



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 1 : PUBLIC SECTOR ACCOUNTING

MONDAY 12 DECEMBER 2022

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 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.

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

Public Financial Management (PFM) involves a number of key players with different responsibilities and different roles to play at various stages of the budget cycle. It is important for Parliament's oversight and monitoring of PFM processes and performance that Members of Parliament and Staff of the National Assembly have a clear understanding of the division of roles and responsibilities between these players.

Required:

- (a) Explain the role of the Ministry of Finance and Controlling Officers in the management of public financial resources. (13 marks)
- (b) Explain the role of internal auditors in the management of public resources. (10 marks)
- (c) Describe the different components of the public sector. (6 marks)
- (d) Outline the qualitative characteristics of information included in General Purpose Financial Reports (GPFRs) of public sector entities. (8 marks)
- (e) Explain the meaning of budget deficit. (3 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section

Attempt any THREE (3) questions.

QUESTION TWO

You have been working as Senior Accountant at the Ministry of Finance and four (4) new accounting officers have just been recruited for the Ministry. As a graduate holder of Diploma in Public Sector Financial Management, you have been requested to brief the new recruits over the following matters as the Ministry is preparing for the 2023 budget presentation to Parliament:

Required:

- (a) The main functions of a government Financial Management System. (10 marks)
- (b) The role of the legislative framework in the Financial Management System of the Government. (4 marks)
- (c) The main processes of the Financial Management System. (6 marks)

[Total: 20 Marks]

QUESTION THREE

Accounting is a business language, and it is concerned with measurement of financial performance of an organization by recording, analyzing, and reporting operating stakeholders. Since all stakeholders should understand the accounting language in the same sense, certain principles, concepts and policies of accounting have been laid down.

Required:

- (a) Distinguish between accounting principles and accounting policies. (5 marks)
- (b) Briefly describe five (5) accounting principles. (5 marks)
- (c) Briefly describe five (5) accounting policies. (5 marks)
- (d) Briefly describe five (5) accounting concepts. (5 marks)

[Total: 20 Marks]

QUESTION FOUR

A chart of accounts can help the public sector to classify and analyze public sector income and expenditure in a more efficient manner. With a simplified chart of accounts, record keeping and filing could be made much easier.

Required:

- (a) Describe a chart of accounts and give four (4) reasons why a public sector organization should use a chart of accounts (10 marks)
- (b) Explain any five (5) risks related to a computerized accounting system and their mitigation measures. (10 marks)

[Total: 20 Marks]

QUESTION FIVE

The Government Republic of Zambia has had series of reforms related to cash management. However, the most remarkable and impactful reform was undertaken during the 2014 to 2018 under the PFM Reform Project. One of the key components of this reform has been strengthening Integrated Financial Management Information System (IFMIS) and Cash Management through Treasury Single Account (TSA). The component's aim is to enhance financial management systems and standards in order to promote good public sector governance practices. Some of the key milestones were the establishment of a functional structure of Treasury Single Account (TSA) in 2015 and the inclusion of the clause under section 40 of the Public Finance Management (PFM) Act, 2018 which provides for all monies received for aided projects by way of loans, grants and donations to constitute public monies and to be paid into the Consolidated Fund. Currently the TSA has been rolled out to fifty-nine (59) spending heads out of sixty-two (62) and the bank accounts of these spending heads have been partially closed and the cash balances consolidated into the TSA account at the Bank of Zambia. The fifty-nine (59) heads have approximately two (2) accounts each translating to 118 accounts held at Bank of Zambia.

Required:

- (a) Explain the five (5) benefits of implementing TSA to the Government. (10 marks)
- (b) State five (5) challenges faced by Government in the implementation of the TSA. (5 marks)
- (c) Suggest five (5) recommendations to addressing challenges faced by Government in the implementation of the TSA. (5 marks)

[Total: 20 Marks]

END OF PAPER

PFM 1 PUBLIC SECTOR ACCOUNTING SUGGESTED SOLUTION

SOLUTION ONE

(a) The Ministry of Finance in Zambia is responsible for the formulation of economic development policies and the economic management of the affairs of Government in order to achieve faster and sustainable economic development. The Ministry is also the principal actor in policy formulation in respect of public finance and as such responsible for the financial soundness of Government's economic policies and for the proper control of revenue and expenditure. The Secretary to the Treasury has the responsibility to ensure that the functions of the Ministry are carried out economically, efficiently and effectively, and its objectives duly achieved.

On the other hand, as provided for in the current regulatory framework, the Controlling Officer is the Chief Accounting Officer in respect of all public moneys collected, received and disbursed on behalf of a Ministry or department. Controlling Officers play a key role in public financial management and are charged with the duty of planning and controlling the expenditure of public funds.

Duties of controlling officers include the following:

- i) Maintenance of an effective, efficient and transparent system of financial and risk management and internal control;
- ii) Maintenance of a system of internal audit under the control and direction of an audit committee complying with and operating in accordance with the Public Finance Act;
- iii) Maintenance of an appropriate procurement and provisioning system in accordance with the Zambia Public Procurement Act;
- iv) Maintenance of a system for properly evaluating capital projects;
- v) Ensuring effective, efficient, economical and transparent use of the resources under their control;
- vi) Preventing unauthorised, irregular and wasteful expenditures and losses resulting from negligence and criminal conduct;
- vii) Immediately reporting, in writing, particulars of the expenditure to the Secretary to the Treasury on discovering any unauthorised, irregular or wasteful expenditure, referred to in (vi);
- viii) Taking immediate, effective and appropriate disciplinary steps against any officer in the Ministry or department who contravenes or fails to comply with the provisions of the Act; and

ix) Not committing Government to expenditures in excess of money appropriated by Parliament.

(b) Internal auditors' responsibilities include:

- i) Reviewing compliance with the existing Government financial regulations, instructions and procedures;
- ii) Evaluating the effectiveness of internal control systems;
- iii) Appraising the economy and effectiveness with which financial and other resources are being used;
- iv) Reviewing the reliability and integrity of record keeping and reporting on financial and operating information systems;
- v) Pre-auditing of payments documents and of all the documents used in initiating commitments, as well as contract agreements;
- vi) Verifying and certifying periodical financial returns such as expenditure returns, revenue returns, staff returns and vehicle returns;
- vii) Reviewing and pre-auditing annual appropriation accounts, fund accounts and other accounting statements to ensure that accurate accounts are prepared to required standards;
- viii) Investigating irregularities identified or reported and reporting on cases leading to wastage of resources or cases of general misuse or misappropriation of financial resources and Government property;
- ix) Ensuring that revenues and other receipts due to the government are collected promptly, banked immediately and are fully accounted for;
- x) Carrying out spot checks on areas such as revenue and receipt collection points, project supply and delivery sites, to ensure compliance with procedure and regulations;
- xi) Reviewing budgetary controls on issuance of warrants, commitments, expenditures, revenues and accounting from time to time;
- xii) Ensuring that the Government's physical assets are appropriately recorded and are kept under safe custody; and
- xiii) Reviewing the budgetary allocation process to ensure legislative and administrative compliance and advising when commitments are made without budgetary provision or adequate cash.

(c) The components of the public sector:

1 – General Government

- i) Central government
- ii) State government
- iii) Local government

2 – Public Corporation

- i) Public non – financial corporation
- ii) Public financial corporation

(d) The qualitative characteristics of useful information are:

Understandability - Taking into account that users have a reasonable knowledge of business and a willingness to study information with reasonable diligence, the financial statements should be prepared in such a way as to be easily understood by such users. This can be enhanced by avoiding use of words that are too technical and use of easy to follow presentations.

Comparability - Use of accounting methods/measurements should be consistent from one year to another or from one company to another; whose results are subject to comparison. Inconsistent methods of accounting for similar transactions will render the financial results incomparable.

Timeliness - Every time financial statements are prepared, they need to be prepared and reported quickly in good time for their use for specified decisions to be passed.

Verifiability - Financial statements need to be supported by written or verbal representation for them to be deemed valid and hence useful.

Relevance – Information is capable of making a difference to users of such information if it has predictive value, confirmatory value or both. For information to be relevant it should be material and provided timely.

Faithful representation – information must be complete, neutral and free from material error. Substance over form is implied.

(e) Budget deficit is the situation where government expenditure estimates outweigh the government total revenue estimates

SOLUTION TWO

(a) Functions of government Financial Management System include:

i) **Macro-fiscal planning**

This involves the establishment of policy objectives, needs for financial resources and a forward-looking strategy for revenue and expenditure. For instance, a fiscal plan would comprise statements of government objectives; a resource framework for the plan period and implementation program during the period

ii) **Budget preparation**

This activity involves allocating resources to various wings of government in order to achieve the objectives of government. It is a tool for both managing national economic and fiscal planning and controlling the use of funds to ensure government objectives are met.

iii) **Budget implementation**

It follows budget approval by the legislature. It involves allocation of funds to specific areas and execution of budget in those areas.

iv) **Budget monitoring and evaluation**

This activity provides feedback to the fiscal planning and policy unit. The feedback helps financial managers to adjust planned activities for the forthcoming periods.

v) **Cash management**

It involves provision of an up to date picture of the amount of cash in government accounts and amount of cash needed. Cash management compares data from cash flow forecasts and fiscal reports to data on cash balances, government bonds, treasury bills and cash deposit maturities.

vi) **Debt management**

It involves managing all transactions relating to external loans. It serves as the mechanism for calculating the future cost of servicing the debt.

vii) **Foreign aid management**

Financial Management Systems match aid agencies to projects and oversees the process of project negotiations and implementation.

viii) **Revenue administration**

Financial Management Systems are government's tool for execution of tax policies through the levy and collection.

ix) **Accounts administration**

It involves government assembling and analyzing accounting information to help it to control business, safeguard assets and prepare financial statements that comply with legislation.

x) **Auditing**

It involves the reviewing of the accuracy and reliability of financial information produced by financial management functions.

(b) The role of the Legislative Framework

Financial management functions and processes are derived from and must adhere to a legislative and regulatory framework or control structure as follows:

- i. Legislation and financial instructions help to define the functional areas that govern financial management. Instructions detail controls needed to ensure that transactions are properly authorized and documented and that they do not exceed the amount of money assigned for the purpose.
- ii. Legislation also require that revenue received by the government is first paid into a fund, and any expenditure from the fund is formally authorized and appropriated.
- iii. Regulation specify the standards and procedures to be followed when carrying out functional processes. Some controls specific to this role are:
 - ✓ Controls at document and transaction level
 - ✓ Controls on access to ensure that only authorized personnel can record, change and report information
 - ✓ Controls over the entire system to ensure that it embodies the established processing standards.

It is therefore very important for an accounting officer to thoroughly understand laws, regulation and controls they need to apply when analyzing financial management systems.

(c) The main processes of the financial management systems include:

i) budget preparation

This process involves:

- making initial budget allocation to agencies and programmes
- issuing budget call circular containing budget ceilings and guidelines
- receiving and analyzing annual budget submissions
- preparing draft budgets
- finalizing budget

ii) budget implementation and cash management

This process involves:

- preparing expenditure plans
- preparing cash flow forecasts
- release funds to agencies
- receive budget authorization and execute programmes and projects
- process payroll and pensions
- procure goods and services (this will involve sub-processes of requesting goods and services, authorizing expenditure, committing funds, issuing purchase orders, verifying receipt of goods and services, receiving bills/invoices, authorizing payment).
- Monitor cash flows and expected cash requirements (this includes; receiving agency expenditure plans, receiving agency revenue forecasts, preparing overall cash flow forecasts, monitor revenue inflows, monitor maturities of cash and term deposits, receive and process agency request funds etc.).
- Issue and redeem government securities etc.

iii) accounts administration and auditing

This process involves:

- administration of payment and receipt system
- administration of general and budget ledger
- carrying out account reconciliation
- develop costs for programs and projects
- audit government accounts.

SOLUTION THREE

(a) Differences between accounting principles and accounting policies

Accounting Principles

Accounting principles are rules of action adopted by the accountants universally while recording accounting transactions. These are the specific policies and procedures used by an organization to prepare its financial statements. These include any methods, measurement systems and procedures for presenting disclosures. That framework is defined by accounting "principles". For example, "matching" is a principle. According to the matching principle, the costs should be matched with the benefits. Hence, if you purchase an operating asset for ZMW100 million, you should not charge all of that to your cost in the first year itself and should match it with the benefits that the asset will generate over time. Hence, we should depreciate the asset over time.

So, an accounting principle tells us that costs should be matched with benefits. Based on this principle, I can decide that my benefits will flow in a straight line, and hence I charge depreciation in a straight line method. But I could also say that the benefits will be higher in the starting years, which is why I charge depreciation using the written down value method.

Accounting principles can be thought of as a framework in which a company is expected to operate. However, the framework is somewhat flexible, and a company's management team can choose specific accounting policies that are advantageous to the financial reporting of the company. Because accounting principles are lenient at times, the specific policies of a company are very important.

Accounting Policies

Policies are the norms, directions, methods that a business decides for themselves. Policies are not universal, they can differ from one organization to another. Accounting policy for an organization basically defines "their" way of accounting for transactions. Policies are entity's way of adhering to the rules or standard ways of following the rules. For example, I can decide that I am going to charge depreciation on the straight line method. Some other company can decide to charge it using the written down value method. That company has its own 'policy' of charging depreciation, which is different from my 'policy'.

But accounting policies cannot be arbitrary or random. For example, I cannot randomly say that I will charge depreciation based on the card that my parrot picks from the deck of cards! Even though accounting policies can differ from person to person, they still have to fall within an overall framework in order to be acceptable.

Accounting policies are a set of standards that govern how a company prepares its financial statements. These policies are used to deal specifically with complicated accounting practices such as depreciation methods, recognition of goodwill, preparation of research and development (R&D) costs, inventory valuation, and the consolidation of financial accounts. These policies may differ from company to company, but all

accounting policies are required to conform to generally accepted accounting principles (GAAP) and/or international financial reporting standards (IFRS).

(b) Five (5) accounting principles

| Principles | Brief description |
|---|---|
| Accrual | States that revenue and expenses shall be recognized in the accounting period in which they are earned and expensed not when they are received or paid. |
| Matching | States that expenses and associated revenue should be matched and recorded during the period in which they are incurred, regardless of when the transfer of cash occurs. |
| Materiality | The information is said to be material if omitting it or misstating it could influence decisions that users make on the basis of an entity's financial statements. |
| Business entity or separate entity | Business is a separate entity and it is different from the owner or proprietor |
| Substance over form | The financial events and statements of the business should show the overall financial reality of the entity (economic substance over form), rather than the legal form of transactions (form) |
| | |

(c) Five (5) accounting policies

| Policies | Brief description |
|--------------------------|---|
| Comparability | Recognize that a financial report can only be compared with reports for other periods if similarities and differences can be identified |
| Relevance | Financial information is relevant only if it affects the business decisions |
| Reliability | Financial information is reliable only if it can be depended upon to represent actual events and is free from error and bias |
| Understandability | Financial reports must be prepared in a way that is capable of being understood by the users of that report |
| Timeliness | Financial information must be produced on time if they are to affect the decisions |
| | |

(d) **The five (5) accounting concepts**

| Concept | Brief description |
|--------------------------|---|
| Going concern | The assumption that a business will continue to operate fairly for a long time to come. |
| Money measurement | All transactions are recorded in monetary terms. A transaction that cannot be expressed in money terms cannot find place in the books of accounts. |
| Duality | All financial transactions have a two-fold aspect to them which are debits and credits. |
| Consistency | Accounting treatment of transactions of similar nature should be consistent within a particular accounting period as well as between accounting periods. |
| Prudence | Income and expenditure shall only be reported where they are reasonably expected and realizable. This means that expenditure should not be recorded before it is incurred and neither should revenue be recorded before it is earned. |
| | |

SOLUTION FOUR

(a) **Chart of accounts description and its purpose**

A Chart of accounts can be described as systematic listing of organizational accounts in one place. The chart of accounts provides a birds' eye-view of every area of the organization which drives expenses, income, liabilities and assets.

Purpose of a chart of accounts:

- To differentiate between capital from revenue expenditure accounts
- To differentiate expense from income accounts as well as assets from liabilities accounts
- To provide a standard framework for the presentation of public sector financial information and analysis
- To facilitate the preparation and presentation of accounting reports
- Enables constructive comparisons of the performance of public sector bodies
- Serves as means of locating an account in the general ledger if one knows type of chart of accounts adopted

(b) **Explain five risks and mitigation measures related to a computerized accounting system**

- Loss of data due to unauthorized access to information on the system hence need for use of access password to restrict access.
- Loss of data due to system break down (program corruption) where, recovery is not possible. Organisations should have robust disaster recovery mechanisms such as offsite data hosting.
- Exposure to ransom ware attacks particularly, where the accounting system is connected to the internet. This calls for appropriate antivirus protection.
- Since information is hidden in computer files, an audit trail may not be traceable and fraud cannot be easily detected and corrected. Most systems will have computer access and usage logs.
- Invisibility of data could restrict users' ability to correct mistakes on time. Use of data validation and authorization could resolve this risk.

SOLUTION FIVE

(a) Five (5) benefits of implementing TSA to the Government

| Benefits | Explanation |
|--|--|
| It allows complete and timely information on Government cash resources. | The TSA is supported by the IFMIS and has its interfaces with the banking system via the Bank of Zambia through the Real Time Gross Settlement System (RTGS). Access to Real Time balances is available on TSA. |
| It improves appropriation control. | The TSA ensures that the Treasury has full control over budget allocations and strengthens the authority of the budget appropriation. When separate bank accounts are maintained, the result is often a fragmented system, where funds provided for budgetary appropriations are augmented by additional cash resources that become available through various creative often extra budgetary measures. |
| It improves transparency and operational control during budget execution. | When the Treasury has full information about cash resources, it can plan and implement budget execution in an efficient, transparent, and reliable manner. The existence of uncertainty regarding whether the Treasury will have sufficient funds to finance programmed expenditures may lead to sub-optimal behavior by MPAs, such as exaggerating their estimates for cash needs or channeling expenditures through off-budget arrangements (Non-Budget payments). |
| It enables efficient cash management. | TSA ensures regular monitoring of Government cash balances. It also enables higher quality comparison of planned cash needs against the actual. (E.g. identifying causal factors of variances and distinguishing causal factors from random variations in cash balances). |
| It reduces bank transaction costs. | The TSA ensures reduction in the number of bank accounts operated resulting in a decline of administrative cost associated with maintenance of these accounts, such as bank charges and fees. |
| It facilitates efficient payment mechanisms. | TSA ensures that there is no uncertainty regarding the volume or the location of the Government funds and makes it possible to monitor payment mechanisms precisely. |
| It improves reconciliation and quality of fiscal data. | TSA allows for effective reconciliation between the Government's accounting data with the central bank system data. This reduces the risk of errors in reconciliation processes and improves the timeliness and quality of the fiscal accounts. |
| It lowers liquidity reserve needs. | TSA reduces the volatility of cash flows through the Treasury, thus allowing it to maintain a lower cash reserve/buffer to meet unexpected fiscal volatility. |
| Elimination of idle balances | TSA ensures that the idle balances that could have been held in various bank accounts are eliminated. |
| | |

(b) Challenges faced by Government in the implementation of the TSA

| Description of the challenges |
|--|
| Vested interest by Banks |
| Lack of political will |
| Limited trust in government by donors |
| Limited Capacity for implementation |
| Weak internal control environment |
| Change management challenges |
| Stakeholder support and government buy in |
| Inadequate Legislation |
| Implementation cost and infrastructural challenges |
| |

(c) Suggested recommendations to addressing the challenges faced by Government in the implementation of the TSA

| Suggested recommendations to the identified challenges |
|---|
| Engage with Banks |
| Win political will |
| Build trust in government by donors through reducing leakages |
| Build capacity among staff |
| Strengthen internal control environment |
| Undertake change management interventions |
| Secure stakeholder support and government buy in |
| Revise legislation |
| Improve infrastructure |
| |

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 2: LEGAL ASPECTS OF PUBLIC SECTOR FINANCE AND ADMINISTRATION

FRIDAY 16 DECEMBER 2022

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

INSTRUCTIONS TO CANDIDATES

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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

- (a) Explain the importance of a Constitution. (7 marks)
- (b) Discuss the Constitution, Act of Parliament and Delegated legislation as a source of law in Zambia. (11 marks)
- (c) Making reference to Christine Mulundika and seven (7) Others V Attorney General, illustrate the supremacy of the Zambian Constitution. (11 marks)
- (d) Making reference to any authority, distinguish between Constitutional Supremacy and Parliamentary Supremacy. (11 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Attempt any THREE (3) questions.

QUESTION TWO

The Constitution of Zambia establishes three (3) organs of the government; the Legislature, Executive and Judiciary. Each one of them has distinct functions and headed by distinct individuals. This is known as separation of powers.

Required:

- (a) With reference to the above statement, explain the rationale for the doctrine of separation of powers. (14 marks)
- (b) State declaration, mandamus and certiorari as remedies granted under Judicial Review. (6 marks)

[Total: 20 Marks]

QUESTION THREE

- (a) Explain how the Public Procurement Authority is Parliamentary controlled in Zambia. (10 marks)
- (b) Discuss the function of law in a society like Zambia. (10 marks)

[Total: 20 Marks]

QUESTION FOUR

Mandy Kunda was a secretary of the DMD party. The party Chairman dismissed her from the party without following proper procedure. Mandy wants to take legal action against the party and the party secretary via Judicial Review.

Required:

- (a) By citing examples, explain to Mandy on the grounds of Judicial Review. (9 marks)
- (b) Explain to Mandy on whether she will succeed with her suit. (11 marks)

[Total: 20 Marks]

QUESTION FIVE

- (a) Discuss the theory of separation of powers on the organs of Government. (14 marks)
- (b) Explain the difference between a declaration and a mandatory order. (6 marks)

[Total: 20 Marks]

END OF PAPER

PFM 2: LEGAL ASPECTS OF PUBLIC SECTOR FINANCE AND ADMINISTRATION

SUGGESTED SOLUTIONS

SOLUTION ONE

- (a) A constitution is a document in which the fundamental/supreme law of the land is found. The law in the constitution is considered supreme because it is above all other law. According to the constitution of Zambia in article 1(1) any law that is not consistent to the constitution is declared void to the extent of the inconsistency. The constitution is important in because first, it constitutes a state. The existence of a state is determined by a constitution which, through the provisions in the constitution, establishes the structures of the state and confers on them the powers and functions they have and regulates how they exercise those powers and functions as conferred on them. Therefore, the executive, legislature and judiciary are all established under the constitution. The constitution is therefore very important and cannot be compared to any other law.
- (b) (i) The constitution as a source of law – the constitution is said to be a document that contains the fundamental laws of a country. In Zambia the constitution comes from the people and it is considered the first of all the laws of the land. The constitution is said to be the primary source of law in Zambia as, all laws made by other bodies with power to make law, are required to make that law in conformity to the constitution. According to article 1 clause 1 -1(1) of the Zambian constitution, the constitution is the supreme law of the land and any other written law, customary law and customary practices that are inconsistent with the law of the constitution, that other law is void to the extent of its inconsistency to the constitution. The constitution is therefore the number one source of law and its source is the people of Zambia.
- (ii) Acts of Parliament in Zambia are laws made by the country's parliament. The constitution has conferred powers on the country's legislature to make laws. However, when laws are made by parliament, they are required to conform to the provisions of the constitution otherwise they are declared null and void should they not. Acts of Parliament are usually known as administrative laws.
- (iii) Delegated legislation is another source of law in Zambia. Delegated legislation is law made pursuant to Acts of Parliament. When parliament has passed legislation, it further gives power to other institutions to make laws. Delegated legislation is made by local authorities (by-laws) and ministers (statutory instruments) and the law they make is supposed to conform to the laws in the enabling Act (under which it is made).
- (c) *Christine Mulundika and Seven Others v the Attorney General* is a classical case in illustrating the supremacy of the Zambian constitution. The case concerns the applicant and seven others who were arrested and charged under section 7 of the Public Order Act for breaching section 5(4) of the same Act. Section 5(4) of the Act required persons wishing to hold a public rally to obtain a permit from the police. Failure to obtain such permit constituted a criminal offence under section 7 of the Act. A permit was denied to *Christine Mulundika and Seven Others* but decided to hold the

rally anyway. They were arrested and charged under the Act and brought before a magistrate. They however challenged the constitutionality of section 5(4) and 7 of the Act contending they were in violation of articles 20 and 21 of the constitution. The matter was referred to the High Court pursuant to article 28 of the constitution. The Supreme Court ruled in favour of the applicants holding that sections 5(4) and 7 of the Act indeed violated the constitution which guaranteed fundamental rights of freedoms of expression, association and assembly. The case is very important in that it illustrates the supremacy of the constitution over other laws in Zambia. The case therefore gave effect to the contents of article 1(1) of the constitution which declares the supremacy of the constitution over the other laws in Zambia. If any other law be inconsistent to the constitution that other law is to the extent of the inconsistency to be declared void.

- (d) Constitutional supremacy applies to countries that have a codified constitution and the constitution declares its supremacy over the other laws of the land where as Parliamentary supremacy relates to countries like Britain without a codified constitution. Example Zambia practices constitutional supremacy by virtue of article 1(1) of the constitution as also illustrated in *Christine Mulundika and 7 Others* where the court rule provisions of the Public Order Act to be unconstitutional in that it contravened specific articles of the Bill of Rights. Conversely, Parliamentary supremacy relates to countries without a codified constitution where the country's parliament is considered the sovereign body and has the power to make all political decisions and make all laws for the country which laws, as long as they are made by parliament which is properly constituted. *Burma Oil v The Lord Advocate* properly illustrates parliamentary supremacy where the British Parliament passed an Act of Parliament which had the effect of overruling a decision of the House of Lords which Act was passed two years after the decision of the court was passed.

SOLUTION TWO

(a) The separation of powers in a democracy is to prevent abuse of power and to safeguard freedom for all. History has time and again shown that unlimited power in the hands of one person or group in most cases means that others are suppressed or their powers curtailed. The system of separation of powers divides the tasks of the state into three branches: legislative, executive and judicial. These tasks are assigned to different institutions in such a way that each of them can check the others. As a result, no one institution can become so powerful in a democracy as to destroy this system. The separation of powers is an essential element of the Rule of Law, and is enshrined in the Constitution. The separation of powers is also reflected in the fact that certain functions must not be exercised by one and the same person. Thus, the President cannot at the same time be a Member of the National Assembly, or a judge who is appointed Minister or elected to be a Member of the National Assembly must be temporarily suspended from his/her judicial duties.

The Legislative Power

The first of the three powers has the task of passing laws and supervising their implementation. It is exercised by Parliament.

The Executive Power

The executive branch has the task of implementing laws. It comprises the President, Cabinet Ministers law enforcement authorities including the police and the armed forces.

The Judicial Power (Judiciary)

Judges administer justice, viz. they decide disputes independently and impartially. It is their task to ensure that laws are complied with. Judges cannot be deposed and cannot be assigned other positions against their will.

(b)

i. **Certiorari** is a quashing order. It is granted in instances where there is want or excess of jurisdiction, where there is pecuniary bias, denial of the right to be heard and where there is denial of granting the right to legal representation on the part of an administrative institution, an inferior court or tribunal.

ii. **Mandamus** is a mandatory order. It is granted in instances where there is need to compel an administrative institution, inferior court or tribunal to exercise a duty which it neglected to exercise.

iii. **Declaration** is granted in an instance where a person is aggrieved by the decision of an inferior court, tribunal or administrative institution so that the High Court can state the legal positions of the parties.

SOLUTION THREE

(a) The Public Procurement Authority is an entity that is also Parliamentary controlled. The entity is subject to parliamentary control mechanisms by the National Assembly. At the end of every financial year for the authority, a financial report is presented to the Minister of Finance who then tables the same before the National Assembly for debate. Section 13(1) of the first schedule to the 2008 Act requires the authority to present its books of account to the Minister who then tables the same before the national assembly, and further controls are exerted on the authority by the auditor general who conducts annual audits on the authority.

The above notwithstanding, these entities are still subject to the High Court for Judicial Review and other non-judicial controls. Even though judicial review is available, the Courts are reluctant to interfere if redress mechanisms provided under the Acts of Parliamentary have not been followed and a complainant leap frog to the high court without considering the alternative dispute resolution mechanism provided by the Acts of Parliament.

(b) The functions of law can be seen from what law is, that is a tool for social control. Thus, its function is to control society. Law brings about order and peace, and the 2 are importance prerequisites for the realization of man's pursuit for happiness and self-development. Societies without laws, cannot attract investment both locally and from foreign investors. The absence of law for example; to curb crime, corruption and other vices that are detrimental to society would mean a collapse of the social fabric.

An individual citizen is only free to do as helices as long as he does not injure the rights of other citizens and does not disturb the public. The first purpose of law in society, therefore, is for the preservation of life and protection of property. The other purpose is to balance conflicting interests in dispensing justice. The administration of justice becomes possible only through law, because law demands equality for all.

Therefore, law has the following functions:

To do justice

To preserve peace and order

To enforce morality

SOLUTION FOUR

- (a) A person seeking leave for Judicial Review before the court should satisfy the following grounds:

ILLIGALITY

In Lord Diplock's words, this ground means that the decision maker "must understand correctly the law that regulates his decision-making power and must give effect to it". A decision may be illegal for many different reasons. There are no hard and fast rules for their classification, but the most common examples of cases where the courts hold administrative decisions to be unlawful are the following:

The decision is made by the wrong person (unlawful sub-delegation)- If the law empowers a particular authority, e.g. a minister, to make certain decisions, the Minister cannot sub delegate this power to another authority, e.g. an executive officer or a committee. This differs from a routine job not involving much discretion being done by civil servants in the Minister's name, which is not considered delegation.

The decision maker went beyond their power: ultra vires- The classic example of this is **Attorney General v Fulham Corporation (1921)** where Fulham council had the power to set up wash-houses for those without the facilities. They decided to charge people to use it. The court held they went beyond their power by trying to benefit commercially from something that was supposed to be for everyone.

IRRATIONALITY

Under Lord Diplock's classification, a decision is irrational if it is "so outrageous in its defiance of logic or of accepted moral standards that no sensible person who had applied his mind to the question could have arrived at it." This standard is also known as Wednesbury unreasonableness, after the decision in **Associated Provincial Picture Houses Ltd v Wednesbury Corporation**, where it was first imposed.

Unlike illegality and procedural impropriety, the courts under this head look at the merits of the decision, rather than at the procedure by which it was arrived at or the legal basis on which it was founded. The question to ask is whether the decision "makes sense". In many circumstances listed under "illegality", the decision may also be considered irrational.

Proportionality is a requirement that a decision is proportionate to the aim that it seeks to achieve. E.g. an order to forbid a protest march on the grounds of public safety should not be made if there is an alternative way of protecting public safety, e.g. by assigning an alternative route for the march. Proportionality exists as a ground for setting aside administrative decisions in most continental legal systems. However, it is not as yet a separate ground of judicial review, although Lord Diplock has alluded to the possibility of it being recognized as such in the future. At present, lack of proportionality may be used as an argument for a decision being irrational.

PROCEDURE IMPROPRIETY

A decision suffers from procedural impropriety if in the process of its making the procedures prescribed by statute have not been followed or if the "rules of natural justice" have not been adhered to.

Statutory procedures

An Act of Parliament may subject the making of a certain decision to a procedure, such as the holding of a public hearing or inquiry, or a consultation with an external adviser. Some decisions may be subject to approval by a higher body. Courts distinguish between "mandatory" requirements and "directory" requirements. A breach of mandatory procedural requirements will lead to a decision being set aside for procedural impropriety.

Breach of natural justice

The rules of natural justice require that the decision maker approaches the decision making process with "fairness". What is fair in relation to a particular case may differ. As pointed out by Lord Bridge in **Lloyd v McMahon [1987] AC 625**, "the rules of natural justice are not engraved on tablets of stone".

- (b) Judicial review is a type of court proceeding in which a judge reviews the lawfulness of a decision or action made by a public body. In other words, judicial reviews are a challenge to the way in which a decision has been made, rather than the rights and wrongs of the conclusion reached. It is not really concerned with the conclusions of that process and whether those were 'right', as long as the right procedures have been followed. The court will not substitute what it thinks is the 'correct' decision. This may mean that the public body will be able to make the same decision again, so long as it does so in a lawful way.

A political party is not a public body henceforth does not within the ambit of judicial review. Therefore, Mandy shall not succeed.

SOLUTION FIVE

(a) The theory of the Separation of powers in order for it to function well is bound by the following three limbs that operate as Check and balances;

- (i) That there should not be any one individual to be found in more than one institution of the Government,
- (ii) That there should not be any one organ to perform the functions that are reserved for another, and;
- (iii) That there should not be anyone institution to have more power than others but that they should all have co equal power.

On whether or not the theory of checks and balances is as effective in practice, this is done by comparing the operations of the organs of government.

Executive and Judiciary. The National Assembly which is a component of parliament provides the personnel to the executive as ministers appointed by the President to Cabinet who must be Members of Parliament. It is thus immediately clear that the Executive, far from being separated from the Legislature is drawn from within it. This automatically defeats the firm limb which suggests that no individual should be found in more than one institution of the Government.

Legislature and Judiciary. The mere perception that Parliament is sovereign and that the Judiciary is Subordinate to Parliament, is paradoxical to the assertion that the Judiciary is independent. Because of this supremacy Parliament has had interfered in the exercise of duty by Judiciary. Judges have at times been criticized in Parliament. For example, in 1977 motions were tabled for the dismissal of judges who had reduced a sentence for rape. Further a judge who describes a rape victim of contributory negligence was controlled in terms of what they may, or may not say though the powers of the speaker of the House of Commons in the United Kingdom.

The Executive and the Judiciary. Between the Executive and the Judiciary, there are several matters with implications for the Separation of powers. For example, the attitude of the Courts in matters entailing the exercise of prerogative powers; Parliamentary privilege; Judicial Review; and the role of Judges in non- judicial functions. All these arrears indicate interference by one institution onto the other.

It can therefore be said that in Zambia, the concept of Separation of powers is merely on paper and not in practice because the limbs that provide for checks and balance are not strictly adhered to.

(b) Mandatory Order is an order of the court against a statutory body compelling the court to act as required by the statute. This is a type of an order that compels someone or something to be done. It is granted in instances where there is need to compel an administrative institution, inferior court or tribunal to exercise a duty which it neglected to exercise. For example, a local authority may be compelled to do what it out to do.

While

A **d**eclaration is granted in an instance where a person is aggrieved by the decision of an inferior court, tribunal or administrative institution so that the High Court can state the legal positions of the parties. Thus, by a declaration, the court recognizes a right that is claimed by a party against a public body. Hence, it is aimed at declaring the rights of the parties so that once they know their rights, they can claim clearly knowing their rights.

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 3: GOVERNANCE AND MANAGEMENT IN PUBLIC SECTOR

TUESDAY 13 DECEMBER 2022

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.
2. This paper is divided into TWO sections:
Section A: One (1) Compulsory question.
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.

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

"AUDITOR GENERAL REVEALS WASTEFUL EXPENDITURE" - OCTOBER 1, 2021

WASTEFUL expenditure was the largest irregularity revealed in the Auditor General's report, with a rise from K3.7 million in 2019 to K1.4 billion in 2020 representing an increase of 378 percent.

According to the Auditor General account of the republic for the financial year ended December 31, 2020, the second largest irregularity was failure to follow procurement procedures in amounts totaling to K234 million in 2020 from K504,500 in 2019 representing 465 percent increment. Speaking at a press briefing, Auditor General Dick Sichembe explained that the irregularities involve the Ministry of Finance, and the Food Reserve Agency. Other Ministries cited were Housing and Infrastructure, Transport and Communication, General Education and Fisheries and Livestock among others.

Dr. Sichembe also disclosed that other irregularities that have seen an upward trend include un-vouched expenditure, unaccounted for revenue, irregular payments, failure to recover loans and unaccounted for funds among others. He said his office through its forensic and investigation unit will actively follow the matter to understand the motive behind such expenditure.

Meanwhile, the Auditor General's report on parastatal bodies and other statutory institutions for the financial year ended December 31, 2019 has revealed poor financial performance such as failure to collect funds in amounts totaling K16. 6 billion followed by failure to remit and settle statutory obligations of K1 billion during the period under review. Dr. Sichembe also disclosed that entities such as National Pensions Scheme Authority, Energy Regulation Board, Zambia Postal Services and Local Authority Superannuation Fund failed to collect and remit employees' contributions from several employers amounting to K3.5 billion and rentals.

Source: *AUDITOR GENERAL REVEALS WASTEFUL EXPENDITURE – Daily Nation (dailynationzambia.com)*

Required:

- (a) Outline five (5) descriptions and four (4) importance of Internal Audit. (9 marks)

- (b) In the scenario cited above, the second largest irregularity is failure to follow procurement procedures. Discuss five (5) benefits of automating procurement procedures. (10 marks)

- (c) Discuss any five (5) benefits of good contract management in Government. (10 marks)

- (d) Discuss, with examples, three (3) practices and behaviors undermining ethics, accountability, transparency, integrity and professionalism in most public institutions. (9 marks)

- (e) Define corporate ethics. (2 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Answer Any Three (3) Questions in this section.

QUESTION TWO

Your boss has come to learn that you are studying to be a Chartered Accountant and is impressed about your ambitions. He has called you to his office and has asked you to be among the people travelling to Livingstone to formulate the new Strategic plan for the organization. Your boss has therefore asked you to draft a preview about the importance of planning.

Required:

- (a) State three (3) reasons why managers may neglect planning. (6 marks)
- (b) Explain the focus of the following strategic levels
 - (i) Corporate strategy (2 marks)
 - (ii) Business Strategy (2 marks)
 - (iii) Functional Strategy (2 marks)
 - (iv) Operational Strategy (2 marks)
- (c) Distinguish between Strategic Planning and Strategic Management. (4 marks)
- (d) What is Management by Objectives (MBOs)? State its elements. (2 marks)

[Total: 20 Marks]

QUESTION THREE

- (a) Describe the four (4) characteristics of an organization. (8 marks)
- (b) Explain the following organizational structures:
 - (i) Functional Structure (3 marks)
 - (ii) Divisional structure (3 marks)
 - (iii) Hybrid structure (3 marks)
 - (iv) Matrix structure (3 marks)

[Total: 20 Marks]

QUESTION FOUR

Public policies are not formulated in a vacuum but are influenced by certain factors.

Required:

- (a) Explain the six (6) factors that influence the formulation of public policies.
(12 marks)
- (b) Outline four (4) roles carried out by a contract manager in contract management.
(8 marks)

[Total: 20 Marks]

QUESTION FIVE

Public administrators have a critical role to play in managing conflicts in public institutions in their pursuit to achieve overall Government goals.

Required:

Discuss five (5) methods a public administrator may apply to manage institutional conflicts.

[Total: 20 Marks]

END OF PAPER

PFM 3 GOVERNANCE AND MANAGEMENT IN THE PUBLIC SECTOR

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) Outline five (5) descriptions and four (4) importance of Internal Audit.

Internal Audit

- i. -Internal audit is a key pillar of good governance.
- ii. -It provides the board of directors, the audit committee, the chief executive officer, senior executives and stakeholders with an independent view on whether the organisation has an appropriate risk and control environment, whilst also acting as a catalyst for a strong risk and compliance culture within an organisation.
- iii. -Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations.
- iv. -It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.
- v. -Internal audit work is risk-based and encompasses both financial and non-financial operations of the organisation.

Its Importance

-Internal audit is a key component in the assurance structure of an organisation.

-Internal Audit is a cornerstone of good corporate governance in organisations and can play an important role to improve management and accountability, both financial and non-financial.

-Internal audit can be a pivotal activity to provide assurance to the board of directors, the audit committee, and the chief executive officer, and stakeholders that the organisation is governed effectively.

-Organisations establish an independent internal audit function to provide continuous review of the effectiveness of risk management, control, and governance processes.

Internal audit does this by:

- Providing independent, unbiased assessment of the operations of the organisation.

- Providing management with information on the effectiveness of risk management, control and governance processes.
- Acting as a catalyst for improvement in risk management, control and governance processes.
- Being an adviser that tells management what it needs to know, when it needs to know it.
- Reviewing achievement of organisation objectives.
- Assessing if decisions are properly authorised.
- Assessing reliability and integrity of information.
- Reviewing assets are safeguarded.
- Assessing compliance with laws, regulations, policies and contracts.
- Assessing efficiency, effectiveness and economy of business activities.
- Reviewing opportunity for fraud and corruption.
- Following-up previous audits to assess if remedial action has been effectively implemented.
- Looking for better ways of doing things.

(b) **The case scenario cited the second largest irregularity as being failure to follow procurement procedures. Discuss FIVE (5) benefits of automating procurement procedures.**

Benefits:

- ***Lower/reduced costs***

E-procurement removes re-work, errors and paperwork. All these factors result in a lower cost of operating a business or organization. Furthermore, electronic procurement results in better supplier relationships. It uses system developments to lessen external spend, whilst enhancing supplier quantity and performance.

- ***-Better visibility***

With E-procurement, all transactions are centralized and this provides a better view of how finances are used within the organization. It enables in depth reporting on items purchased, payments made, requisitions and orders processes. This great visibility also extends to making certain that the organization complies with established and existing contracts.

- **-Better control**

E-procurement leads to better control of the organization as the decisions are easily made. This is made possible by the central organization of data and presence of time stamps. Additionally, standardized process of approval and a formal workflow ensures that the same degree of control is applied onto every transaction. Compliance to regulations is also improved with E-procurement.

- **-Eliminating Paperwork**

With e-procurement, everything can be saved and stored electronically. This not only saves you from needing more room, it also makes the process of finding older tenders simpler.

- **-Increased Transaction Speed**

E-procurement is both time-saving and efficient. As the electronic handling of tasks supports and simplifies the purchasing process, transaction speed is increased. Also, because of e-enabled relationships with suppliers, procurement cycle times speed up. The e-procurement process eliminates unnecessary activities, allowing you to focus on more valuable tasks.

- **-Reduced Errors**

Electronic paperwork is streamlined and thus easier to check for errors—there's no messy printing to get in the way either. Along with this, past orders are more easily referenced, meaning there's a greater chance that your company can compare orders to ensure new ones are correct.

- **-Avoid invoice delays and duplicate payments**

One of the more complex validations is matching an invoice and the related documents in the procure-to-pay lifecycle. The pricing and terms on an invoice should match those mentioned in the purchase order and the goods receipt note.

Additionally, the line-item quantities, product descriptions and per-unit pricing on the invoice must match those of the purchase order and the actual goods received. Although three-way matching can be performed manually, the cost, accuracy, and time required for the validations can be significantly reduced through automation.

- **-Eliminate dark purchasing**

Dark purchasing reigns when organizations use outdated or disparate tools to manage procurement. When procurement is handled manually, stakeholders have no idea of who is requesting what and why. This leads to expenses incurring outside of

established practices like redundant or unnecessary purchases, submissions to unapproved vendors, and more.

- ***-Remove approval bottlenecks***

A procurement system that depends on too many manual intervention and spreadsheets and emails is subject to human errors and associated risks. In a people-based system, people tend to do things their own way even if it means bypassing policies to cut down purchase cycles.

An effective e-procurement tool, on the other hand, will address such purchase risks with enforced accountability and role-based accessibility, protecting sensitive information and restricting confidential information to relevant stakeholders while keeping the procurement cycle moving forward.

Additionally, an e-procurement solution will reduce the workload of the procurement and finance team by automating administrative tasks such as field-level arithmetic calculations, approval routing, and deadline adherence.

(c) Discuss any Five (5) benefits of good contract management in government.

Benefits

- Good practice contract management has the capacity to increase revenue opportunities, decrease costs and enhance service delivery.
- Contracts that are managed well give rise to future contracts being awarded and can create more revenue opportunities.
- Costs on poorly managed contracts is high due to overruns and time lost. Managing a contract well can drastically reduce such costs.
- Ensures that contractual obligations by both the sourcing supplier and client are met.
- Helps eliminate potential breach of contract situations.
- Improves adherence to outsourcing contract objectives.
- Provides a well-documented audit trail.
- Ensures more favourable contract outcomes.
- Improves quality of service and customer focus.
- Achieves value for money and financial control.
- Decreases the level of risk.
- Clarifies the roles and responsibilities of the contract manager, contractors, and end-users.

- Provides early identification and resolution of poor performance, other problems or disputes.
- Provides evaluation of the specification against contract performance and identification of contract changes or variations.

(d) Discuss, with examples, Three (3) practices and behaviours undermining ethics, accountability, transparency, integrity and professionalism in most public institutions.

The three practices and behaviours

-Corruption

Corruption promotes unprofessional behaviour and therefore erodes accountability, transparency and integrity among staff and organisation leaders. For example, receiving bribes for awarding contracts to suppliers.

-Conflict of Interest

Conflict of interest is a situation in which an individual has competing interests or loyalties. A conflict of Interest can exist in many different situations with a public official whose personal interests conflict with his/her professional position. It results in unethical practice, dishonesty and unprofessionalism. For example, Self-Dealing: which refers to an officer entering into a transaction/contract with another organization that benefits the officer, but to the detriment of the institution.

-Human resource management malpractices

This may include using one's position to influence decisions regarding recruitment. For example, awarding jobs to family members without respect of the due process.

(e) Define corporate ethics

This is a form of applied ethics or professional ethics that examines ethical principles and moral or ethical problems that can arise in a business environment

SOLUTION TWO

Your boss has come to learn that you are studying to be a Chartered Accountant and is impressed about your ambitions. He has called you to his office and has asked you to be among the people travelling to Livingstone to formulate the new Strategic plan for the organisation. Your boss has therefore asked you to draft a preview about the importance of planning.

Required:

(a) State three (3) reasons why managers may neglect planning.

- i. They are uncomfortable thinking about the future, they prefer thinking about routine chores.
- ii. They are impatient and tend to act before thinking, i.e. they focus on getting the job done.
- iii. They feel others should do the planning, i.e. they feel planning is top management task.
- iv. They falsely feel superior in what they are already doing, i.e. they believe rather wrongly that they are experts in what they are doing and do not need planning.
- v. Planning is time consuming and managers do not have the time to waste.

(b) Distinguish between the following:

(v) Corporate strategy

This answers the question, 'What business should we be in?' it gives scope and direction for the business.

(vi) Business Strategy

This answers the question, "How are we going to compete in this particular business?" It is used to manage the different investments (potfolio) the company has ventured in. It uses the Marketing Mix to give the Product, Pricing, Distribution and Promotion strategy.

(vii) Functional Strategy

This answers the question, "How can we best apply the functional expertise to serve the needs of the business unit in the organisation? Different departments of the organisation fulfill the organizational objectives by efficiently and effectively discharging their functional tasks.

(viii) Operational Strategy

This answers the question, 'How should we operate to meet the daily targets. They ensure that everyday activities are running smoothly and that employees are available to do their job.

(c) Distinguish between Strategic Planning and Strategic Management.

- i. **Strategic planning:** A strategy is a comprehensive plan action that sets critical direction for an organization and guides the allocation of its resources.

Strategic planning is the process of formulating and implementing strategic plans. It involves identifying the major objectives of an organization, choosing the strategies needed to achieve them, creating plans to implement the strategies, and doing the required work. Although strategic planning for the organization as a whole is largely a top management responsibility, manager at all levels must participate in its formulation and support the process.

- ii. **Strategic management.**

The process of leading strategic planning effort and ensuring that strategies are well implemented is strategic management. Strategic management includes responsibilities for both strategy "formulation "and strategy "implementation.

(d) What is Management by Objectives (MBOs)? State its elements.

This is management style of setting mutually agreed upon goals and using those goals to evaluate employees. Elements include:

- Goal specificity
- Participative decision making
- An explicit time period
- Performance feedback

SOLUTION THREE

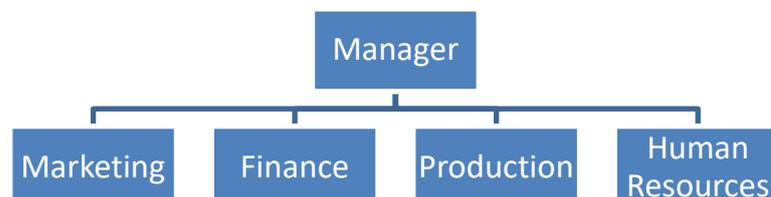
(a) Describe the four (4) characteristics of an organisation.

- i. **Organizations are collection of people:** They combine the efforts of many people to accomplish more than they are otherwise capable of doing. This is called *synergy*, the creation of a whole that is greater than the sum of its individual parts.
- ii. **Organizations involve a division of labour:** work in an organization is divided up and allocated specific tasks to be performed by individuals and groups. This division of labour allows people to develop the skills and expertise needed to perform the tasks with high level of accomplishment.
- iii. **An organisation involves people working together.** People have specialized activities they perform Coordination ensures that people work together so that their many efforts contribute to the higher level accomplishment.
- iv. **An organization involves a common purpose:** all work in an organization should share a common direction, or organizational purpose. This sense of "mission" should be clear to all members and relevant outsiders, and it should define a role for the organization as a viable component in society.

(b) Explain the following organizational structures:

- i. Functional Structure

In functional structure, people with similar skills and performing closely related activities are placed together in formal groups.



- ii. Divisional structure

This structure groups people with diverse skills and tasks but who work on the same product, with similar customers/clients; in the same geographic

region, or on the same time schedule. Divisional structures can take the form of:

- Product structure
- Geographic structure
- Customer structure
- Time structure.

iii. Hybrid structure

Divisional and Functional structure can be used in the different parts of the same organisation and thereby allow different needs to be served.

iv. Matrix structure

This approach uses permanent cross-functional teams to blend the technical strengths of functional structures with the integrating potential of divisional structures. It results in many members belonging to two different formal groups at the same time-one of functional group and the other is product or project group.

SOLUTION FOUR

(a) **The factors that influence public policy formulation are:**

- (i) **Public opinion:** The public, who are citizens, express their views on certain social and economic matters that are negatively affecting people or a specific group of people. The public may give suggestions on how that matter may be resolved through formulation of certain policies that will favour the people. For instance people may give an opinion that certain nature of businesses must be reserved for Zambian in order to create employment.
- (ii) **Research Findings:** Scientific research may be conducted to establish the causes and solutions to a certain problem facing the nation or the globe. Therefore, the findings and the recommendations could made to the public, government or regional bodies. This information may influence public policy formulation. For example the issue of climate change has compelled nations to be formulating policies that will mitigate the negative effects of climate change.
- (iii) **Economic Conditions:** The economic situation of a country could influence the government to formulate public policies that will stimulate economic development. For example to promote local production the government may formulates economic policies that give local entrepreneurs incentives in terms of tax rebates, imposing an embargo on specific imported goods .
- (iv) **Technological Change:** There is rapid advancement in technology that is impacting positively and negatively on the community and businesses. Advancement in technology has changed the production systems, how consumers use and buy goods/services. Therefore, to ensure that consumers, businesses and the environment are protected government formulate public policies in line with change in technology.
- (v) **Profession Association:** Profession Associations may influence public policy formulation by lobbying the government to make policies that support the activities of their members.

(vi) **Business Association:** The associations act collectively to influence public policy formulation in the best interest of their members and specific industries through associations such as Bankers Association of Zambia, Chamber of Commerce, Zambia Manufactures Association etc.

(b) **Roles of a contract manager in contract management:**

- (i) To ensure that the terms and conditions of the contract are in line with those negotiated with the institution.
- (ii) The goods and services supplied are according to the specifications agreed in the contract.
- (iii) Proper management of the contract documents through out the agreed contract period.
- (iv) To be able to effectively negotiate and communicate before and during the execution of the contract.

SOLUTION FIVE

Methods of resolving conflicts

(i) **Compromise**

This type of method is used where management has adopted a democratic type of leadership. This is an approach where both parties win some and lose some because compromise is based on negotiation of give and take. This means that both parties forfeit some conditions in the interest of reaching an agreement. It may leave one or both parties feel cheated hence it's a temporal method of resolving conflicts.

(ii) **Avoiding**

This is where administrators simply ignores the fact that there is a conflict. This method may be applied where both parties know that there is no clear solution to the conflict or one party needs to settle and strategize for confrontation. This is a lose-lose situation on both parties.

(iii) **Competing**

This is the method used by management when there is a need to make quick decisions. Management uses formal authority to resolve the conflict in their favour. Management will use this approach where they are confident that it will reduce on cost and its in the best interest of the organisation. This is a situation where one party wins and the other loses.

(iv) **Collaborating**

This is the method of resolving conflicts where by both parties cooperatively identify the problem and find a solution. Therefore, both parties find mutually agreeable solutions to a problem. A win-win solution is achieved by both parties.

(v) **Accommodating**

This is a method where one party neglects their concern to satisfy the concern of the other party. This method involves playing down differences while emphasizing commonalities. The method can be applied where issues are more important to the other party and foster corporation. This is a lose-

win situation. However, the losing party may do this with the intension of benefiting in return.

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT EXAMINATIONS

DIPLOMA LEVEL

PFM 4 : PUBLIC SECTOR FINANCIAL MANAGEMENT

FRIDAY 16 DECEMBER 2022

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.
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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 is compulsory and must be attempted.

QUESTION ONE

The Roads and Transport Company, is a Government owned company considering constructing a toll gate in the western province. The western province has experienced rapid growth in trade in the last decade mainly due to increase in exports of agriculture produce.

One of the reasons for constructing the toll gate is to generate revenue for the maintenance of the recently completed 400 Kilometers great – west road which links the western province to a country across the western border. Most of the agricultural produce is exported to the same country across the western border. The exports are transported by trucks via the great-west road. This has negatively affected the quality of the great-west road as a result of wear and tear caused by heavy loads from the trucks.

Sixty percent (60%) of the funds for the construction will be sourced from a government grant received from the Ministry of Finance and forty percent (40%) from equity financing. The cost of the toll gate is estimated at K500 million. The government uses a social opportunity cost of five percent (5%) to appraise projects of this nature.

The great-west road is expected to cost government K0.5 million per kilometer to maintain per annum. This money would have been sourced from the annual government budget support had the toll gate not been constructed. The toll gate is expected to have a lifespan of fifty (50) years.

The cost of constructing the toll gate includes feasibility studies which were undertaken for K10 million. Maintenance costs for the toll gate are estimated at K0.1m per annum. The Roads and Transport Company is expected to recruit six (6) personnel to work at the toll gate as revenue collectors. Each of them would be paid a monthly salary of K4,500.

There has been criticism raised by various stakeholders concerning the cost of constructing the toll gate. The critics allege that the cost of construction is excessively high.

However private consultants engaged by the company to appraise the proposed toll gate argue that the toll gate, once completed, will recoup the initial investment within four (4) years. This period is one (1) year earlier than the government target of five (5) years required for projects of this nature. They estimate that the gate is expected to generate revenue of K0.12m per day.

The consultants further explained that a capital expenditure decision of this nature is not only based on financial factors but also non-financial factors.

Assume 360 days in a year.

Required:

- (a) Calculate the payback period of the proposed toll gate using:
 - (i) The Traditional method. (8 marks)
 - (ii) The Discounted payback method. (5 marks)

- (b) Based on your calculations in part (a) recommend with reasons whether or not the Roads and Transport Company should proceed with the proposed investment. (2 marks)

- (c) Explain any five (5) non-financial factors which should be considered by the Road and Transport Company in deciding whether or not to invest in capital projects of this nature. (15 marks)

- (d) Explain any five (5) benefits to the Roads and Transport Company of using equity capital to finance capital expenditure projects of this nature. (10 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Attempt any THREE (3) questions.

QUESTION TWO

Country X realized the importance of investment in the railway line by upgrading and modernizing it. The reason for this realization being that the road transportation became expensive because of frequent repairs caused by wear and tear of the roads. The wear and tear has been attributed to high traffic and the use of heavy trucks on the roads. This has resulted into delays in the transportation of goods both inland and for export. It was also further noted from research findings carried out by independent consultants that the tarmacs that were constructed were not up to the specified specifications by the engineers and this resulted into shoddy works.

International consultants were engaged to carry out a feasibility study on the construction of the rail-lines. The conclusion of the study culminated into the signing of a memorandum of understanding for the construction of the railway net -work of country X. The total cost of this capital investment was US\$10,000,000 (Ten Million United States Dollars). Country X obtained funds from the international markets by issuing a 10-year Euro-Bond of the Equivalent amount at an interest rate of 4.5% payable half yearly (Interest component) and the balloon payment on maturity (i.e. after 10 years).

The terms of the loan agreement were that the borrowed funds were specifically for the construction of the rail lines, the purchase of modernized wagons, replacement of the fully depreciated lines, and the revitalization (of capital expenditure nature) of old storage facilities to that of modern storage facilities at every strategic area in the country for the goods that will be transported through the line. It was further argued that once the rail network of country X is revitalized, it will result into improved trade; both local and international. The country's balance of payments which was currently in deficit was going to be positive.

However, the Government of country X decided to apportion 5% (US\$500,000) of the amount to meet some recurrent expenses unrelated to what was agreed and signed for in the memorandum of understanding between country X and the Lenders. The Government argued that they were going to create a 'sinking fund' to accumulate funds required to meet the interest payments and eventually the balloon payment so they were at liberty to 'divert' the US\$500,000 to recurrent expenses as it will eventually be repaid.

Other independent financial analysts and experts argued against the decision by the Government of Country X in diverting the borrowed funds for investment to revenue expenditure which was not part of the conditions of the loan agreement. They argued that it was not good management of sovereign debt as such decisions will culminate into default. They further argued that in the event of default, it is such decisions that will make it difficult to structure the debt.

Required:

- (a) Identify and discuss the differences between revenue expenditure and capital expenditure in relation to both private and public institutions. (7 marks)
- (b) Explain the reasons why Governments borrow money. (5 marks)
- (c) Identify and explain the various types of Government securities which constitute the Public Domestic Debt of a country like Zambia. (8 marks)

[Total: 20 Marks]

QUESTION THREE

Risk Management is particularly important for most governments because in the recent past most governments have embarked on redesigning their business processes. The government of country Z recently launched a risk management framework and has since embarked on an exercise of rolling out the framework to all ministries. All ministries are now required to prepare risk registers for their ministry and indeed any other National Development Plan.

Required:

- (a) Define risk appetite and outline how the risk appetite can be set up in a Government. (12 marks)
- (b) Explain the advantages and disadvantages of government embarking on roll out of risk management. (8 marks)

[Total: 20 Marks]

QUESTION FOUR

An extract of the 2022 national budget is provided in the table below:

| | KM | Share of Budget |
|---|------------|------------------------|
| Total domestic revenue, grants and financing | 172,987.00 | 100% |
| Total domestic revenue and domestic financing | 123,318.00 | 71% |
| Domestic revenue | 98,859.10 | 57% |
| Total foreign financing and grants | 49,668.90 | 29% |
| Domestic Financing | 24,458.90 | 14% |
| | | |
| Total foreign financing and grants: | 49,668.90 | |
| Programme loans | 39,347.30 | |
| Project loans | 8,499.60 | |
| Foreign grants | 1,821.90 | |

Required:

- (a) Describe the concept of a budget surplus and explain at least one reason for the Government to run such a budget. (4 marks)
- (b) Explain with examples the nature of domestic revenue as provided in the 2022 national budget. (8 marks)
- (c) List and explain the general stages of the budget cycle in Zambia. (8 marks)

[Total: 20 Marks]

QUESTION FIVE

In the Public Sector, performance is critical in order for goods and services to be provided to the communities. The councils should perform as per expectation in order for clean water to be provided in their communities. They also have to ensure that garbage is collected and disposed-off appropriately in order to maintain a clean environment.

It is therefore critical that institutions, both Public and Private have a scientific and measurable means of assessing performance at all levels. This will ensure that the goods and services are provided with quality, promptly and at the right price. Deviations should immediately be identified and where these deviations are negative, corrective action should be taken, where the deviations are positive, rewards and motivation should be encouraged.

Required:

- (a) Explain what is meant by Performance Management. (6 marks)
- (b) Identify the five (5) elements that suggest how an organization can implement the performance management cycle (10 marks)
- (c) Explain the four (4) types of indicators of performance management (4 marks)

[Total: 20 Marks]

END OF PAPER

Formulae

Modigliani and Miller Proposition 2 (with tax)

$$k_e = k_e^i + (1 - T)(k_e^i - k_d) \frac{V_d}{V_e}$$

Two asset portfolio

$$s_p = \sqrt{w_a^2 s_a^2 + w_b^2 s_b^2 + 2w_a w_b r_{ab} s_a s_b}$$

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

$$g = br_e$$

The weighted average cost of capital

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

The Fisher formula

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

Purchasing power parity and interest rate parity

$$S_1 = S_0 \times \frac{(1 + h_c)}{(1 + h_b)} \quad F_0 = S_0 \times \frac{(1 + i_c)}{(1 + i_b)}$$

Modified Internal Rate of Return

$$MIRR = \left[\frac{PV_R}{PV_I} \right]^{\frac{1}{n}} (1 + r_e) - 1$$

The Black-Scholes option pricing model

$$c = P_a N(d_1) - P_e N(d_2) e^{-rt}$$

Where:

$$d_1 = \frac{\ln(P_a / P_e) + (r + 0.5s^2)t}{s\sqrt{t}}$$

$$d_2 = d_1 - s\sqrt{t}$$

The Put Call Parity relationship

$$p = c - P_a + P_e e^{-rt}$$

Present Value Table

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

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

| <i>Periods</i> (n) | <i>Discount rate (r)</i> | | | | | | | | | | |
|-----------------------|--------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|----|
| | 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 | 0.941 | 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 | 0.305 | 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 |

Standard normal distribution table

| | 0-00 | 0-01 | 0-02 | 0-03 | 0-04 | 0-05 | 0-06 | 0-07 | 0-08 | 0-09 |
|-----|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| 0-0 | 0-0000 | 0-0040 | 0-0080 | 0-0120 | 0-0160 | 0-0199 | 0-0239 | 0-0279 | 0-0319 | 0-0359 |
| 0-1 | 0-0398 | 0-0438 | 0-0478 | 0-0517 | 0-0557 | 0-0596 | 0-0636 | 0-0675 | 0-0714 | 0-0753 |
| 0-2 | 0-0793 | 0-0832 | 0-0871 | 0-0910 | 0-0948 | 0-0987 | 0-1026 | 0-1064 | 0-1103 | 0-1141 |
| 0-3 | 0-1179 | 0-1217 | 0-1255 | 0-1293 | 0-1331 | 0-1368 | 0-1406 | 0-1443 | 0-1480 | 0-1517 |
| 0-4 | 0-1554 | 0-1591 | 0-1628 | 0-1664 | 0-1700 | 0-1736 | 0-1772 | 0-1808 | 0-1844 | 0-1879 |
| 0-5 | 0-1915 | 0-1950 | 0-1985 | 0-2019 | 0-2054 | 0-2088 | 0-2123 | 0-2157 | 0-2190 | 0-2224 |
| 0-6 | 0-2257 | 0-2291 | 0-2324 | 0-2357 | 0-2389 | 0-2422 | 0-2454 | 0-2486 | 0-2517 | 0-2549 |
| 0-7 | 0-2580 | 0-2611 | 0-2642 | 0-2673 | 0-2704 | 0-2734 | 0-2764 | 0-2794 | 0-2823 | 0-2852 |
| 0-8 | 0-2881 | 0-2910 | 0-2939 | 0-2967 | 0-2995 | 0-3023 | 0-3051 | 0-3078 | 0-3106 | 0-3133 |
| 0-9 | 0-3159 | 0-3186 | 0-3212 | 0-3238 | 0-3264 | 0-3289 | 0-3315 | 0-3340 | 0-3365 | 0-3389 |
| 1-0 | 0-3413 | 0-3438 | 0-3461 | 0-3485 | 0-3508 | 0-3531 | 0-3554 | 0-3577 | 0-3599 | 0-3621 |
| 1-1 | 0-3643 | 0-3665 | 0-3686 | 0-3708 | 0-3729 | 0-3749 | 0-3770 | 0-3790 | 0-3810 | 0-3830 |
| 1-2 | 0-3849 | 0-3869 | 0-3888 | 0-3907 | 0-3925 | 0-3944 | 0-3962 | 0-3980 | 0-3997 | 0-4015 |
| 1-3 | 0-4032 | 0-4049 | 0-4066 | 0-4082 | 0-4099 | 0-4115 | 0-4131 | 0-4147 | 0-4162 | 0-4177 |
| 1-4 | 0-4192 | 0-4207 | 0-4222 | 0-4236 | 0-4251 | 0-4265 | 0-4279 | 0-4292 | 0-4306 | 0-4319 |
| 1-5 | 0-4332 | 0-4345 | 0-4357 | 0-4370 | 0-4382 | 0-4394 | 0-4406 | 0-4418 | 0-4429 | 0-4441 |
| 1-6 | 0-4452 | 0-4463 | 0-4474 | 0-4484 | 0-4495 | 0-4505 | 0-4515 | 0-4525 | 0-4535 | 0-4545 |
| 1-7 | 0-4554 | 0-4564 | 0-4573 | 0-4582 | 0-4591 | 0-4599 | 0-4608 | 0-4616 | 0-4625 | 0-4633 |
| 1-8 | 0-4641 | 0-4649 | 0-4656 | 0-4664 | 0-4671 | 0-4678 | 0-4686 | 0-4693 | 0-4699 | 0-4706 |
| 1-9 | 0-4713 | 0-4719 | 0-4726 | 0-4732 | 0-4738 | 0-4744 | 0-4750 | 0-4756 | 0-4761 | 0-4767 |
| 2-0 | 0-4772 | 0-4778 | 0-4783 | 0-4788 | 0-4793 | 0-4798 | 0-4803 | 0-4808 | 0-4812 | 0-4817 |
| 2-1 | 0-4821 | 0-4826 | 0-4830 | 0-4834 | 0-4838 | 0-4842 | 0-4846 | 0-4850 | 0-4854 | 0-4857 |
| 2-2 | 0-4861 | 0-4864 | 0-4868 | 0-4871 | 0-4875 | 0-4878 | 0-4881 | 0-4884 | 0-4887 | 0-4890 |
| 2-3 | 0-4893 | 0-4896 | 0-4898 | 0-4901 | 0-4904 | 0-4906 | 0-4909 | 0-4911 | 0-4913 | 0-4916 |
| 2-4 | 0-4918 | 0-4920 | 0-4922 | 0-4925 | 0-4927 | 0-4929 | 0-4931 | 0-4932 | 0-4934 | 0-4936 |
| 2-5 | 0-4938 | 0-4940 | 0-4941 | 0-4943 | 0-4945 | 0-4946 | 0-4948 | 0-4949 | 0-4951 | 0-4952 |
| 2-6 | 0-4953 | 0-4955 | 0-4956 | 0-4957 | 0-4959 | 0-4960 | 0-4961 | 0-4962 | 0-4963 | 0-4964 |
| 2-7 | 0-4965 | 0-4966 | 0-4967 | 0-4968 | 0-4969 | 0-4970 | 0-4971 | 0-4972 | 0-4973 | 0-4974 |
| 2-8 | 0-4974 | 0-4975 | 0-4976 | 0-4977 | 0-4977 | 0-4978 | 0-4979 | 0-4979 | 0-4980 | 0-4981 |
| 2-9 | 0-4981 | 0-4982 | 0-4982 | 0-4983 | 0-4984 | 0-4984 | 0-4985 | 0-4985 | 0-4986 | 0-4986 |
| 3-0 | 0-4987 | 0-4987 | 0-4987 | 0-4988 | 0-4988 | 0-4989 | 0-4989 | 0-4989 | 0-4990 | 0-4990 |

This table can be used to calculate $N(d)$, the cumulative normal distribution functions needed for the Black-Scholes model of option pricing. If $d_i > 0$, add 0.5 to the relevant number above. If $d_i < 0$, subtract the relevant number above from 0.5.

PFM 4 PUBLIC SECTOR FINANCIAL MANAGEMENT

SUGGESTED SOLUTIONS

SOLUTION ONE

(a)

| | |
|---------------------------------|--------------|
| Traditional Payback | KM |
| Revenue | |
| Toll fees K0.12*360 | 43.2 |
| Saving on maintenance k0.5m*400 | 200 |
| Total | 243.2 |

Annual costs

| | |
|--------------------------------|----------------|
| Salary 4500*6*12 | 0.324 |
| Maintenance cost for toll gate | 0.1 |
| Total | 0.424 |
| Net Cash flows | 242.776 |

Payback Period

Initial Investment / Net annual cash flow

500/242.776

2.059512

Payback period = 2.1 Years

Total

Discounted Payback

| Year | | cash flow | DF 5% | PV | |
|------|----------|-----------|-------|---------|---------|
| 0 | Invest | -500 | 1 | -500 | |
| 1 | Net cash | 242.776 | 0.952 | 231.123 | -268.88 |
| 2 | Net cash | 242.776 | 0.907 | 220.198 | -48.679 |
| 3 | Net cash | 242.776 | 0.863 | 209.516 | |
| 4 | Net cash | 242.776 | 0.823 | 199.805 | |

Payback period = $2 + 48.679 / 209.516$
2.232years

(b) The Roads and Transport Company should proceed with the construction as the payback period is below the target of four years.

(c)

(1) Availability and skills of the personnel.

When a company is considering investing in a capital project, it should consider the available personnel. The company should consider whether they have enough personnel to implement the project once construction is completed. They should consider whether they have the required technical knowledge to operate the automated machinery for revenue collection.

(2) Government Regulation.

The RTC should consider the relevant laws and requirements for setting up such a project. It should seek clearance from various regulatory authorities such as the environmental agency and any other licenses required to operate such a project.

(3) Social Trends.

How the views of society will change overtime is a key qualitative consideration. Will consumers prefer an automated toll gate in future? What is the service delivery rate for the toll gate?

(4) Political Factors.

Political decisions affect how the project is implemented. The toll fees should not be excessively high as this could create political criticism from the opposition parties. Political reactions of constructing the toll gate from various political and social groups should be considered. The use of equity financing could be questioned by some critics. Since the project is of a public nature, some political layers would prefer the use of budget support only to avoid the private sector getting involved.

(5) Qualitative Factors.

The toll gate should be constructed from good quality materials. This will guarantee a long lifespan of the project. Its estimated life span of 50 years should be compared with other similar toll gates.

(d)

Benefits of equity financing

(1) Dividends.

Dividends payable on shares to the ordinary shareholders are not a legal obligation of the company. Non- payment of dividend in a particular year may not be challenged in court by shareholders.

(2) The equity capital is a permanent source of finance to RTC as share capital is generally not repayable to the shareholders.

(3) The issue of equity does not increase the gearing of the company. Gearing is the measure of debt capital as a percentage of equity capital or total capital. The higher the gearing the higher the risk of non-payment of interest on debt.

(4) Dividend payments may sometimes be paid as a percentage of profits. This means in a year in which profits are poor, very little or no dividend is payable. This is in contrast to interest payments which are usually fixed.

(5) In the case of winding up or liquidation of a company the ordinary shareholders are usually the last to be paid after creditors and preference shareholders have been paid.

SOLUTION TWO

(a) Identify and discuss the differences between revenue expenditure and capital expenditure in relation to both private and public institutions.

Revenue expenditures are expenses that immediately recognized and expensed. In accrual accounting, the revenues are recognized immediately as they are earned and the expenses when spent. When the expenses are immediately recorded they are subsequently matched with the revenue on which these expenses were incurred.

As for assets, revenue expenses are those that maintain the asset for regular use.

Capital expenses are those are most for new assets or major improvements on the asset to extend their useful economic life. The company or institution will usually develop a capitalization policy. This will also guide the institution as to which ceiling of expenditure will be regarding as revenue expenditure or which expenditure will be capitalized.

However, the major differences between these two types of expenditure are as follows:

- i. Timing- Capital expenditure are expensed on gradual basis based on the rate of depreciation the company follows. At the end of its useful life the capital expenditure will have been fully depreciated. As the other had the revenue expenditure is expensed as in the current period or thereafter.
- ii. Consumption- As stated in the timing, a capital expenditure is assumed to be consumed over the useful life of an asset, whereas revenue expenditure is assumed to be consumed within a very short period of time.
- iii. Size-Depending on the capitalizations policy, a capital expenditure involved large monetary amounts than revenue expenditure. Nevertheless in some cases, large expenditures may still be expensed upon their incurrence as long as they are directly associated with sale transactions or are period costs.

(b) Explain the reasons why Governments borrow money.

There are various legitimate reasons as to why government borrows. The following are the main reasons:

- i. To finance national government deficits
- ii. In order to mobilize foreign exchange
- iii. In some cases, the government borrows so as to secure financing at more favorable terms than the opportunity cost of revenues
- iv. To take advantage of the benefits that accrue to the funds, e.g. technology
- v. To balance the timing of resources with the project gestation and repayment of benefit

(c) Identify and explain the various types of Government securities, which constitute the Public Domestic Debt of a country (Zambia)

The various types of government securities which constitute the public domestic debt of a country include the following:

- i. Consolidated Bond- This is a consolidation of various debt owed by government to the Central Bank. In most cases, a long-term bond agreement has 10year tenure with a coupon rate of 6% with an option to roll over for another 10 years.
- ii. Government Bonds-These are issued mostly for fiscal and monetary policies objectives. As for now, there are five(5) types on issue largely; 12months, 18months and 24months as short-term, 3-5years as medium term and 15 years as long-term
- iii. Treasury Bills- These are short-term instruments issued by the central bank through the auction system. The offer amounts are determined by the liquidity on the market, the financing requirements of government and maturities needed to be rolled- over. As at now, there are five (5) types of treasury bills on issue; 28days, 91days, 273days and 364days.
- iv. Kwacha Bridging Loan-This is an advance to government against further revenues to meet budgetary allocations. It is short-term borrowing for fiscal year.

SOLUTION THREE

(a) Define risk appetite and outline how the risk appetite can be set up in a government.

Definition of Risk Appetite

- Risk appetite is the level of risk that an organization is willing to accept while pursuing its objectives, and before any action is determined to be necessary in order to reduce the risk.

How Risk Appetite can be Set up in Government :

- Understanding the government's strategic goals and objectives
- Develop risk appetite scale. Some objectives may require government to be creative in order to achieve them while other may require government to be conservative.
- Connect with senior - Once the risk appetite scale has been developed to consistently measure how much risk an organization is willing to take to achieve its strategic goals and objectives, the leadership needs to provide its input
- Utilize common language to develop risk appetite statement. – The cornerstone of an effective risk appetite framework involves the development of a risk appetite statement.
- Develop prioritization tools - develop a set of tools that allow staff to prioritize their tasks in relation to the established risk appetite

(b) Explain the advantages and disadvantages of government embarking on roll out of risk management

Advantages of Roll out of Risk Management

- Risks are identified before implementation of a programme
 - It provided an opportunity for government to assess the risk on a regular basis
 - Treatment of the risk is identified before hand
 - Minimizes the risks to reoccur
- Helps government is coming up with realistic plans of various programs in government

Disadvantages of Rollout of Risk Management

- Complex to come up with calculations
- Certain risks identified depend on external entities
- Certain risks identified may be ambiguous therefore making it difficult for management to be proactive to deal with the risks.

SOLUTION FOUR

(a) Budget surplus.

This is a budget where revenue exceeds expenditure.

A government may run such a budget if they want to slow down expenditure and consequently slow down economic activity. This may be done where inflation is too high and government wants to reduce inflation.

(b) Domestic Revenue.

(1) Domestic Income tax.

This comprises a variety of direct tax sources, the most significant of which are:

- (i) Company Income Tax. – A tax on profit made by Limited Companies.
- (ii) PAYE. – Method of collecting income tax at source from individuals in employment.
- (iii) Withholding Tax. Deducted at source from certain sources of investment income.
- (iv) Mineral Royalty Tax. A tax due as consideration for the extraction of minerals.

(2) Value Added Tax. This is an indirect tax. It is a consumption based tax levied in the supply chain at each point where value is added to a good or service.

(3) Customs and Excise. – on imported goods

(4) Non-Tax Revenue e.g. fees and charges for the use of public services to ensure cost recovery.

(c) Stages of The Budget Cycle.

(1) Budget Formulation.

The executive drafts budget with careful thought at the ground level as to what is needed and what new initiatives can be started and at the same time giving guidance as to what should be accepted. In the public sector once each government spending agency makes its decisions on what it intends to do, their requests are then sent to the Ministry Of Finance for inclusion in or exclusion from the final document.

(2) Budget enactment.

Ministry of finance presents budget to parliament, debates and approvals provided by the members of parliament.

(3) Budget Execution.

Government agencies and departments implement programs and spend the money.

(4) Budgeting auditing and assessment.

The agencies and departments as a requirement report on expenditure to the Auditor General. The auditors ensure that the money is being spent effectively in accordance with the law and intended purpose.

SOLUTION FIVE

(a) Briefly explain what is meant by Performance Management

The performance management entails a continuous process of identifying, measuring and developing the performance of individuals and alignment such performance with the strategic goals of an organisation.

Some authors have defined performance measurement as quantifying, either qualitatively or quantitatively, the output or level of activity of an event or process. Performance management is action, based on performance measures and reporting, which results in improvements in behavior, motivation and processes and promotes innovation.

(b) Identify the 5 (five) elements that suggest how an organization can implement the performance management cycle

It has been noted that there are identifiable 5(five) elements that an organisation can implement. The elements are as follows;

- i. Identifying and setting aims
- ii. Comparing expected performance and measuring actual performance
- iii. Identifying variances and provision of feedback.
- iv. Reward system based on performance outcomes.
- v. Adjustments to objectives and activities where necessary

(c) Explain the 4 (four) types of indicators of performance management

In performance management, there are four identifiable indicators and these are as follows:

- i. Output
- ii. Welfare
- iii. Performance
- iv. Composite indicators that consolidate output, welfare and performance.

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 5 : PUBLIC SECTOR AUDITING

THURSDAY 15 DECEMBER 2022

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

You were recently appointed as an Audit Manager in the Audit Department of the Supreme Audit Institution (SAI). You are responsible for the financial statement audit for the Ministry of Finance and National Planning.

The Finance Director at the Ministry of Finance and National Planning requested that an Audit Senior, be assigned to the audit team. This Audit Senior has not previously been assigned to the audit for the Ministry of Finance and National Planning. On further investigation it transpired that he is the brother to the Chief Accountant at the Ministry of Finance and National Planning.

The Ministry of Finance and National Planning is experiencing staff shortages, and it has been suggested that Supreme Audit Institution (SAI) audit staff be seconded to the Ministry of Finance and National Planning for six (6) months.

The Permanent Secretary invited you to the Ministry's annual ball for its members of staff. The Minister of Finance and National Planning and members of the Public Accounts Committee (PAC) will be in attendance.

The Supreme Audit Institution (SAI) has been approached by the Minister of Finance and National Planning to negotiate loan restructuring with the International Monetary Fund (IMF).

The Ministry of Finance and National Planning is the Government Ministry that is responsible for mobilising the financial resources needed by the government and allocating them to other Ministries, provinces and other spending agencies. The Ministry supervises the Zambia Revenue Authority (ZRA) in ensuring that the authority collects tax revenue that it is expected to collect in a given period of time.

The Ministry of Finance and National Planning has a controlling interest in all publicly owned entities.

During the year, the Ministry of Finance and National Planning arranged a loan amounting to K30 million with Construction Bank for building a new football stadium in Ndola. The bank charged interest at a rate of 12% per annum; the Ministry is allowed to invest any surplus funds at 8% per annum.

The Ministry of Finance and National Planning has an ownership interest in ZamZam Railways, which operates as a Government Business Enterprise (GBE). The rail authority is allowed to

operate autonomously and does not rely on the Government for funding, but has raised capital through significant borrowings that are guaranteed by the government. The Government has power to appoint and remove a majority of the members of the governing body of the rail authority. The government has never exercised the power to remove members of the governing body.

Required:

- (a) Explain the responsibilities of the Auditor-General's Office and the Public Accounts Committee (PAC) in the Republic of Zambia. (4 marks)
- (b) Using the information in the scenario:
- (i) Explain the ethical threats that may affect independence of the auditors in relation to the audit of Ministry of Finance. (4 marks)
- (ii) Describe appropriate safeguards for each ethical issue identified in (b) (i) above. (4 marks)
- (c) Discuss, giving suitable examples, six (6) methods that can be used to gather sufficient appropriate audit evidence in the financial statement audit of the Ministry of Finance and National Planning. (12 marks)
- (d) Define audit risk, giving one (1) relevant example. (2 marks)
- (e) Explain, from the information given, five (5) audit risks. (10 marks)
- (f) Explain four (4) audit procedures to be performed on completeness of related party disclosures in the financial statements. (4 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Attempt any THREE (3) questions.

QUESTION TWO

- (a) Many countries in the world have attained independence through democratic elections. The reason for holding elections is to enable the citizens elect their representatives to represent them in Parliament.

Governments, world over, collect money from the citizens by way of taxes and the public funds are held in trust for the benefit of the citizens. It is common that those who are responsible for the public funds do act in the best interest of the general citizenry. It is for this reason that there is need for those who are responsible for public funds to be transparent and accountable on how they use public funds.

Required:

- (i) Explain the principles of 'transparency' and 'accountability' in the handling of public funds. (4 marks)
- (ii) Explain how the Supreme Audit Institutions (SAI) helps in holding those responsible for public funds accountable. (4 marks)
- (b) You have been seconded to carry out a review of the operations of the Supreme Audit Institution (SAI) of an International Organisation for Supreme Audit Institutions (INTOSAI) member country. The main area of concern in the reviews is that of compliance with the ethical values by the SAI and its staff.

You interviewed staff within the Supreme Audit Institution (SAI) and you reviewed the existing procedure manuals and policies.

The following is a summary of your findings from the interviews and review of procedure manuals:

The majority of the staff does not have any formal qualifications, but have work experience gained through working for Government. It is common for staff of the Supreme Audit Institution (SAI) to be paid daily allowances when out of station by the

entities being audited. This is in addition to the allowances paid in advance by the Supreme Audit Institution (SAI) each time staff travel out of town on duty.

A review of the allowances paid during one quarter of the year revealed fraud by staff assigned to audits. There were instances of staff claiming allowances for more days than those actually spent doing audits. When questioned on how this happened, you were told that allowances are paid in advance in accordance with the plan and where assignments are done in a shorter period no refunds of money is made by staff.

Your efforts to gain access to the code of ethics for the Supreme Audit Institution (SAI) failed and it would appear that there is no code of ethics for staff to follow.

Required:

- (i) Explain four (4) fundamental ethical principles issues in the Supreme Audit Institution (SAI) that have been compromised. (8 marks)

- (ii) Explain the meaning and use of 'professional judgment' and 'professional skepticism'. (4 marks)

[Total: 20 Marks]

QUESTION THREE

The Ministry of Health, last year awarded a K17 million contract for the supply of health centre kits to a company called Honey Beans Pharmacy Limited, which did not legally exist. However, owing to a K11 million drug supply debt, the company stopped supplying in December 2018, demanding that the Government first settles its debt; a move that forced the Ministry of Health to find an alternative supplier.

Ministry of Health officials declined to explain the circumstances under which a company that was not in existence could win a contract worth a staggering sum of K17 million.

You work for the Office of the Auditor General (OAG) and you have been assigned to lead a team of auditors to conduct a forensic audit of the procurement of drugs in the last three (3) years. Quality control in the performance of work is important to the Supreme Audit Institutions (SAI) where guidance is provided by ISSAI 40 Quality Control.

The procurement of drugs is currently undertaken by the Zambia Public Procurement Authority (ZPPA) in conjunction with the Ministry of Health. Your investigations will be directed towards establishing whether tender procedures were followed.

A review of the conditions of service for the staff in the ZPPA shows that they are lowly paid in relation to the value of goods they are deal with. It has come to your attention that the controls over drugs purchased are weak resulting in overstocking. This has led to large quantities of drugs expiring.

Required:

- (a) Using information in the scenario briefly describe four (4) stages in a forensic investigation assignment. (8 marks)

- (b) Evaluate the performance of the procurement process of the Ministry of Health using the principle of value for money and dealing with:
 - (i) Economy (2 marks)
 - (ii) Efficiency (2 marks)
 - (iii) Effectiveness (2 marks)

- (c) Explain three (3) elements of quality control for audits of SAIs in accordance with ISSAI 40 *Quality Control*. (6 marks)

[Total: 20 Marks]

QUESTION FOUR

- (a) The internet is used to improve mankind’s information-seeking behaviors. To a certain extent the internet can be a very reliable source of information. But this statement cannot be applied in general to all websites. The internet can be trusted only to a certain extent and not completely. One of the disadvantages that are associated with the internet connectivity is the higher risk of cyber-crime.

Required:

Define cyber-crime and describe three (3) main threats posed by cyber-crime.

(8 marks)

- (b) You are the Audit Manager for the audit assignment of Kalomo District Council. You are about to undertake the audit of financial statements of the council. You are cognizant of the requirements of ISSAI 1315: performance risk assessment procedures to provide a basis for identifying and assessing risk of material misstatement. These procedures include appropriate analytical procedures.

Part of the audit design is focused on attaining the following objectives:

1. Verifying costs of providing services to the local community have been included in the financial statements.
2. Verifying that the costs incurred in providing the services are sustainable in relation to service charges paid by the local community; and
3. Verifying the management control exercising over the costs of providing the services.

Required:

- (i) Formulate and describe an appropriate analytical procedure to meet each of the audit objectives listed above, clearly explaining further actions that can be taken after undertaking the procedure. (8 marks)
- (ii) Explain the accountability triangle. (4 marks)

[Total: 20 Marks]

QUESTION FIVE

You were recently promoted to the level of Audit Manager at the Supreme Audit Institution (SAI). As part of your training at this level, the Head of the SAI wants you to evaluate the following suggested audit opinions for four (4) clients.

Ministry of Defence

A misstatement of K2 million has been detected in the value of inventory for lubricants. The misstatement is considered to be immaterial. The Audit Senior has suggested an unmodified audit opinion.

Competition and Consumer Protection Commission (CCPC)

An employee was awarded K500,000 by the Industrial Relations Court after successfully suing CCPC for unfair dismissal. The Finance Director has not recognised any liability. The amount awarded is considered material but not pervasive to the financial statements. The Audit Senior has suggested a disclaimer of opinion.

Ministry of Transport and Logistics

There was no evidence available to reliably verify the accuracy of the depreciation figure of K45 million for a number of motor vehicles. This is considered to material and pervasive to the financial statements. The Audit Senior has suggested an adverse opinion and the inclusion of an emphasis of matter paragraph.

Business Regulatory Review Agency (BRRA)

Trade receivables have been overstated by K7 million. This is considered material but not pervasive to the financial statements. The Audit Senior has suggested an unmodified opinion and the audit report must include a Key Audit Matter (KAM) section.

Required:

- (a) Define reasonable assurance given by Public Sector Auditors in assurance engagements. (2 marks)
- (b) Explain the factors to consider when determining to use the work of the internal auditors by external Public Sector Auditors. (6 marks)
- (c) Evaluate the appropriateness or otherwise of the suggested audit opinions for the four (4) clients. (12 marks)

[Total: 20 Marks]

END OF PAPER

PFM 5 PUBLIC SECTOR AUDITING

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) Responsibilities of the Auditor-General Office and the Public Accounts Committee (PAC): The Audit-General's Office is responsible for the examination of public accounts to attest to the use of various public funds as were sanctioned by Parliament at the beginning of the year. It is seen to assist Parliament to control public funds and their use, through its assistance to the Public Accounts Committee (PAC) in the form of its examinations of all accounts of government organisations.

The Public Accounts Committee (PAC) receives the audited public accounts and departmental accounts and other special audit reports, examines and debates the contents and submits its report(s) in the form of findings and recommendations to the whole House. Parliament takes action on the Public Accounts on the basis of the recommendations of the committee.

(b) Ethical threats and safeguards

| (i) Ethical threats | Explanations | (ii) Safeguards |
|---|---|---|
| (1) The audit senior | The audit senior is the brother to the Chief Accountant for the Ministry of Finance and National Planning. This creates both familiarity and self-interest threats, which may impair independence and objectivity. He may not exercise appropriate levels of professional scepticism. | Since both of them occupy senior positions, the familiarity and self-interest threats are more significant. Hence, He should be replaced with someone who is independent. |
| (2) Temporary engagement of audit staff | This will create both self-review and familiarity threats. The seconded audit staff could end up auditing their own work. This may adversely impact on objectivity. | It is possible that auditors seconded may learn and gain new perspectives from working at the Ministry and the new skills could benefit the firm in the long-run. However, seconded audit staff should not be assigned to the audit team. |
| (3) Invitation to the annual ball | The invitation to the annual ball creates a self-interest threat to the audit team. This can lead to the team losing objectivity in the carrying out of the audit. The motive to invite the audit team to the annual | The invitation to the annual ball must be politely declined. |

| | | |
|---|--|---|
| | ball may be to influence them in the audit work. | |
| (4) Negotiating loan restructuring with the International Monetary Fund (IMF) | This will entail taking management responsibility. This creates advocacy threat to objectivity. The Auditor-General (AG) will be expected to support the Ministry of Finance and National Planning at all costs. | The AG should politely refuse to negotiate loan restructuring with the International Monetary Fund (IMF). |

(c) Methods of gathering sufficient appropriate audit evidence in the financial statement audit of the Ministry of Finance and National Planning:

- **Inspection** – this will involve the examination of documents or records in the Ministry of Finance and National Planning. It also includes physical inspection of items such as tangible non-current assets. In the financial statement audit of the Ministry of Finance and National Planning, inspections may include physical inspection of the vehicles.
- **Observation** – this will involve the public sector auditors looking at a process being performed by others with the objective of confirming that the process is being carried out as it should be. An example of observation in the Ministry of Finance and National Planning could be the public sector auditor's observation of inventory counting.
- **External Confirmation** – this will be done by way of the public sector auditor seeking third party confirmation. In the financial statement audit of the Ministry of Finance and National Planning, external confirmation will be used to confirm account balances, such as bank balances.
- **Recalculation** – this will involve checking the mathematical accuracy of documents and records by the auditor. In the financial statement audit of the Ministry of Finance and National Planning, recalculation may include recalculating, on a sample basis, the depreciation figures.
- **Re-performance** – this will involve the public sector auditor executing a procedure or control originally performed as part of the internal controls of the entity. In the financial statement audit of the Ministry of Finance and National Planning, re-performance may include re-performance of the bank reconciliation for a particular month.
- **Analytical procedures** – this will involve evaluating and comparing financial and/or non-financial data for plausible relationships. It will also involve the investigations of identified fluctuations and relationships that are not consistent with other relevant information or deviates from predicted amounts. In the financial statement audit of the Ministry of Finance and National Planning, analytical procedures may include comparing of actual payroll costs and the budgeted payroll costs.
- **Enquiry** – this will range from formal written enquiries to oral enquiries to oral enquiries of persons within and outside the entity. In the financial statement

audit of the Ministry of Finance and National Planning, enquiry may be used when gaining an understanding of the Ministry of Finance and National Planning and its environment.

(d) Meaning of audit risk:

Audit risk is the risk that auditors issue an incorrect audit opinion to the audited financial statements. For example, auditors issue an unmodified audit opinion to the audited financial statements even though the financial statements are materially misstated. Or a modified audit opinion is issued as the result of immateriality found in financial statements.

(e) Audit risks in the audit of the Ministry of Finance:

First audit

The Audit Manager was recently appointed and there is a possibility that this is the first time for him/she to be in charge of such a "big audit" involving the Ministry of Finance and National Planning. The Audit Manager may not have all the knowledge of the operations of the Ministry of Finance and National Planning. Hence, the risk of not detecting material misstatements could be higher.

Public sector

The public sector is an inherently risky sector, which increases the overall audit risk associated with the assignment. Various items in the financial statements could be affected by this inherent risk. The sector is subject to substantial political pressure and public scrutiny.

Recognition of the loan K30 million with Construction Bank

There is a risk that the loan has not been recognised in accordance with the guidelines given in IPSAS 5 *Borrowing costs*. It is possible that the net borrowing costs may have been expensed instead of capitalised, resulting in an overstatement of the surplus and understatement of non-current assets.

Ministry of Finance and National Planning has an ownership interest in a ZamZam Railways, which operates as a Government Business Enterprise (GBE) and other entities

IPSAS 6 *Accounting for Controlled Entities* gives detailed guidance in this area. Although the rail authority is allowed to operate autonomously and does not rely on the government for funding, the government has the power to appoint and remove a majority of the members of the governing body of rail authority. This is despite that the government has never exercised this power before. There is a risk that the accounting treatment is not in accordance with the guidance given in IPSAS 6.

Related parties

IPSAS 20 *Related Party Disclosure* gives detailed guidance in this area. Dealing between two entities under same control are related party transactions. The accounting requirement is that related parties and related party transactions must be

disclosed in the financial statements. There is a risk that there is no disclosure of related party relationship and dealings with them in accordance with IPSAS 20.

- (f) Audit procedures to be performed on completeness of related party disclosures:
- Enquire of management and the directors as to whether transactions have taken place with related parties that are required to be disclosed by the disclosure requirements that are applicable to the Ministry of Finance and National Planning
 - Review of prior year working papers for names of related parties
 - Review of accounting records for large or unusual transactions or balances, in particular transactions recognised at or near the end of the financial period
 - Examine any agreements and contracts involving directors and connected persons, including tracing the details of such transactions to any source documentation.
 - Review subsequent events in order to consider whether they might have any impact on the matters requiring disclosure.
 -

SOLUTION TWO

- (a) (i) **Principles of transparency and accountability in the public sector:**
It is required that those entrusted with the use of public funds should be transparent on how they use the public funds and should be held accountable and answerable on how they have used the public funds.

Transparency – This principle requires that those who spend public funds should be open on how they use the funds. This is because public funds are required to be spent in the interest of the general citizenry.

Accountability – This principle requires that those entrusted with the use of public funds should be answerable on how they spend the public funds. All funds must be spent in the interest of the citizens who pay taxes to the government.

- (ii) **Role of Supreme Audit Institution in public sector:**
The Supreme Audit Institution (SAI) plays a major role in holding those who are responsible for the public purse are transparent on how these funds are used and are held accountable on the use of public funds.

This is achieved in the following way:

- The SAI carried out audits of how the executive spends public funds and issues reports of their findings and also makes recommendations as necessary.
- The reports of the SAI are passed on to the Public Accounts Committee which is responsible for following up audit findings with the relevant controlling officers in the public sector.

- (b) (i) **Ethical issues in the Supreme Audit Institution:**
- 1. Lack of formal education by staff in the SAI:**
The lack of relevant qualifications could be an ethical issue in that the staff may not be able to perform effective audits. This is in breach of the principle of *professional competence and due care*.
 - 2. Staff receiving allowances from audited entities:**
The fact that staff of the SAI receive allowances from the organizations that they audit is an ethical issue. It means that the staff lack integrity in the carrying out of their work. They are required to be straight forward and honest in discharging their work.
 - 3. Claims for allowances not worked for:**
Claiming allowances for days not worked for is fraud on the part of the staff of the SAI. This is in breach of the ethical principle of **integrity** and **professional behavior**. The action by the staff of the SAI brings the name of the accountancy profession into disrepute.

4. Lack of SAI Code of ethics:

The lack of a code of ethics by the SAI in a matter that is not acceptable. The SAI is required to lead by example in all that it does. The SAI should have its own code of ethics which SAI staff are expected to follow.

(ii) **Professional judgment and professional skepticism:**

Professional judgment – This is the use by the public sector auditors the skills and competences acquired through training in making decisions. For example, to determine the size of samples to test is a matter of professional judgment.

Professional skepticism – This is the attitude of maintaining a questioning mind by the auditor and looking out for evidence that may contradict other evidence.

SOLUTION THREE

(a) KEY STAGES OF A FORENSIC INVESTIGATION

1. Before carrying out a forensic investigation it is necessary for the forensic auditor to determine the scope and objectives of the investigation.

This requires answers such as:

- What is the nature of the fraud being investigated?
- Who are involved?
- What is the extent of the fraud in terms of monetary value?
- What evidence is required and what reporting form will be required?

In the case at hand:

The objective is to establish how staffs within the procurement division and those at the ministry have managed to carry out the fraud undetected during the last three years.

2. Understanding the organization and the allegations:

Before embarking on the fraud investigation, it is necessary that the auditor has a clear understanding of the nature of the organization as well as the nature of fraud itself.

In the case at hand:

There is need to gain an understanding of the operations of the Ministry of Health and specifically matters relating to procurement. The roles played by the officials within the ministry and the procurement division. There is need to look out for any opportunities for fraud in gaining an understanding of the organization

3. Securing and safeguard financial and other information:

Auditors will need to gather evidence which will help in establishing the facts on how the fraud was carried out. This evidence could be electronic or indeed hard papers such as invoices and other documentation. Staff being investigated will be motivated to cover up and destroy any such evidence.

In the case at hand:

There is need for the investigator to quickly move in and secure all important documents. In this case all documents used in the procurement of drugs are kept by the Chief Procurement Officer. These must be retrieved and kept securely and only returned at the conclusion of the investigation. Documents that may be kept by the financial department can also be retrieved for safe keeping.

4. Inspecting financial information and document:

Critically examining documents and identifying 'red flags' which are indicative of fraud having taken place. To do this the auditor should have the skill and required experience and matters that should be looked into include signature forgeries, signs of tempering with documents, copies instead of originals.

In the case at hand:

This will involve inspecting the documents for procurement as well as the supplier invoices and any documentation related to the receipt of drugs purchased.

5. Interviewing staff and third parties:

This is an important element of the investigation and may result in confessions. This requires skills of interviews and interrogations.

In the case at hand:

The auditor may need to interview staff involved in procurement at the ministry of health and also staff from the procurement division.

6. Drawing conclusions:

This is the outcome of the investigation. The investigator should be aware that the conclusion and report thereon may be passed on the investigating authorities and so the conclusions should be based on facts obtained and should not be biased.

In the case at hand:

The investigator will have to conclude based on evidence gathered whether there was fraud in the procurement of drugs and the people who are involved.

7. **Producing the report:**

A report will be the outcome of the investigation and the form of report will depend on the nature of the assignment. The report should be clear easily understood and supported by evidence.

In the case at hand:

At the end of the investigation for alleged fraud in the procurement of drugs a report will be prepared and circulated as expected to the relevant authority.

(b) **Economy** – this relates to the cost of undertaking an activity. Economy refers to minimizing of cost without ignoring quality.

In the case of the procurement of drugs it is clear that this has not been achieved because prices were inflated in order to perpetuate fraud by those responsible for procurement.

Efficiency – this refers to comparing the outputs comparing the inputs of an activity. The higher the productivity for given resources the better.

In the case of the procurement of drugs this element has also not been fulfilled. Substantial sums of financial resources were allocated for the procurement of drugs but the outcome was far below the expectations because of the fraud.

Effectiveness – drugs are not available at the health facilities run by the government. Effectiveness refers to being able to meet the objectives of the activity in this case availability of drugs at health facilities.

This element has not been achieved as there were noted shortages of drugs at most health care facilities.

(c) **Elements of quality control for an SAI:**

1. **Leadership responsibilities for quality**

SAI should establish policies and procedures which promote quality as part of the culture of the institution. This should be from the highest level of the institution.

2. **Relevant ethical requirements**

The SAI should have its own code of ethics which staff working for the SAI should follow. The SAI should lead by example in complying with its own code of conduct containing ethical values of the SAI.

3. **Acceptance and continuation of audits to be carried out**

SAI should have policies to ensure that the integrity of management is not questionable. It should be noted that SAIs largely do not have the discretion about the work they will carry out. Considering integrity helps the SAI decide how to deal with risk that will arise due to lack of integrity of management.

4. **Human resources**

SAI should have policies and procedures to provide it with reasonable assurance that it has necessary resources with the requisite skills and competences to perform its duties.

5. Engagement performance

Policies and procedures to ensure work were conducted in accordance with relevant standards. This entails supervision and a review of responsibilities of the work that has been carried out.

6. Monitoring

There should be monitoring systems in place in order to give reasonable assurance to the SAI that quality control processes and procedures are relevant, adequate and operating effectively all the times.

SOLUTION FOUR

(a) Definition of cybercrime:

Cyber-crime is the threat passed to an organizations computer systems. It arises from the fact that organizations no longer have closed systems and are connected to other organizations i.e. supplies, banks etc.

It comes about due to unauthorized access to a system with the motive to cause harm to the organization.

THREATS POSED BY CYBER – CRIME

- **Direct threat**

Involves theft by people who gain unauthorized access to an organization's systems. It could involve transfer of money from the organization into the criminal's bank account.

- **Malicious Damage**

Involves accessing an organizations system and corrupting the programs. It leads to data being deleted and installing programs which cause damage overtime through data corruption.

- **Data Theft**

Involves unauthorized access to an organizations' IT system and thereby accessing sensitive data.

- **Ransom-Ware Attacks**

Involves gaining access to an organization's data and encrypting the data so that it cannot be used. Later, the criminals demand a ransom in order for them to decrypt the data to have it accessed.

- **DENIAL OF SERVICE ATTACKS**

Involves targeting the website of the organization's system and flooding it with traffic so that accessing the website is made difficult.

(b) **i. ANALYTICAL PROCEDURE TO MEET EACH OF THE AUDIT OBJECTIVES IN THE QUESTION**

The following are possible procedures and actions:

1. Procedure

A trend analysis of the total costs of the provision of services to the local community in previous financial years.

Action

Any deviation from the trend may indicate errors in the allocation of costs and should be presented to management for them to provide explanations for the deviation. The persuasiveness of the explanations provided will help to determine the assessed risk to this objective and subsequent audit activity.

2. Procedure

Calculate the unit costs of the provision of each type of service with the rates paid for the service of the procedure. Although surpluses in one type of service can be used to offset deficits in the delivery of others, in the longer term this will put pressure on the overall cost of delivery, particularly if the direction of movement on rates is downward. Trend analysis of costs and rates for different would help to further assess sustainability in this area.

Action

Where problems are apparent, management should be asked to provide details of their action plans to address the problems.

3. Procedure

Expenditure on the provision of different types of rates should be profiled over the year and compared with the council's budget for the procedures. significant variances from budget may indicate problems in planning or cost control.

Action

Where variances occur, management should be asked to provide details of their analysis of the causes, and the action taken to bring actuals back into line with the budget, or to reallocate resources to meet requirements.

(ii) **ACCOUNTABILITY TRIANGLE**

- Parliament – Confers responsibility
- Auditors reporting/Accountability audits

- Auditor General - Conferred responsibility
- Ministers – Conferred responsibility

SOLUTION FIVE

(a) Reasonable assurance

Reasonable assurance is high but not absolute. The audit conclusion is expressed positively, conveying that, in the auditor's opinion, the subject matter is or is not compliant in all material respects, or, where relevant, that the subject matter information provides a true and fair view, in accordance with the applicable criteria.

(b) The public sector auditors shall determine:

- Whether the work of the internal auditor's is likely to be adequate for the purpose of the audit.
- If, so the planned effect of the work of the internal auditors on the nature, timing or extent of the external auditor's procedures.
- The objective of the internal audit function
- The technical competence of the internal auditors
- Whether the of the internal auditors is likely to be carried out with due professional care
- Whether there is likely to be effective communication between the internal and the external auditors.
- The nature and scope of the specific work performed by the internal auditors.

(c) Appropriateness of audit opinions

Ministry of Defence

The misstatement is considered to be immaterial and therefore the opinion will not be modified. Hence the suggested unmodified opinion is appropriate. However, it may be worth including this in the report to management.

Competition and Consumer Protection Commission (CCPC)

The omitted liability is considered material but not pervasive and the audit opinion will need to be modified. A disclaimer of opinion applies where there is lack of sufficient appropriate evidence which is considered material and pervasive. The suggested audit opinion is inappropriateness as sufficient appropriate audit evidence is available. The appropriate audit opinion is a qualified audit opinion since the misstatement is material but nor pervasive to the financial statements.

Ministry of Transport and Logistics

An adverse audit opinion is given where there is a misstatement considered both material and pervasive. In this case, there is lack of sufficient appropriate audit evidence and adverse is grossly inappropriate. In addition, an emphasis of matter paragraph is not used if a modification is given.

The suggested audit opinion is wrong. The appropriate audit opinion will be a disclaimer of audit opinion since there is lack of sufficient appropriate audit evidence which is considered material and pervasive.

Business Regulatory Review Agency (BRR)

The misstatement is considered material but not pervasive to the financial statements. Since the misstatement is material, the audit opinion will need to be modified. The suggested unmodified audit opinion is incorrect. In addition, the inclusion of a key audit matter paragraph is not appropriate.

The appropriate audit opinion is a qualified audit opinion.

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 6: FINANCIAL REPORTING FRAMEWORK FOR PUBLICSECTOR ENTITIES

MONDAY 12 DECEMBER 2022

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 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.

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

Below is a Kitwe City Council (KCC) trial balance as at 31 December 2021.

| Descriptions | Debit K'000 | Credit K'000 |
|---|------------------------|-------------------------|
| Cash and cash equivalents | 16,000 | |
| Trade and other receivables (less than one year) | 12,000 | |
| Other financial assets (less than one year) | 70,000 | |
| Revaluation reserve | | 3,000 |
| Accumulated surpluses | | 32,000 |
| Trade and other receivables (more than one year) | 93,000 | |
| Other financial assets (more than one year) | 2,910 | |
| Inventory as at 1 January 2021 | 12,000 | |
| Investment property | 60,000 | |
| Provision for depreciation on investment property | | 15,000 |
| Property, plant and equipment | 45,300 | |
| Provision for depreciation on property, plant and equipment | | 12,000 |
| Intangible assets | 36,000 | |
| Short term Trade and other payables | | 30,000 |
| Short term Borrowings | | 8,000 |
| Long term Trade and other payables | | 13,000 |
| Long term Borrowings | | 140,000 |
| Rates, levies and charges | | 77,450 |
| Fines and charges | | 5,200 |
| Rental income | | 4,780 |
| Interest received | | 1,600 |
| Sales revenue | | 600 |
| Other income | | 500 |
| Revenue grants | | 40,000 |
| Capital grants as at 1 January 2021 | | 90,000 |
| Salaries and wages | 84,900 | |
| Materials and services | 28,700 | |
| Finance costs | 12,320 | |
| Total | 473,130 | 473,130 |

Additional information

(1) The accounting policies are as follows:

- Revenue grant is to be treated as a credit in the statement of financial performance.
- Capital grants are treated as deferred income and 20% is transferred to statement of financial performance annually.

- (2) Depreciation policy
- Investment property 10% on cost
 - Property, plant and equipment 25% on cost
- (3) As at 31 December 2021, closing inventory had a cost of K18,000,000 although the net realisable value was K15,000,000.
- (4) Sales revenue of K20,000 was posted to Rental income in error.
- (5) A transfer from Revaluation Reserve of K1,000,000 should be made to Accumulated Surpluses.

Required:

- (a) Using the information above, prepare the following in accordance with IPSAS1:
- (i) Statement of Financial Performance for the year ended 31 December 2021. (14 marks)
 - (ii) Statement of Financial Position as at 31 December 2021. (13 marks)
- (b) List four (4) internal users and four (4) external users of General Purpose Financial Reports (GPFR). (4 marks)
- (c) Explain the following qualitative characteristics of information included in the General Purpose Financial Reports (GPFR):
- (i) Faithful representation. (3 marks)
 - (ii) Comparability. (3 marks)
 - (iii) Timeliness. (3 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Attempt THREE (3) questions.

QUESTION TWO

You are the Director of Finance for Drug Enforcement Commission (DEC), which prepares financial statements in accordance with accrual-based International Public Sector Accounting Standards (IPSASs). The Senior Financial Accountant has requested advice from you regarding the following transactions relating to the year ended 31 December 2021:

Transaction one

The National Government (transferor) lent the Drug Enforcement Commission (DEC) (reporting entity) K50 million to enable the DEC to acquire a drug testing machine. After a change in policy, the national government decides to forgive the loan. There are no stipulations attached to the forgiveness of the loan. The National Government writes to DEC and advises it of its decision; it also encloses the loan documentation, which has been annotated to the effect that the loan has been waived.

Transaction two

On 11 January 2022, when the Drug Enforcement Commission's (DEC's) business was closed for a national holiday, an arsonist set fire to DEC's inventories with a carrying amount of K1,220,000 and they were all destroyed. This is considered as material. The inventories are insured and the insurance company has agreed to settle the claim in full.

Transaction three

Further, the DEC acquired a piece of land from Kapiri Mposhi District Council at a cost of K60,000 on 1 January 2021. The Commission has by 31 December 2021, not decided what to do with this land. The land has a fair value of K80,000 at the year end.

Transaction four

The DEC has spent K600,000 on research related to the development of a methodology which could assist the commission in facilitating the quick rehabilitation of drug addicts. The methodology will be patented once fully developed.

Required:

- (a) Explain the relationship between the International Federation of Accountants (IFAC) and the International Public Sector Accounting Standards Board (IPSASB). (4 marks)
- (b) Explain any two (2) publications developed and issued by the International Public Sector Accounting Standards Board (IPSASB). (4 marks)
- (c) Using appropriate International Public Sector Accounting Standards (IPSASs), explain the accounting treatment of the four (4) transactions given in the scenario.

(12 marks)

[Total: 20 Marks]

QUESTION THREE

The following entries we discovered during the consolidation of the Financial Report by the Auditor General.

- (i) On 1 April 2020 the sum of K15,000,000 was withdrawn from Ministry of National Development Planning Account and charged to the consolidated fund. The fraud was discovered on 15 February 2021.
- (ii) On 17 July 2021, an over payment of K2,050,000 was made to Luke Warm Ltd in respect of Supply of Furniture to the new Government built by the former Administration. This was discovered on 21 September 2021.
- (iii) On 30 October 2021, an amount of K55,000 being revenue accrued to the government from rent of property which was never received but was abandoned.
- (iv) On 30 November 2021, an officer died on duty. The aggregate of this person emoluments and gratuity was K78,705, while he had an outstanding motor vehicles advance K106,815.
- (v) On 15 November 2021 the sum of K465,000 which was initially charged to correspondence advance had been abandoned.

Required:

- (a) Prepare journal entries for the transactions above before consolidating the financial reports. (10 marks)
- (b) Explain the main elements of IPSAS 20: Related Party Disclosures and key related party disclosures in the Financial Statements. (10 marks)

[Total: 20 Marks]

QUESTION FOUR

The Railways Development Agency (RDA), is a parastatal body which is mandated to supervise the construction of Railway projects in the country. It also approves designs and cost estimates of railway projects. RDA receives its funding for its operations from the Central Government and the fees it collects from cargo and passengers. RDA's mission statement is to be the most preferred railway company for bulk cargo and travelers who want to have a feel of rural and peri- urban scenic beauty of the country.

RDA has appointed a new Board of Director after the previous Board was dissolved due to alleged poor performance. The new Board has received several recommendations from its stakeholders and some feel that the company has concentrated on making money at the expense improved services. It was also felt that the company need to improve its internal operations in order to reduce cost and pass on the benefits of such savings to customers in form of low charges.

Among other measures to be implemented, the new Board is considering appraising the past financial statements using key important ratios. In addition, they would like to assess the RDA in a more holistic way by using a Balance Score Card. This was due to the reason that it is difficult to accurately measure the performance of a public sector due to the underlying

weaknesses in the public sector financial reporting as compared to a private sector organization.

An extract of Statement of the Financial Performance and Statement of Financial Position for the year ended 31 December 2021 is given below;

RDA Statement of Financial Performance for the year ended 31 December 2021;

| REVENUE | K'000 |
|-----------------------------------|-----------------------|
| Revenue from passengers and cargo | 1,196,000 |
| Other income | <u>46,250</u> |
| Total operating income | 1,242,250 |
| Expenditure: | |
| Total expenditure | <u>(515,820)</u> |
| Operating profit | 726,430 |
| Interest income | <u>17,652</u> |
| | 744,082 |
| Interest expense | <u>(6,200)</u> |
| SURPLUS | <u>737,882</u> |

Statement of Financial Position as at 31 December 2021

| Non-Current assets | K'000 | K'000 |
|---|----------------|------------------|
| Property, Plant and Equipment | | 1,433,920 |
| Total Current assets | | <u>184,640</u> |
| Total assets | | <u>1,618,560</u> |
| Capital Fund, reserves and Liabilities | | |
| Capital Fund | 258,402 | |
| Surplus | <u>737,882</u> | |
| | 996,284 | |
| Revaluation reserves | <u>40,915</u> | |
| | | 1,037,199 |
| Liabilities; | | |
| Non-current liabilities | | <u>512,791</u> |
| | 1,549,990 | |
| Total current liabilities | | <u>68,570</u> |

Note:

1. Closing inventory was valued at K23,400,000
2. Receivables amounted to K12,600,000 while trade payables amounted to K13,500,000

Performance ratios for 2020 are as follow:

- (i) Operating profit margin =42%
- (ii) Gross profit margin=51%
- (iii) receivable days= 5 days
- (iv) payable days =6 days
- (v) current ratio =3:1
- (vi) acid–test ratio =2:1

Required:

- (a) Calculate any two (2) accounting ratios under each of Profitability, liquidity, efficiency and debt gearing ratios for the year ended 31 December 2021. (8 marks)
- (b) Comment briefly on the **profitability** and **liquidity** ratios only of RDA in 2021 compared to 2020. Comments on other ratios are not required. (2 marks)
- (c) Explain five (5) weaknesses that exist in measuring performance of a public sector entity's reporting framework. (5 marks)
- (d) Explain five (5) advantages of measuring the performance of RDA using a Balanced Score Card. (5 marks)

[Total: 20 Marks]

QUESTION FIVE

The Government of Republic X prepares its Financial Statement at the end of 31 December each year. In March 2021, the parliamentary accounts committee heard that the financial statements of the Government were not reliable. The Auditors disclosed that they had incorrectly accounted for large amounts of non-tax revenue over the past three (3) years. Apparently the Government had recorded K10 millions of income at the end of the year that should have been attributed to next quarter. In this way the Government manipulated the accounts because they were scheduled to meet the International Monetary Fund who had set a bench mark on the percentage of non-tax revenue to be collected by the government.

Required:

- (a) Discuss the governance issues regarding financial reporting in Government X and reforms the Government should embark on to improve financial reporting of revenues. (9 marks)
- (b) Explain the risks associated with revenue accounting for country X and how these risks can be mitigated. (11 marks)

[Total: 20 Mark]

END OF PAPER

PFM 6 FINANCIAL REPORTING FRAMEWORK FOR PUBLIC SECTOR ENTITIES

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) Kitwe City Council (KCC)

(i) Statement of Financial Performance for the year ended 31 December 2021

| Descriptions | K'000 | K'000 |
|------------------------------------|--------|----------------|
| Revenue | | |
| Rates, levies and charges | | 77,450 |
| Fines and charges | | 5,200 |
| Rental income (W1) | | 4,760 |
| Interest received | | 1,600 |
| Sales revenue (W2) | | 620 |
| Other income | | 500 |
| Amortisation of capital grant (W3) | | 18,000 |
| Revenue grants | | 40,000 |
| Total revenues | | 148,130 |
| Expenses | | |
| Salaries and wages | 84,900 | |
| Materials and services (W4) | 25,700 | |
| Depreciation (W5) | 17,325 | |
| Finance costs | 12,320 | |
| Total expenses | | 140,245 |
| Surplus/(Deficit) for the year | | 7,885 |

(ii) Statement of Financial Position as at 31 December 2021.

| Descriptions | K'000 | K'000 |
|--|--------|----------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | | 16,000 |
| Trade and other receivables (less than one year) | | 12,000 |
| Other financial assets (less than one year) | | 70,000 |
| Inventory at 31 December 2022 | | 15,000 |
| Total current assets | | 113,000 |
| Non-current assets | | |
| Trade and other receivables (more than one year) | 93,000 | |
| Other financial assets (more than one year) | 2,910 | |
| Investment property (W6) | 39,000 | |
| Property, plant and equipment (W7) | 21,975 | |
| Intangible assets | 36,000 | |
| Total non-current assets | | 192,885 |
| Total assets | | 305,885 |
| Liabilities and equity | | |
| Liabilities | | |
| Current liabilities | | |
| Short term Trade and other payables | 30,000 | |

| | | |
|------------------------------------|---------|----------------|
| Short term Borrowings | 8,000 | |
| Total current liabilities | | 38,000 |
| Non-current liabilities | | |
| Capital grants (W8) | 72,000 | |
| Long term Trade and other payables | 13,000 | |
| Long term borrowings | 140,000 | |
| Total non-current liabilities | | 225,000 |
| Total liabilities | | 263,000 |
| Net assets | | 42,885 |
| Net assets/Equity | | |
| Revaluation reserve (W9) | | 2,000 |
| Accumulated surpluses (W10) | | 40,885 |
| Total net Assets/Equity | | 42,885 |

Workings

(1) Rental income

| | |
|------------------------|--------------|
| | K'000 |
| Per trial balance | 4,780 |
| Less error in posting | <u>(20)</u> |
| Adjusted rental income | <u>4,760</u> |

(2) Sales revenue

| | |
|-------------------------------|------------|
| | K'000 |
| Per trial balance | 600 |
| Add error in posting | <u>20</u> |
| Adjusted sales revenue figure | <u>620</u> |

(3) Amortisation of capital grant

| | |
|---------------------|---------------|
| | K'000 |
| 20% X K90,000,000 = | <u>18,000</u> |

(4) Materials and services

| | |
|-------------------|--------|
| | K'000 |
| Per trial balance | 28.700 |
| Opening inventory | 12,000 |

| | |
|--|-----------------|
| Closing inventory | <u>(15,000)</u> |
| Adjusted figure | <u>25,700</u> |
| (5) Depreciation | |
| | K'000 |
| Investment property (60,000 X 10%) | 6,000 |
| Property, plant and equipment (45,300 X 25%) | <u>11,325</u> |
| Total | <u>17,325</u> |

| | |
|--|-----------------|
| (6) Investment property | |
| | K'000 |
| Per trial balance | 60,000 |
| Less Accumulated depreciation (15,000 + 6,000) | <u>(21,000)</u> |
| Carrying amount | <u>39,000</u> |

| | |
|---|-----------------|
| (7) Property, plant and equipment | |
| | K'000 |
| Per trial balance | 45,300 |
| Less Accumulated depreciation (12,000 + 11,325) | <u>(23,325)</u> |
| Carrying amount | <u>21,975</u> |

| | |
|------------------------|-----------------|
| (8) Capital grants | |
| | K'000 |
| Per trial balance | 90,000 |
| Less Amortisation (W3) | <u>(18,000)</u> |
| Net amount | <u>72,000</u> |

| | |
|-------------------------|-------|
| (9) Revaluation reserve | |
| | K'000 |
| Per trial balance | 3,000 |

| | |
|----------------------------|----------------|
| Less transfer | <u>(1,000)</u> |
| Net amount | <u>2,000</u> |
| (10) Accumulated surpluses | |
| | K'000 |
| Per trial balance | 32,000 |
| Add transfer | <u>1,000</u> |
| Net amount | <u>33,000</u> |

(b) Users of General Purpose Financial Reports (GPFR)

- **Internal users**

- The President/Vice President and Ministers
- The National Assembly/Parliament
- Regulatory and oversight bodies
- Top public administrators such as Permanent Secretaries, Directors/Heads of departments
- The Chief Executives of Parastatals
- Labour union' etc.

- **External users**

- Members of the Public
- Companies that do business with Government
- Foreign countries
- Financial institutions such as the World Bank, International Monetary Fund (IMF), African Development Bank (ADB), Commercial Banks etc.
- Creditors, both local and foreign
- Investors
- Researchers and
- Political parties, trade unions, civil society organisations etc.

(c) Qualitative characteristics of information included in the General Purpose Financial Reports (GPFR)

- **Faithful representation** – this is attained when information is complete, neutral, and free from material error. Information that faithfully represents an economic or other phenomenon depicts the substance of the underlying transaction, which is not necessarily always the same as its legal form. An omission of some information can cause the representation of an economic or other phenomenon to be false or misleading.

- **Comparability** – this is not a quality of an individual item of information, but rather a quality of the relationship between two or more items of information. Comparability differs from consistency. Comparability is the goal, and consistency helps in achieving that goal. Comparability also differs from uniformity. For information to be comparable, like things must look alike and different things must look different. An over-emphasis on uniformity may reduce comparability by making unlike things look alike.
- **Timeliness** – this means having information available for users before it loses capacity to be useful for accountability and decision-making purposes. A lack of timeliness can render information less useful. Having relevant information available sooner can enhance its usefulness as input to assessments of accountability and its capacity to inform and influence decisions that need to be made.

SOLUTION TWO

(a) Relationship between the International Federation of Accountants (IFAC) and the International Public Sector Accounting Standards Board (IPSASB)

The IPSASB, is a Board of IFAC formed to develop and issue under its own authority International Public Sector Accounting Standards (IPSAS).

Currently, the IPSASB comprises 18 members, 15 of whom are nominated by the member bodies of IFAC and three of whom are appointed as public members. Public members may be nominated by any individual or organisation.

This is intended to enhance the quality and transparency of Public Sector Financial Reporting by providing better information for public sector financial management and decision making.

The IPSASB supports the convergence of international and national public sector accounting standards and the convergence of accounting, and also promotes the acceptance of its standards and other publications.

(b) Publications

The IPSASB develops and issues the following publications:

- (1) IPSASs; as the standards to be applied in the preparation of General Purpose Financial Reports (GPFR's) of public sector entities other than GBEs.
- (2) Recommended Practice Guidelines (RPGs) to provide guidance on good practice that public sector entities are encouraged to follow.
- (3) Studies, other papers and research reports to provide information that contributes to the body of knowledge about Public Sector Financial Reporting issues and developments.

(c) Accounting treatments

Transaction one

IPSAS 23, Non-Exchange Transactions gives detailed guidance in this area. When it receives the letter and documentation from the national government, which communicates this decision, the DEC derecognizes the liability for the loan and recognises revenue in the statement of financial performance of the reporting period in which the liability is derecognised.

Transaction two

This is normally classified as a non-adjusting event, according to IPSAS 14, *Events After the Reporting Date*. Since the matter is material, the standards requires that the details of this non-adjusting event to be disclosed as a note to the financial statements for the year ended 31 December 2021 as a total loss of K1,220,000 and the effect of the insurance recovery should be disclosed separately.

Transaction three

IPSAS 16, Investments in Property gives detailed guidance in this area. The piece of land should be classified as investment property. The management of the DEC should decide whether it wishes to follow a cost model or a fair value model for all its investment property. If the fair value model is selected, the DEC should take the gain of K20,000 through surplus or deficit for the period.

Transaction four

IPSAS 31 *Intangible Assets* gives guidance in this area. The standard states that research expenditure should be expensed. Capitalisation of development expenditure is only allowed if it meets the criteria in IPSAS 31.

SOLUTION THREE

(a) Journal Entries

| | Details | DR | CR |
|---|--|------------|------------|
| i) | Non Personal Advance A/C | 15,000,000 | |
| | Consolidated A/C | | 15,000,000 |
| Being Funds Fraudulently with drawn | | | |
| ii) | Non Personal Advance A/c | 2,050,000 | |
| | Ministry of Housing and Infrastructure | | 2,050,000 |
| Being overpayment for supply of Furniture | | | |
| iii) | No Adjustment required | | |
| iv) | Loss A/c | 28,110 | |
| | Motor vehicle A/C | | 28,110 |
| Being irrecoverable advance written off | | | |
| v) | Loss A/C | 465,000 | |
| | Correspondence Advance A/C | | 465,000 |
| Being amount charged to advance account now abandoned. | | | |

(b)

| | |
|--|--|
| | <p>Explain the main elements of IPSAS 20: Related Party Disclosures and examples of related parties.</p> <p>Related party has two elements Control and Significant Influence</p> <ul style="list-style-type: none"> • Control is the ability to obtain benefits by governing the operating and financial policies of an entity. • Significant influence is the ability to participate in, rather than control , the financial and operating policy decisions of another entity <p>Key related Party Disclosures:</p> <ul style="list-style-type: none"> • The nature of relationships between a parent or controlling entity and subsidiaries or controlled entities , even if there were no transactions between those related parties • The name of the entity's parent or controlling entity and, if different the ultimate controlling entity • Compensation or remuneration of key management personnel and if applicable, information about the compensation or remuneration of close family members of key personnel • Detail of loans to key management personnel and their close family members including advances , repayments and closing balances |
|--|--|

SOLUTION FOUR

(a)

Profitability ratios

- (i) Operating profit /funds employed x 100 = $746,430/1,549,990 \times 100 = 48\%$
- (ii) Profit margin=Surplus/revenue= $737,882/1,196,000 \times 100 = 62\%$

Liquidity ratios

- (i) Current assets ratio=current assets /current liability= $184,640/68,570 = 2.7: 1$
- (ii) Quick/acid test ratio=current assets-stock/current liabilities = $184,640-23,400/68570 = 2.4: 1$

Efficiency ratios

- (i) Receivables days=receivables /total income= $12,600/1,196,000 \times 365 = 3.8\text{days}$
- (ii) Assets turnover=revenue/ capital employed = $1,196,000/1,549,990 = 0.77: 1$

(b)

- Profitability

The operating print margin of RDA in 2020 was not good as compared to 2019/In 2020, it dropped by 6% (48% -42%) and the gross profit margin had also dropped by 11%. This could be as a result of reduced income from tourist activities in 2020.

- Liquidity ratios

The current ratio for 2020 was 3:1 as compared to 2.7:1 in 2019. The quick ratio was 2.1 in 2020 as compared to 2.4 in 2019.if this reduction in liquidity worsened, RDA will face challenges in meeting operational costs as well as its statutory obligations.This reduction in current ratio could have been caused by reduced activities during the year.

Conclusion

The performance of RDA in 2020 has not been impressive as compared to 2019.The outbreak of Covid-19 had restricted movement of tourists around the globe which impacted negatively on tourist arrivals. Therefore the touts sector, which included RDA, was not negatively affected as well

(c) **Five performance measurement weaknesses**

- i. Economic and demographic factors are not usually reported regularly
- ii. There are very little comparisons between what each country is applying as opposed to IAS /IFRS that are used for private sector entities
- iii. The impact and measurements of policies that are implemented by the Government cannot be seen through the financial statements
- iv. The development and the use of data on the outcome of efforts spent on service provisions and accomplishments are not easily visible from the financial statements
- v. The performance measures that are used in the preparation of financial statements are not openly comprehensive. Interval that exist between reporting times varies from organization to organisation.

(d) The benefits of measuring performance using a balance score card in a public sector entity are as follows:

- (i) RDA will be able to measure its performance against the demands of the passengers and cargo transporters
- (ii) RDA will use the balance score card to measure its performance against the needs of shareholders by using financial ratios.
- (iii) RDA will be able to use a balance score card by aligning its mission, vision and strategy and aligning with strategic objectives.
- (iv) RDA will be able to view its own organizational performance through its lenses of quality and efficiency related to its key services such as passenger and cargo transportation.
- (v) RDA will be able to evaluate its performance through the lenses of human capital, infrastructure, technology, culture and other capacities that are key to breakthrough.

SOLUTION FIVE

- (a) Discuss the governance issues regarding financial reporting in government X and reforms the government should embark on to improve financial reporting of revenues.

Country X has to ensure that financial reports are reliable and transparent. It is important that Country X gets it right because financial reporting impacts on:

- Aggregate financial management – fiscal sustainability, resource mobilization and allocation
- Operational management – performance, value-for money and budget management
- Governance – transparency and accountability
- Fiduciary risk management – controls, compliance and oversight

The Government should embark on the following reforms:

- Developing accounting standards, reporting systems and financial procedures.
- Improving government auditing systems and standards.
- Developing human resource management, organization and systems development.
- Provision of professional-level training and strengthening professional and specialist skills.
- Development of management information systems to support information technology requirements.

- (b) Identify the risks associated with accounting of revenue of country Z and how these risks can be mitigated.

Risks Associated with Accounting of Revenue

- Management override of entity controls over revenue recognition resulting in misstatement of revenue.
- Premature revenue recognition.
- Recording fictitious revenue
- Non Reconciliation of Revenue on a daily basis
- Handling of physical cash

Mitigating the Risks Associated with Accounting of Revenue

- Automating Revenue Collection Processes
- Policies and Processes for accounting for revenue should be integrated
- Reconciliation and Financial Analysis process should be executed weekly
- Capacity Building of Finance Staff
- Monitoring system of performance against objectives
- Performance measures to continually monitor the effectiveness and efficiency of the changes effected.

END OF SOLUTIONS