter was assessed as both material and pervasive. The auditor proposed a qualified opinion which was wrong. The appropriate audit opinion should have been a disclaimer of opinion.

(b) The three audit procedures that can be performed during the audit of inventory of Southern Farmers Cooperatives are:

- (i) Observations- auditors need to attend an inventory count and observe how the client whether client staff are adhering to count instructions.
- (ii) Test counts- the count will be done in order to ascertain whether internal controls relating to counting are working.
- (iii) Confirm whether procedures for identifying obsolete and slow moving goods are working properly by reviewing count instructions.
- (iv) External auditors also need to confirm whether any bags of maize that belong to third parties have been separated from that which belong to Southern Farmers Cooperative.

(c) **The following elements can enhance quality for an SAI**

- (i) Leadership responsibility for quality –
An SAI should be able to promote a culture whereby all accounting staff abide by the policies and procedures relating to a quality audit.
- (ii) Relevant ethical requirement- all members of staff are expected to follow all the five fundamental ethical principles that can contribute to a quality audit.
- (iii) Acceptance and continuance-in order to carry out a quality audit, an SAI should assure the client that they have competence, resources and time.

(d) A performance audit is conducted in order to assess whether the investment was Economical, Efficient and Effective. In the case of Southern Farmers Co-operative the performance audit can be undertaken as follows:

- (i) Economy –it means minimizing the cost of resources used by a public sector entity such as time and human costs spent for activities without compromising quality. In addition, external auditors will have to make an

assessment as to whether the benefits or revenue streams from investments in technology and other capital expenditure exceeds the best cost.

- (ii) Efficiency –external auditors from an SAI should make an assessment as to whether a public sector entity had applied its resources (input) have been put to optimal or satisfactory use.
- (iii) Effectiveness- external auditors have to make an informed opinion as to whether the investments and policies are helping the entity to achieve its objectives of being the best cooperative in the whole country.

SOLUTION THREE

(a) The meaning of an IT audits:

When a public entity uses information to process data, it is assumed that the system functions correctly and that IT controls will reduce risks to an acceptably low level. Therefore an IT audit is an examination and review of IT systems and related controls to gain assurance or identify, violations of the principles of legality, efficiency, economy and the effectiveness of IT systems and related controls.

The three examples in which an IT audit can be applied to:

- (i) Financial audits –financial statements are prepared from transactions that are imputed into the accounting system. The system processes the input and gives out output. The results from a computer system can only be credible if internal controls systems relating to IT are working effectively. Therefore an IT audit is paramount before any other audits are conducted.
- (ii) Compliance audits- IT systems audits are part and parcel of compliance audits. An IT audit will be conducted in order to verify whether its operations are not overstepping the boundaries in relation to laws and regulations.
- (iii) Performance audits – it is an audit that covers Economy, Effectiveness and Efficiency. An IT audit can contribute to the better assessment as to whether the client is able to achieve value for their money. This will also entail confirmation as to whether the IT itself is able to achieve greater outputs at minimal cost.

(b) The benefits of planning for an audit in public sector organisation are:

- (i) An auditor can allocate adequate time and resources to risk areas if the planning was done properly.
- (ii) It helps an external auditor to identify risky and potential problems early, which can occur during an audit.
- (iii) If planning is considered first before an audit is carried, external auditors can conduct audits much more effectively and efficiently.
- (iv) Planning can also help to assess the type of audit staff are suitable for a given public sector organisation such as Zambia Titling Agency.
- (v) When an audit plan is considered well in advance, an engagement partner will be able to direct, supervise other audit members.
- (vi) Planning can help to coordinate the work of component auditors especially if the client is in a group system.

(c) The following are the audit risk in relation to the Audit of Zambia Titling Agency:

- (i) Control Risks - There are lot of processes involved before titles are issued. There has not been a deliberate check if all the cash being received are recorded correctly. There is also a system in which titles are being processed quickly for disadvantaged groups such as disabled families. There has not been a mention as to whether there are checks and balances as to whether the system can be hijacked by people who are not in the category of those marginalized groups.
- (ii) Detection risk – the AGs office has a good number of trainee auditors .Therefore, they are likely to design audit procedures that may not detect material misstatements in the financial statements of a public sector entity.
- (iii) Inherent risks – these arise due to the nature of the entity or certain transactions that are estimates and can be misstated individually or when aggregated with other misstatements. For instance the Cooperative has an allowance of 2% for uncollected fees.

(d) Factors to consider before analytical procedures are used;

- (i) The Suitability of particular analytical procedures –external auditors need to determine which analytical procedures are to be used for certain assertions. Substantive analytical procedures will be suitable in this case as the number of titles involved in huge (two-million)
- (ii) The Reliability of data-auditors needs to be assured of the reliability of data captured from applicants for titles. They are also need to determine whether internal controls relating payments and processing of titles is strong. Indication in the scenario is that internal controls are weak.
- (iii) Auditors need to consider whether there is an expected amount or ratio will exist. In addition they also need to consider whether there is a sufficient way of identifying a misstatement from financial reports of Zambia Titling Agency.
- (iv) Acceptability of the difference-auditors needs to take into account whether the amount of the difference can be within acceptable limits without conducting any further investigations.

SOLUTION FOUR

(a) Ethical issues

- (i) Advocacy threat- Mr. Mwenzo, an auditor leading audits for Fitwala University has been asked to be a witness in the case were the University has been sued. This will compromise the independence and objectivity of the audit. It is advisable that he declines the task of being a witness in this particular case.
- (ii) The offer of scholarships to two relatives of auditors. This will compromise the independence and objectivity due to this gift or assistance. They should not have accepted this offer and therefore should have declined.
- (iii) Familiarity / Self-review threat – Mr. Mwenzo has been a Senior Auditor in the office of the AG .He previously worked with some of the accounts staff at the client before joining the Auditor General’s office. His is familiar and also is likely to come across or audit some of the work that he had prepared. Therefore it is important that he is not involved in the audit of this client.

- (b) There is a special relationship that exists between the Parliament, the Office of the Auditor General and the Executive. The president or executive appoints the Auditor General and Parliament is given the powers to ratify the appointment. The office of the Auditor General therefore assures the public of Government accountability through the audits of various public institutions that receive funding from the government.

(c) Explanation of meanings of the following:

- (i) **A conceptual framework** establishes the authority for requirements for Financial Reporting for a public sector entity such as Fitwala University. It just gives guidance on the issues that are not referred to by IPSAs or Recommended Practice Guidance (RPGs).Therefore public sector accountants and the others can refer to definitions, recognition criteria, measurement principles, and other concepts as mentioned in the conceptual framework.

(ii) Specific Purpose Financial Reporting Framework

These are Special Purpose Financial Reports (SPFR) for public entities. They are prepared and tailored towards the needs of specific users such as Government. Even in this case, the International Public Sector Board (IPSAB) expects that International Public Sector Accounting Standards (IPSASs) are being followed.

(iii) General-Purpose Financial Framework

These are much more comprehensive public sector financial statements that may include both the specific requirements for certain users and the scope is also widened to include even those that may not require specific reporting issues.

- (d) The following factors will be used to assist auditors to determine whether confirmations can be used as substantive procedures:
- (i) The ability of the willing intended third party to respond auditors.
 - (ii) The cost involved maybe more and the auditors will decide to sue substantive procedures instead of information from the third party.
 - (iii) Where the responsible party operates in an environment in which confirmations are not an aspect of day-to-day operations.
 - (iv) Where the respondent is close to the entity and responding to a confirmation maybe less reliable.

SOLUTION FIVE

(a) Elements of public sector audit engagements:

- (i) Three parties to the audit engagement namely:
 - The public sector auditor
 - The responsible party who is subject to the public sector audits.
 - The intended users who may be parliament and the public.
- (ii) The criteria which are the benchmarks used for assessing the subject matter.
- (iii) The resulting subject matter information – which refers to the outcome of measuring and evaluating the subject matter against the criteria.

(b) A Public Audit Committee:

This is the committee that is formed as the special committee on the Board of Directors for a public sector entity. The major roles are as follows:

- (i) It provides a forum on which both internal and external auditors from the office of the AG can freely discuss their concerns.
- (ii) It is a committee that assesses the policies and procedures regarding internal controls and make recommendations where possible.
- (iii) They provide a forum at which disputes that can arise between internal and external auditors can be resolved.
- (iv) The Public Audit Committee can also liaise with the auditor's office before some input from the audit of that entity are transferred to the final auditor's report.

(c) Auditor General Independence:

The Auditor General's office is created by the executive via an act of parliament. Parliament debates who the head will be as Auditor General. The AG is funded by Government which will be audited by the same office. The government is held accountable through the work of Auditor General's office.

The independence of the AG is guaranteed through the constitution and other details in the legislation. As per Lima declaration, the independence of decision makers of the SAI is guaranteed as their removal is embodied in the constitution.

After the report is ready, AG or SAI submits to the Parliamentary Accounting Committee (PAC). The PAC can summon any erring member of staff especially controlling officers from the respective Ministries that are cited in the report.

(d) Difference between compliance audit and financial audits:

A compliance audit is undertaken by auditors in order to verify whether the public sector entity has followed all the laws and regulations. These laws could be those that applies to the industry and those to do with the reporting framework. On the other hand a financial audit is an audit in which an independent auditor examines the books of accounts in order to establish in all material respects, whether the financial statement show a true and fair view, in accordance with an applicable financial reporting framework. Compliance audit is for a short period of time as compared to a financial audit which is extensive and detailed using International Public Sector

Accounting Standards (IPSAS). In addition, in compliance audit, a public sector auditor does not specify an opinion but incorporates it into an overall audit report.

In case of a financial audit, an external auditor examines various pieces of audit evidence in order to form an opinion whether financial statements show a true and fair view or not.

END OF SOLUTIONS